TELEFONICA S A
Form 20-F
April 18, 2005

As filed with the Securities and Exchange Commission on April 15, 2005.

SECURITIES AND EXCHANGE COMMISSION

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2004

Commission file number: 1-9531

TELEFONICA, S.A.
(Exact name of registrant as specified in its charter)

KINGDOM OF SPAIN
(Jurisdiction of incorporation or organization)

Gran Via, 28, 28013 Madrid, Spain
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Ordinary Shares, nominal value (euro)1.00 per share	New York Stock Exchange
American Depositary Shares, each representing three Ordinary Shares	New York Stock Exchange

* Not for trading, but only in connection with the registration of American Depositary Shares, pursuant to the requirements of the New York Stock Exchange.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

The number of issued shares of each class of stock of
Telefonica, S.A. at December 31, 2004 was:

Ordinary Shares, nominal value (euro)1.00 per share: 4,955,891,361

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 [ ] Item 18 [X}

==

TABLE OF CONTENTS

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report contains statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the U.S. Securities Exchange Act of 1934, as amended, and the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The forward-looking statements in this Annual Report can be identified, in some instances, by the use of words such as "expects", "aim", "hope", "anticipates", "intends", "believes" and similar language or the negative thereof or by the forward-looking nature of discussions of strategy, plans or intentions. These statements appear in a number of places in this Annual Report including, without limitation, certain statements made in "Item 3--Key Information--Risk Factors", "Item 4--Information on the Company" and "Item 5--Operating and Financial Review and Prospects" and include statements regarding our intent, belief or current expectations with respect to, among other things:

- the effect on our results of operations of competition in the Spanish telecommunications market and our other principal markets;
- trends affecting our financial condition or results of operations;
- acquisitions or investments which we may make in the future;
- our capital expenditures plan;

- supervision and regulation of the Spanish telecommunications sector and in other countries where we have significant operations;
- our strategic partnerships;
- the potential for growth and competition in current and anticipated areas of our business; and
- the adoption of International Financial Reporting Standards in preparing our Consolidated Financial Statements beginning January 1, 2005.

Such forward-looking statements are not guarantees of future performance and involve numerous risks and uncertainties, and actual results may differ materially from those anticipated in the forward-looking statements as a result of various factors. The risks and uncertainties involved in our businesses that could affect the matters referred to in such forward-looking statements include but are not limited to:

- changes in general economic, business, or political conditions in the domestic or international markets in which we operate or have material investments that may affect demand for our services;
- changes in currency exchange rates and interest rates;
- the impact of current, pending or future legislation and regulation in Spain, other countries where we operate and the European Union;
- new pronouncements from the International Accounting Standards Board regarding International Financial Reporting Standards;
- the actions of existing and potential competitors in each of our markets;
- the outcome of pending litigation; and
- the potential effects of technological changes.

Some of these and other important factors that could cause such differences are discussed in more detail under "Item 3--Key Information--Risk Factors", "Item 4--Information on the Company", "Item 5--Operating and Financial Review and Prospects" and "Item 11--Quantitative and Qualitative Disclosures About Market Risk".

Readers are cautioned not to place undue reliance on those forward-looking statements, which speak only as of the date of this Annual Report. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date of this Annual

Report including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

CERTAIN TERMS AND CONVENTIONS

Our ordinary shares, nominal value one euro each, are currently listed on each of the Madrid, Barcelona, Bilbao and Valencia stock exchanges under the symbol "TEF". They are also listed on various foreign exchanges such as the London, Frankfurt, Paris, Buenos Aires, Lima, Sao Paulo and Tokyo stock exchanges and are quoted through the Automated Quotation System of the Spanish stock exchanges and through the SEAQ International System of the London Stock Exchange. American Depositary Shares ("ADSs"), each representing the right to receive three ordinary shares, are listed on the New York Stock Exchange under the symbol "TEF" and on the Lima Stock Exchange. ADSs are evidenced by American Depositary Receipts ("ADRs") issued under a Deposit Agreement with Citibank, N.A., as Depositary. Brazilian Depositary Shares ("BDSs"), each representing the right to receive one ordinary share, are listed on the Sao Paulo Stock Exchange. BDSs are evidenced by Brazilian Depositary Receipts ("BDRs") issued under a Deposit Agreement with Banco Bradesco, S.A., as Depositary.

As used herein:

- "Telefonica", "Telefonica Group" and terms such as "we", "us" and "our" mean Telefonica, S.A. and its consolidated subsidiaries unless the context otherwise requires;

- "Telefonica de Espana" means Telefonica de Espana, S.A., our subsidiary that conducts our fixed line telecommunications services business in Spain, and its consolidated subsidiaries;

- "Telefonica Moviles" means Telefonica Moviles, S.A., our subsidiary that conducts our worldwide wireless communications services business, and its consolidated subsidiaries;

- "Telefonica de Contenidos" (formerly "Admira") means Telefonica de Contenidos, S.A., our subsidiary that conducts our worldwide audiovisual content and media business, and its consolidated subsidiaries;

- "Telefonica Latinoamerica" means Telefonica Internacional, S.A., our subsidiary that conducts our fixed line telecommunications business in Latin America, and its consolidated subsidiaries;

- "Terra Networks" (formerly "Terra Lycos") and the "Terra Group" mean Terra Networks, S.A., our subsidiary that conducts our worldwide Internet-related business, and its consolidated subsidiaries.

PRESENTATION OF CERTAIN FINANCIAL INFORMATION

In this Annual Report, references to "dollars" or "$" are to United States dollars and references to "euro" or "(euro)" are to the single currency of the participating member states in the Third Stage of the European Economic and Monetary Union pursuant to the treaty establishing the European Community, as amended from time to time.

PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

A. DIRECTORS AND SENIOR MANAGEMENT

Not applicable.

B. ADVISORS

Not applicable.

C. AUDITORS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

A. SELECTED FINANCIAL DATA

The following table presents selected consolidated financial data of Telefonica, S.A. You should read this table in conjunction with "Item 5--Operating and Financial Review and Prospects" and the Consolidated Financial Statements included elsewhere in this Annual Report. The consolidated income statement data for each of the three years in the period ended December 31, 2004 and the consolidated balance sheet data as of December 31, 2004 and 2003 set forth below are derived from, and are qualified in their entirety by reference to, the Consolidated Financial Statements and notes thereto included in this Annual Report. The consolidated income statement data for each of the two years in the period ended December 31, 2001 and the consolidated balance sheet data as of December 31, 2002, 2001 and 2000 set forth below are derived from Telefonica, S.A.'s Consolidated Financial Statements, which are not included herein. Our Consolidated Financial Statements have been prepared in accordance with Spanish GAAP, which differ in certain respects from U.S. GAAP. Please refer to note 25 to our Consolidated Financial Statements for a discussion of these differences.

The basis of presentation and principles of consolidation are described in detail in note 2 to our Consolidated Financial Statements.

	At and for the year ended		
	2000	2001	2002
	(in millions of euro, except per sh		
INCOME STATEMENT DATA			
Amounts in accordance with Spanish GAAP:			
Revenues from operations..........................	28,485.5	31,052.6	28,411.3
Other operating revenues(1).......................	266.7	254.7	297.6
Internal expenditures capitalized.................	899.1	730.4	496.7
Increase (decrease) in inventories (net)...........	112.3	(103.9)	(18.1)
Total revenues....................................	29,763.6	31,933.8	29,187.5
Goods purchased...................................	(6,045.2)	(7,111.9)	(6,953.6)
External services and local taxes.................	(5,786.1)	(5,534.3)	(4,976.7)
Personnel expenses................................	(5,111.7)	(5,390.3)	(4,793.8)
Provision for depreciation and amortization........	(6,960.8)	(7,374.0)	(6,692.4)
Trade provisions..................................	(761.1)	(1,023.8)	(645.6)
Other operating expenses..........................	(140.7)	(69.3)	(93.7)
Total operating costs before financial expenses and goodwill amortization.....................	(24,805.6)	(26,503.6)	(24,155.7)

5

	At and for the year ended		
	2000	2001	2002
	(in millions of euro, except per sh		
Operating profit.................................	4,958.0	5,430.2	5,031.8
Amortization of goodwill and reversal of negative goodwill...	(500.6)	(841.6)	(665.4)
Financial income (expense), net...................	(1,611.8)	(1,608.4)	(1,589.3)
Exchange gains (losses), net......................	(248.5)	(782.7)	(632.3)
Income (losses) from associated companies..........	(161.4)	(376.5)	(527.9)
Profit from ordinary activities...................	2,435.7	1,821.1	1,616.8
Extraordinary revenues............................	4,302.3	1,167.1	474.6
Losses on fixed assets............................	(239.9)	(233.0)	(9,614.6)
Extraordinary expenses............................	(3,630.5)	(721.3)	(7,078.0)
Income (loss) before tax and minority interest.....	2,867.6	2,033.9	(14,601.1)
Corporate income tax..............................	(242.2)	(198.1)	3,228.7
Minority interest.................................	(120.6)	271.0	5,795.6
Net income..	2,504.8	2,106.8	(5,576.8)
Net income (loss) per share(2)....................	0.59	0.43	(1.13)
Weighted average number of shares (thousands)......	4,269,839	4,916,564	4,948,037
Net income (loss) per ADS(2)(3)...................	1.76	1.28	(3.38)
Weighted average number of ADSs (thousands)........	1,423,280	1,638,855	1,649,346
Amounts in accordance with U.S. GAAP(4):			
Total revenues....................................	27,326.1	31,577.2	28,912.6
Income (loss) before tax..........................	1,549.7	(6,713.6)	(8,693.5)
Corporate income tax..............................	295.0	(477.8)	3,387.5
Net income (loss).................................	1,844.6	(7,191.3)	(5,206.1)
Net income (loss) per share(2)(5).................	0.43	(1.46)	(1.05)
Net income (loss) per ADS(2)(3)(5)................	1.30	(4.39)	(3.16)
BALANCE SHEET DATA			
Amounts in accordance with Spanish GAAP:			
Cash..	765.6	621.9	517.5
Property plant and equipment......................	38,721.9	36,606.1	27,099.7
Total assets......................................	92,377.3	86,422.6	68,041.3
Total long term debt..............................	24,692.9	27,692.4	21,726.1
Total shareholders' equity........................	25,930.5	25,861.6	16,996.0
Amounts in accordance with U.S. GAAP(4):			
Cash..	678.7	619.6	517.5
Property, plant and equipment.....................	38,277.9	35,563.2	25,282.7
Total assets......................................	107,884.6	90,930.9	67,211.0
Total long term debt..............................	20,618.5	27,771.2	21,778.0
Total shareholders' equity........................	44,225.3	31,659.6	16,973.7
CASH FLOW DATA			
Amounts in accordance with Spanish GAAP:			
Net cash provided by operating activities..........	8,996.9	8,828.8	8,814.6
Net cash used in (provided by) investing activities	(17,719.5)	(9,895.4)	(5,780.2)

Net cash used in (received from) financing activities(6)................................	14,320.9	(1,321.1)	(2,101.1)
Amounts in accordance with U.S. GAAP:			
Net cash provided by operating activities..........	16,370.1	8,995.8	9,019.5
Net cash used in (provided by) investing activities	(25,572.6)	(9,528.5)	(5,585.4)
Net cash used in (received from) financing activities(6)................................	14,689.4	(1,347.0)	(2,082.0)

----

(1) Includes internal capitalized expenditures on fixed assets and increase in inventories (net).

(2) The per share and per ADS computations for all periods presented have been adjusted to reflect the stock split and stock dividends which occurred during the periods presented.

(3) Each ADS represents the right to receive three ordinary shares. Figures do not include any charges of the Depositary.

(4) U.S. GAAP data for the years ended December 31, 2000, 2001, 2002, and 2003 have been restated retroactively to record our investment in Portugal Telecom, SGPS under the equity method. See Note 25.7 to our Consolidated Financial

Statements included elsewhere herein. The effect of the change on net income in 2003, 2002, 2001 and 2000 was an increase or (decrease) of (euro) 4.2 million,(euro) 8.4 million, ((euro)9.0) million and ((euro)11.4) million, respectively. The effect of the change on Shareholders equity in 2003, 2002, 2001 and 2000 was a decrease of (euro)67.3 million, (euro)15.6 million, (euro)110.2 million and (euro)132.5 million, respectively.

(5) U.S. GAAP earnings per share and per ADS have been computed using the weighted average number of shares outstanding for each period.

(6) Includes net cash outflow for capital expenditures and for investments in affiliates.

Exchange Rate Information

Effective January 1, 1999, the following 11 European Union member states adopted the euro as a common currency: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Portugal and Spain. They also established fixed conversion rates between their respective sovereign currencies and the euro. On January 1, 2001, Greece joined the European Economic and Monetary Union. The exchange rate at which the Spanish peseta has been irrevocably fixed against the euro is Ptas 166.386 = (euro)1.00. On January 1, 2002, the participating member states began issuing new euro-denominated bills and coins for use in cash transactions. As of March 1, 2002, the participating member states have withdrawn the bills and coins denominated in their respective currencies from circulation, and they are no longer legal tender for any transactions. As used in this Annual Report, the term "Noon Buying Rate" refers to the rate of exchange for euros, expressed in U.S. dollars per euro, in the City of New York for cable transfers payable in foreign currencies as certified by the Federal Reserve Bank of New York for customs purposes. The Noon Buying Rate certified by the New York Federal

Reserve Bank for the euro on April 14, 2005 was $1.2819 = (euro)1.00.

The following tables describe, for the periods and dates indicated, information concerning the Noon Buying Rate for the euro. Amounts are expressed in U.S. dollars per (euro)1.00.

	Noon Buyin	
Year ended December 31,	Period end	Average(1)
2000	0.9388	0.9207
2001	0.8901	0.8909
2002	1.0485	0.9495
2003	1.2597	1.1411
2004	1.3538	1.2478

Source: Federal Reserve Bank of New York.

----

(1) The average of the Noon Buying Rates for the euro on the last day of each month during the relevant period.

Month ended
October 31, 2004
November 30, 2004
December 31, 2004
January 31, 2005
February 28, 2005
March 31, 2005
April 30, 2005 (to April 14)

Source: Federal Reserve Bank of New York.

Monetary policy within the member states of the euro zone is set by the European Central Bank. The European Central Bank has set itself the objective of containing inflation and will adjust interest rates in line with this policy without taking account of other economic variables such as the rate of unemployment. It has further declared that it will not set an exchange rate target for the euro.

Our ordinary shares are quoted on the Spanish stock exchanges in euro. Currency fluctuations may affect the dollar equivalent of the euro price of our shares listed on the Spanish stock exchanges and, as a result, the market

7

price of our ADSs, which are listed on the New York Stock Exchange. Currency fluctuations may also affect the dollar amounts received by holders of ADRs on conversion by the Depositary of any cash dividends paid in euro on the underlying shares.

Our consolidated results are affected by fluctuations between the euro and the currencies in which the revenues and expenses of some of our consolidated subsidiaries are denominated (principally the Brazilian real, the Argentine peso, the Chilean peso, the Peruvian nuevo sol, the Mexican dollar and the U.S. dollar). See "Item 11--Quantitative and Qualitative Disclosures About Market Risk".

B. CAPITALIZATION AND INDEBTEDNESS

Not applicable.

C. REASONS FOR THE OFFER AND USE OF PROCEEDS

Not applicable.

D. RISK FACTORS

In addition to the other information contained in this Annual Report, prospective investors should carefully consider the risks described below before making any investment decisions. The risks described below are not the only ones that we face. Additional risks not currently known to us or that we currently deem immaterial may also impair our business and results of operations. Our business, financial condition or results of operations could be materially adversely affected by any of these risks, and investors could lose all or part of their investment.

Risks Related to Our Business

We endeavor to implement our business plans successfully, but factors beyond our control may prevent us from doing so, which could have a material adverse effect on our business.

Our ability to increase our revenues and maintain our position as a leading European and Latin American provider of advanced telecommunications and Internet services will depend in large part on the successful, timely and cost-effective implementation of our business plans, including our plan to operate our various businesses along global business lines.

Factors beyond our control that could affect the implementation and completion of our business plan include:

- difficulties in developing and introducing new technologies;
- declining prices for some of our services;
- the effect of adverse economic trends in our principal markets;
- the effect of foreign exchange fluctuations on our results of operations;
- difficulties in obtaining applicable government, shareholder and other approvals;
- difficulties in entering into key contracts with third parties;
- the effect of increased competition;
- our ability to establish and maintain strategic relationships;
- difficulties in integrating our acquired businesses;

- the effect of future acquisitions on our financial condition and results of operations;

- difficulties in securing the timely performance of independent contractors hired to engineer, design and construct portions of our network;
- the potential lack of attractive investment targets;
- difficulties in attracting and retaining highly skilled and qualified personnel; and
- the effect of unanticipated network interruptions.

A material portion of our foreign operations and investments is located in Latin America, and we are therefore exposed to risks inherent in operating and investing in Latin America.

At December 31, 2004, approximately 41.8% of our assets were located in Latin America. In addition, approximately 37.1% of our revenue from operations for 2004 was derived from our Latin American operations. Our foreign operations and investments in Latin America are subject to various risks, including risks related to the following:

- government regulations and administrative policies may change quickly;
- currencies may be devalued or may depreciate or currency restrictions and other restraints on transfer of funds may be imposed;
- governments may expropriate assets;
- governments may impose burdensome taxes or tariffs;
- political changes may lead to changes in the business environments in which we operate;
- our operations are dependent on concessions and other agreements with existing governments;
- economic downturns, political instability and civil disturbances may negatively affect our operations; and

In addition, revenues from operations of our Latin American subsidiaries, their market value and the dividends and management fees received from them are exposed to material country risk as a result of adverse economic conditions in the region that may adversely affect demand, consumption and exchange rates.

For example, our operations in Argentina were affected by the devaluation of the Argentine peso, high inflation and other adverse macroeconomic conditions in Argentina and related legislative measures adopted by the Argentine Government in 2001 and 2002. During 2003 and 2004 the Argentine economy has stabilized and experienced significant growth. However, the effects of laws adopted during the economic crisis continue to affect the results of operations and financial condition of our operations in Argentina. In addition, the Argentine economic and social situation has quickly deteriorated in the past and may quickly deteriorate in the future and we cannot assure you that the Argentine economy will continue to experience sustained growth. Furthermore, approximately 50% of the bonds issued by the Republic of Argentina remain in default and this may influence measures taken by its government affecting business development in the private sector.

Our fixed line business in Argentina derive a majority of their revenues from regulated tariffs for telecommunication services. Prior to the enactment of the Public Emergency Law on January 7, 2002 in response to the economic crisis, those tariffs were linked to a rate per unit of usage expressed in U.S. dollars, which could also be adjusted semiannually in accordance with variations in the U.S. consumer price index. Under the Public Emergency Law, however, any tariff index clauses or any other index mechanism incorporated in the agreements executed by the Argentine government, including those agreements with telecommunication service providers, are void and not applicable. Any increase in inflation will thus result in a decrease in revenues from our fixed line business in Argentina in real terms, as tariffs are not adjusted for inflation, which could have a material adverse effect on our results of operations and financial conditions. Our fixed line operator Telefonica de Argentina is in the process of renegotiating the tariffs it charges customers for fixed line telephone service with the Argentina

government. No assurance can be given that the outcome of these negotiations will be favorable to Telefonica de Argentina.

The Public Emergency Law also mandated "pesification" by stating that fixed line tariffs must be established in pesos using a Ps.1.00 per U.S.$1.00 exchange rate. Since our fixed line business in Argentina realizes substantially all of its revenues in pesos, any depreciation in the peso against the euro will negatively affect our results of operations since Telefonica de Argentina has not been allowed to alter its tariffs in response to such depreciation. Exchange rates were stable in 2004. However, any future depreciation of the peso against the euro may have an adverse effect on our results of operations.

If applied to telecommunication services as originally drafted, the "Project of Law for Public Services" presently under discusion in the Argentine parliament would create uncertainty regarding certain critical issued faced by our subsidiaries in Argentina such as the status of licenses and concessions granted to the declared public services. The project under discussion also lacks provisions for tariff adjustments, conditions on investments, financial policies of the operators and obligations of universal services. We cannot predict whether this project will be enacted into law or become part of the regulatory framework that governs our operations in Argentina. Similarly, since the project is still under discussion we cannot predict what effects this project, or any other regulations arising from the deliberations on the project, could have on our business, financial condition or results of operations.

The effects of inflation and currency depreciation may require certain of our subsidiaries to undertake a mandatory recapitalization or commence dissolution proceedings.

Under Argentine corporate law, if a corporation presents annual financial statements that report negative shareholders' equity, the corporation is required to commence dissolution proceedings unless its shareholders take action (either by making a capital contribution or authorizing the issuance of additional shares of the corporation) that increases capital stock. As of the date of this Annual Report, certain of our subsidiaries have negative shareholders' equity. Telefonica Holding Argentina and Telefonica Comunicaciones Personales had a negative shareholders' equity of (euro)1,142.8 million at December 31, 2004. As a consequence, in the next annual shareholders' meeting of each such subsidiary, the shareholders must resolve to recapitalize the company to avoid dissolution proceedings. These subsidiaries must recapitalize before December 31, 2005 or be subject to dissolution proceedings instigated by Argentine authorities. If such dissolutions were to occur, our subsidiary Telefonica Comunicaciones Personales could lose its license to provide wireless telecommunications in Argentina.

Our financial condition and results of operations may be adversely affected if we do not effectively manage our exposure to foreign currency exchange and interest rate risk.

We are exposed to various types of market risk in the normal course of our business, including the significant impact of changes in foreign currency exchange rates, as well as the impact of changes in interest rates. We employ risk management strategies to manage this exposure, in part through the use of financial derivatives such as foreign currency forwards, currency swap agreements and interest rate swap agreements. In particular, in order to limit our exposure to Latin American currency exchange rate fluctuations, we use financial derivatives and other instruments. If the financial derivatives market is not sufficiently liquid for our risk management purposes, or if we cannot enter into arrangements of the type and for the amounts necessary to limit our exposure to Latin American currency exchange rate fluctuations, such failure could adversely affect our financial condition and results of operations. Also, our other risk management strategies may not be successful, which could adversely affect our financial condition and results of operations. For a more detailed description of our financial derivatives transactions, see "Item 11--Quantitative and Quantitative Disclosures About Market Risk".

The development of our business could be hindered if we fail to maintain satisfactory working relationships with our partners.

Some of our operations are conducted through joint ventures in which we own a significant, but less than controlling, ownership interest. For example, Brasilcel in Brazil, which is jointly controlled by Telefonica Moviles and Portugal Telecom, is conducted through a joint venture. As a result of our less than controlling interest in these joint ventures, our company does not have absolute control over the operations of the venture.

In addition, in some cases where we own a majority of the venture, we may be subject to provisions in shareholders' agreements restricting our ability to control the venture. The relevant corporate governance provisions vary from venture to venture and often depend upon the size of our investment relative to that of the other investors, our experience as a telecommunications operator in the relevant jurisdiction compared to that of the other investors and the preference or requirement of foreign governments that local owners hold an interest in licensed telecommunications operators. As a result, we must generally obtain the cooperation of our partners in order to implement and expand upon our business strategies and to finance and manage our operations.

The risk of disagreement or deadlock is inherent in jointly controlled entities and there is the risk that decisions against our interests will be made and that we may not realize the expected benefits from our joint ventures, including economies of scale and opportunities to realize potential synergies and cost savings. Our joint venture partners may choose not to continue their partnerships with us.

The costs and difficulties of acquiring and integrating businesses could impede our future growth and adversely affect our competitiveness.

We may enter into acquisition transactions in order to, among other things, provide services in countries in which we do not currently have operations or to enhance our product portfolio in a market where we currently have operations, as we have done in recent years. These acquisitions may expose us to certain risks, including the following:

- the difficulty of assimilating the operations and personnel of the acquired entities;
- the potential disruption to our ongoing business caused by senior management's focus on the acquisition;
- our failure to incorporate successfully licensed or acquired technology into our network and product offerings;
- the failure to maintain uniform standards, controls, procedures and policies; and
- the impairment of relationships with employees as a result of changes in management and ownership.

We cannot assure you that we will be successful in overcoming these risks, and our failure to overcome these risks could have a negative effect on our business, financial condition and results of operations.

Telefonica Moviles' acquisition of BellSouth's wireless operations in Latin America and of Telefonica Movil from CTC Chile may require us to increase our capital resources and financing requirements.

On March 5, 2004, Telefonica Moviles entered into a stock purchase agreement with BellSouth Corporation, or BellSouth, to acquire 100% of BellSouth's interests in its wireless operations in Argentina, Chile, Peru, Venezuela, Colombia, Ecuador, Uruguay, Guatemala, Nicaragua and Panama. The shares of these operators were effectively transferred in 2004 and in January 2005. The total acquisition cost for Telefonica Moviles, adjusted by the net debt of all the companies, amounted to (euro)3,252.5 million (excluding the acquisition cost of the companies acquired in 2005). Furthermore, on May 18, 2004 the Board of Compania de Telecomunicaciones de Chile, or CTC Chile, accepted a binding offer from Telefonica Moviles S.A. for the acquisition of 100% of the shares of Telefonica Movil Chile, S.A., a subsidiary of CTC Chile. The total amount paid by Telefonica Moviles for this acquisition was $1,058 million.

Telefonica Moviles has funded these acquisitions through cash generated by its operations and from loans provided by us. In addition to the financing required for these acquisitions, our capital resource requirements may increase in order to upgrade and integrate the networks of these operators, involving in some cases changes in technology. We may be required to further increase our debt or use a portion our existing cash flow from operations to invest in same of these new acquisitions, which could have a material adverse effect on our revenues and overall results of operations.

We may be adversely affected by unanticipated network interruptions.

Unanticipated network interruptions as a result of system failures whether accidental or otherwise, including due to network, hardware or software failures, that affect the quality of, or cause an interruption in, our service could result in customer dissatisfaction, reduced revenues and traffic, and costly repairs and could harm our reputation. Although we carry business interruption insurance, our insurance policy may not provide coverage in amounts sufficient to compensate us for any losses we incur.

Risks Relating to Our Industry

We face intense competition in most of our markets, which could result in decreases in current and potential customers, revenues and profitability.

We face significant competition in all of the markets in which we operate. Governmental authorities in many of the countries in which we operate continue to grant new licenses and concessions to new market entrants, which results in increased competition in those countries and markets. In addition, technological developments are increasing cross-competition in certain markets, such as between wireless providers and fixed line telephony operators.

Regulatory policies applicable in many of the countries in which we operate generally favor increased competition in most of our market segments, especially in the fixed line and wireless services industries, including by granting new licenses in existing licensed territories in order to permit the entry of new competitors. These regulatory policies are likely to have the effect, over time, of reducing our market share in the relevant markets in which we operate. For example, Spanish telecommunications regulators have attempted to promote competition in fixed line telecommunications services through policies that favor other fixed line telecommunications operators. Regulations introduced in recent years in Spain have allowed other operators to locate their equipment in or adjacent to our exchanges (i.e., local loop unbundling) and have made it easier for our customers to route some or all of their calls over our competitors' networks (i.e., carrier pre-selection). Additional regulatory changes resulting in increased competition could have a further adverse effect on our business, results of operations, financial condition and prospects.

In addition to this, because we hold leading market shares in many of the countries in which we operate, we could face regulatory actions by national or, in Europe, European Union antitrust or competition authorities if it is determined that we have prevented, restricted or distorted competition. These authorities could prohibit us from making further acquisitions or continuing to engage in particular practices or impose fines or other penalties on us, which, if significant, could harm our financial performance and future growth.

For a complete description of the regulatory proceedings we currently face please see "Item 8--Financial Information--Legal Proceedings".

As a result of these policies, we may lose market share in Spain and in other markets where we are the incumbent operator.

In addition, we are subject to the effects of actions by our competitors in the markets where we have operations. Our competitors could:

- offer lower prices, more attractive discount plans or better services and features;

- develop and deploy more rapidly new or improved technologies, services and products;

- bundle offerings of one type of service with others;
- in the case of the wireless industry, subsidize handset procurement; or
- expand and enhance more rapidly their networks.

Furthermore, some of our competitors in certain markets have, and some potential competitors may enjoy, competitive advantages, including the following:

- greater name recognition;
- greater financial, technical, marketing and other resources;
- larger customer bases; and
- well-established relationships with current and potential customers.

To compete effectively with our competitors, we will need to successfully market our services and anticipate and respond to various competitive factors affecting the relevant markets, such as the introduction of new products and services by our competitors, pricing strategies adopted by our competitors, changes in consumer preferences and general economic, political and social conditions. If we are unable to compete effectively with our competitors, it could result in price reductions, lower revenues, under-utilization of our services, reduced operating margins and loss of market share.

We operate in a highly regulated industry and could become subject to more burdensome regulation, which could adversely affect our businesses.

As a multinational telecommunications company, we are subject to different laws and regulations in each of the jurisdictions in which we provide services. Furthermore, the licensing, construction, operation and interconnection arrangements of our communications systems are regulated to varying degrees by national, state, regional, local and supranational authorities, such as the European Union. These authorities could adopt regulations or take other actions that could adversely affect us and our companies, including revocation of any of our licenses or concessions to offer services in a particular market, failure to renew a license or concession, modification of the terms of a license or concession or the granting of new licenses or concessions to competitors. Increased or significant changes in the regulation of the activities of our operating companies, including the regulation of rates that may be charged to customers for services, could have a material adverse effect on our business, financial condition or results of operations.

We operate under license and concession contracts.

Most of our operating companies require licenses or concessions from the governmental authorities of the countries in which they operate. These licenses and concessions specify the types of services permitted to be offered by our operating companies. The continued existence and terms of our licenses and concessions are subject to review by regulatory authorities in each country and to interpretation, modification or termination by these authorities. The terms of these licenses granted to our operating companies and conditions of the license renewal vary from country to country. Although license renewal is not usually guaranteed, most licenses do address the renewal process and terms, which we believe we will be able to satisfy. As licenses approach the end of their terms it is our intention to pursue their renewal as provided by each of the license agreements.

For example, Telefonica del Peru has requested a renewal of the existing contract to provide fixed line telecommunication services, which expires in 2019, for an additional five-year period. In June 2004, the Peruvian government notified Telefonica del Peru of its recommendation not to renew the concession for such additional period. Telefonica del Peru may petition for the additional five-year extension period in December 2008.

Many of these licenses and concessions are revocable for public interest reasons. The rules of some of the regulatory authorities with jurisdiction over our operating companies require us to meet specified network build-out requirements and schedules. In particular, our existing licenses and concessions typically require that we satisfy certain obligations, including minimum specified quality, service and coverage conditions and capital investment. Failure to comply with these obligations could result in the imposition of fines or revocation or forfeiture of the license for the relevant area. In addition, the need to meet scheduled deadlines may require our companies to expend more resources than otherwise budgeted for a particular network build-out.

Our operations in Latin America face different risks, including the possibility of a material modification to the applicable regulatory framework, political uncertainty, economic volatility or social unrest.

The industry in which we operate is subject to rapid technological changes and if we are unable to adapt to such changes our ability to provide competitive services could be materially adversely affected.

The telecommunications industry is in a period of rapid technological change. Our future success depends, in part, on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge and that existing products and technologies will further develop. These new products and technologies may reduce the prices for our services or they may be superior to, and render obsolete, the products and services we offer and the technologies we use, and may consequently reduce the revenues generated by our products and services and require investment in new technology. Our most significant competitors in the future may be new entrants to our markets who are not burdened by an installed base of older equipment. As a result, it may be very expensive for us to upgrade our products and technology, in order to continue to compete effectively with new or existing competitors. Such increased costs could adversely affect our business, financial condition or results of operations.

Our business depends on the upgrading of our existing networks.

We must continue to upgrade our existing wireless and fixed line networks in a timely and satisfactory manner in order to retain and expand our customer base in each of our markets, to enhance our financial performance and to satisfy regulatory requirements. Among other things, we could:

- upgrade the functionality of our networks to permit increased customization of services;

- increase coverage in some of our markets;
- expand and maintain customer service, network management and administrative systems; and
- upgrade older systems and networks to adapt them to new technologies.

Many of these tasks are not entirely under our control. If we fail to successfully execute them, our services and products may be less attractive to new customers and we may lose existing customers to our competitors, which would adversely affect our results of operations.

Failure to generate sufficient cash flow and higher capital expenditure requirements could make us more dependent on external financing. If we are unable to obtain financing, our business may be adversely affected.

The operation, expansion and upgrading of our networks, as well as the marketing and distribution of our services and products, require substantial financing. Moreover, our liquidity and capital resource requirements may increase if we participate in other fixed line or wireless license award processes or make acquisitions. We also have major capital resource requirements relating to, among other things, the development of distribution channels in new countries of operations and the development and implementation of new technologies.

If our ability to generate cash flow were to decrease, we might need to incur a significant amount of debt to support our liquidity and capital resources requirements for the ongoing development and expansion of our business. Our ability to raise capital is also related to our stock price and the liquidity of the equity markets. Adverse trends in these areas could prevent us from raising capital. If we have insufficient internal cash flow or we are unable to borrow the amounts we need at affordable rates or we cannot raise equity, we may be unable to pursue our business plans, which could adversely affect our financial condition and results of operations.

Our business could be adversely affected if our suppliers fail to provide necessary equipment and services on a timely basis.

We depend upon a small number of major suppliers for essential products and services, mainly network infrastructure. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own shortages and business requirements. If these suppliers fail to deliver products and services on a timely

basis, our business and results of operations could be negatively affected. Similarly, interruptions in the supply of telecommunications equipment for our networks could impede network development and expansion, which in some cases could adversely affect our ability to satisfy our license requirements.

The wireless industry may be harmed by reports suggesting that radio frequency emissions cause health problems and interfere with medical devices.

Media and other reports have suggested that radio frequency emissions from wireless handsets and base stations may cause health problems. If consumers harbor health-related concerns, they may be discouraged from using wireless handsets. These concerns could have an adverse effect on the wireless communications industry and, possibly, expose wireless providers, including us, to litigation. Even if the authorized health institutions confirm there is no scientific evidence of adverse health effects, we cannot assure you that further medical research and studies will refute a link between the radio frequency emissions of wireless handsets and base stations and these health concerns. Government authorities could increase regulation of wireless handsets and base stations as a result of these health concerns or wireless companies, including Telefonica Moviles, could be held liable for costs or damages associated with these concerns, which could have an adverse effect on our business. In Spain, for example, Telefonica Moviles was required by law to test and certify the emissions of all its base stations in or close to populated areas. For the year ended 2004, such tests have again confirmed lower emission levels than those required by regulations. If in the future Telefonica Moviles fails to comply fully with these standards, it could be subject to claims or regulatory actions.

Other Risks

We face risks associated with litigation.

We are party to lawsuits and other legal proceedings in the ordinary course of our business. An adverse outcome in, or any settlement of, these or other lawsuits (including any that may be asserted in the future) could result in significant costs to us. In addition, our senior management may be required to devote substantial time to these lawsuits which they could otherwise devote to our business. For a more detailed description of current lawsuits, see "Item 8--Financial Information--Legal Proceedings".

We must adopt new accounting standards in 2005 that will impact our financial reporting.

In 2004 we prepared our financial statements in accordance with Spanish GAAP, and prepared a reconciliation of certain items to U.S. GAAP as required by SEC regulation. Under current European Union law, listed EU companies had to apply from January 1, 2005 the International Financial Reporting Standards (IFRS) adopted by the EU in preparing their consolidated financial statements.

Applying these standards to our Consolidated Financial Statements will imply a change in the presentation of our financial information, since the financial statements will include more components and additional disclosure will be required. Additionally, there will be a change in the valuation of certain items. Regarding the former, at this moment it is not possible to determine the exact impact that this new regulation will entail compared to Spanish GAAP, since new pronouncements from the International Accounting Standards Board (IASB), or pronouncements that are not endorsed by the European Union (EU) prior to the preparation of our December 31, 2005 Consolidated Financial Statements, may have an impact on our financial statements. Regarding the latter, we have performed a preliminary analysis of how the adoption of IFRS will impact our financial condition and results of operations. Based on this analysis, we estimate that the principal adjustments to our total shareholders' equity at December 31, 2004 under IFRS would result in a decline in our shareholders' equity of approximately (euro)3,729 million from (euro)16,225.1 million at that date under Spanish GAAP. A decrease in our shareholders' equity when measured under IFRS at December 31, 2005 could cause certain of our loan covenants to become more restrictive, which could have a material adverse effect on our business, financial condition and results of operations.

For additional information concerning significant differences identified between IFRS and Spanish GAAP, see "Item 5--Operating and Financial Review and Prospects-- Preliminary Guidance on Differences Between IFRS and Spanish GAAP".

ITEM 4. INFORMATION ON THE COMPANY

A. HISTORY AND DEVELOPMENT OF THE COMPANY

Overview

Telefonica, S.A. is a corporation duly organized and existing under the laws of the Kingdom of Spain, incorporated on April 19, 1924. We are:

- a diversified telecommunications group which provides a comprehensive range of services mainly in Spain and Latin America through one of the world's largest and most modern telecommunications networks;
- the leading provider of fixed line voice telephone services, wireless communications services, Internet access services and data transmission services in Spain;
- one of the largest telecommunications operators in Latin America, with operations principally in Brazil, Argentina, Chile, Peru, Mexico, Colombia, Ecuador, Nicaragua, Panama, Uruguay, Venezuela, El Salvador and Guatemala; and
- a leading Spanish multinational corporation.

At December 31, 2004, we had approximately 43.2 million access lines in service and 74.4 million wireless subscribers. In addition, we have 0.4 million pay television subscribers. We had a total of approximately 118.1 million customers at December 31, 2004, more than half of which are in Latin America.

Beginning in 2004, we retroactively changed our calculation of our customer base to count as customers only those which we directly manage. Accordingly, we do not consider the customers of subsidiaries in which we have a financial interest but do not control to be part of our customer base. Therefore, we have retroactively removed all customers of CANTV for 2002 and 2003.

The following table reflects the development of our customer base since 2002.

	At December 31,			% chang
	2002	2003(1)	2004	2003 vs 2004
	(in thousands)			
Lines in service (in thousands)(2)	40,440.4	41,128.4	43,249.5	5.
In Spain	18,705.6	19,100.4	19,835.3	3.
In other countries	21,734.8	22,028.0	23,414.3	6.
Mobile telephony customers (in thousands)(3)	41,376.1	51,848.6	74,442.5	43.
In Spain	18,412.0	19,660.6	18,977.0	(3.
In other countries	22,964.1	32,188.0	55,465.4	72.
Total(4)	82,156.5	93,351.3	118,100.3	26.

----

(1) Beginning on January 1, 2003, we have retroactively introduced a modification in our calculation formula for the lines in service. This criteria will apply to the following equivalencies: PSTN (x1), basic ISDN (x2), primary ISDN (x30), 2/6 digital access for switchboards and Ibercom (x30), ADSL (x1) and unbundled loops (x1). PSTN, or Public Switched Telephone Network, are lines that offer basic telephony services. ISDN, or integrated service digital networks, are lines that allow the integration of voice, data and video services through two 64kbits/s channels. ADSL, or asymmetrical digital subscriber lines, are lines that allow for voice and high speed data transmission. This new criteria introduces a difference in the manner in which we account for ISDN primary access and of the 2/6 access for switchboards and Ibercom, which will be multiplied by the number of access channels (30) instead of the extensions using it.

(2) Includes all the lines in service (traditional and ADSL) of Telefonica de Espana, CTC Chile, Telefonica de Argentina, Telefonica del Peru, Telesp, Telefonica Moviles El Salvador, Telefonica Moviles Guatemala and Telefonica Deutschland.

(3) Includes all the customers of Telefonica Servicios Moviles Espana, MediTelecom, Telefonica Movil Chile, TCP Argentina, Telefonica Moviles Peru, Brasilcel, Telefonica Moviles Guatemala, Telefonica Moviles El Salvador, Telefonica Moviles Mexico and, for 2004 only, the customers of companies acquired from BellSouth in 2004 including those with operations in Venezuela, Guatemala, Nicaragua, Panama, Ecuador, Colombia, Peru and Uruguay but does not include the former BellSouth companies operating in Chile and Argentina as the acquisitions of the BellSouth companies in Chile and Argentina were not closed until 2005.

(4) Includes all pay television subscribers of Cable Magico in Peru, Multiservicio in El Salvador and Imagenio in Spain. After the merger between Via Digital and Sogecable, the TV-platform clients are not included in 2002 (775,000).

During 2004, we implemented certain measures to simplify our business lines by integrating the former Telefonica Empresas business line's operations into the Spanish and Latin American fixed line businesses. Pursuant to this reorganization, the operations of Telefonica Data Espana and Telefonica Soluciones are now conducted by Telefonica de Espana and the operations of Telefonica Data Latinoamerica and Telefonica International Wholesale Services (TIWS) are now conducted by Telefonica Latinoamerica.

As a result of this reorganization, our operations are organized according to five principal lines of business, each of which is headed by an operating subsidiary that is under our direct control and two additional non-strategic business lines. Our five principal lines of business are:

- Spanish fixed line business conducted through Telefonica de Espana;

- Mobile business conducted through Telefonica Moviles;

- Latin American fixed line business conducted through Telefonica Latinoamerica;

- Internet portal business conducted through Terra Networks; and

- Content and media business conducted through Telefonica de Contenidos.

Our other lines of business are:

- Directories business conducted through Telefonica Publicidad e Informacion, S.A.; and

- Call center business in Europe (Spain), Latin America and Northern Africa (Morocco) conducted through Atento N.V.

Our new organization allows us to shift from a product-oriented strategy to a customer-oriented strategy by focusing on our key businesses, divesting unprofitable operations and reorganizing the group in order to facilitate services tailored to our customer's needs rather than offering different products conducted by separate business lines. The final objective of this process is to maximize the quality and breadth of the services we provide to our corporate and professional clients through integrated management of our service catalog, better organizational coordination and through cost and investments synergies.

On February 23, 2005 our Board of Directors approved a merger plan for the acquisition of Terra Networks by Telefonica. The Board of Directors of Terra Networks also approved the merger plan. The merger is subject to approval by our shareholders and the shareholders of Terra Networks. Upon completion of the merger, we intend to integrate the Internet portal business currently conducted through Terra Networks into our other existing business lines.

Telefonica, S.A., the parent company of the Telefonica Group, also operates as a holding company with the following objectives:

- coordinate the group's activities;

- allocate resources efficiently among the group;

- provide managerial guidelines for the group;

- manage the portfolio of businesses;

- provide cohesion within the group; and

- foster synergies among the group's subsidiaries.

The following chart shows the organizational structure of the principal subsidiaries of the Telefonica Group at December 31, 2004, including their jurisdictions of incorporation and our ownership interest.

TELEFONICA S.A.

|

```
      ------------------------------------------------------------------------------------------
       |                    |                      |                    |              |
       |                    |                      |                    |              |
Fixed-Line              Worldwide wireless    Fixed-Line           Worldwide       Worldwide
telecommunications      communications        telecommunications   Internet        audiovisual
services in Spain       services              services in      --| related         content
       |                    |                 Latin America      | services        and media
       |                    |                                    |     |                |
       |                    |                                    |     |                |
TELEFONICA             TELEFONICA MOVILES     TELEFONICA --------| TERRA NETWORKS  TELEFONICA DE
DE ESPANA              (Spain)                INTERNACIONAL      |  (Spain)        CONTENIDOS
(Spain)                92.46%                 (Spain)            |  75.87%         (Spain)
100%                        |                 100%               |  |              100%
|                           |                 |                  |  |               |
|                           |                 |                  |  |               |
|--Telefonica   Telcel      |   Telefonica    |  Telefonica      |  |  Terra        |   Atco
|  Tele-        (Venezuela)-|---Moviles       |--de Argentina    |  |  Networks     |---(Argentina
|  comuni-      92.46%      |   Espana        |  (Argentina)     |  |--Espana       |   100%
|  caciones                 |   (Spain)       |  98.03%          |  |  (Spain)      |
|  Publicas                 |   92.46%        |                  |  |  75.87%       |
|  (Spain)                  |                 |                  |  |               |
|  100%                     |                 |                  |  |               |
|               TEM Colombia|---Brasilcel     |  Compania de     |  |  Terra        |   Sogecable
|               (Colombia)  |   Brasil        |--Telecomuni-     |  |  Networks     |---(5)
|--TELYCO       92.46%      |   (Brazil)      |  caciones        |  |--Brasil       |   (Spain)
|  (Spain)                  |   46.23%        |  de Chile        |  |  (Brazil)     |   23.83%
|  100%                     |                 |  (Chile)         |  |  75.87%       |
|                           |                 |  44,89%          |  |               |
|                           |                 |                  |  |               |
|  Telefonica   Comunicaciones--Telefonica    |                  |  |  Terra        |   Endemol (2
|--Empresas     Moviles del |   Moviles       |  Telefonica      |  |  Networks     |---(Netherlan
|  Espana       Peru        |   Argentina     |--de Peru         |  |--Mexico       |   99.70%
|  (Spain)      (Peru)      |   (Argentina)   |  (Peru)          |  |  (Mexico)     |
|  100%         92.32%      |   90.58%        |  98.19%          |  |  75.86%       |
|                           |                 |                  |  |               |
|                           |                 |                  |  |               |
|  Telefonica   TEM Guatemala---Telefonica    |                  |  |  Terra        |   Hispasat
|--Soluciones    y Cia      |   Moviles       |  Telesp          |  |  Networks     |---(Spain)
   Sectoriales  (Guatemala) |   Peru          |  (Brasil)(1)     |  |--Argentina    |   13.23%
   (Spain)      92.46%      |   (Peru)        |--(Brazil)        |  |  (Argentina)  |
   100%                     |   90.58%           87.49%          |  |  75.87%       |
                            |                                    |  |               |
                Otecel------|---Telefonica                       |  |  Terra Net-   |   Telefonica
                (Ecuador)   |   Moviles          Telefonica      |  |--works        |   Servicios
                92.46%      |   Mexico        |--International---|  |  Guatemala    |---Audiovisua
                            |   (Mexico)      |  Wholesale       |  |  (Guatemala)      (Spain)
                TEM Panama--|---85.06%        |  Services        |  |  75.87%           100%
                (Panama)    |                 |  100%            |  |
                92.06%      |                 |                  |  |
                            |   Telefonica    |                  |  |  Terra Networks
                Abiatar-----|---El Salvador   |  EMERGIA S.A.    |  |--Peru
                (Uruguay)   |   (El Salvador) |--(Uruguay) (4)   |  |  (Peru)
                92.46%      |   84.83%           100%            |  |  75.86%
                            |                                    |  |
                Telefonia   |                                    |  |
                Celular-----|---Telefonica                       |  |  Terra Networks
                Nicaragua       Guatemala        Telefonica      |  |--Chile
                (Nicaragua)     (Guatemala)   |--Empresas  ------|  |  (Chile)
                92.46%          92.46%        |  America            |  75.87%
                                              |  100%               |
                                              |                     |
                                Telefonica    |                     |  Terra Networks
```

```
Movil Chile   |  Telefonica        |--Venezuela
(Chile)       |  Data                 (Venezuela)
92.46%        |--USA                  75.87%
              |   (USA)
              |  100%
              |
              |
              |  Telefonica
              |  Empresas
              |--Brasil (3)
              |   (Brazil)
              |  93.98%
              |
              |
              |  Telefonica
              |  Data
              |--Argentina
              |   (Argentina)
              |  97.92%
              |
              |
              |  Telefonica
              |--Empresas Peru
                  (Peru)
                 97.07%
```

(1) 84.34% representing voting interest
(2) Ownership in Endemol is held directly by Telefonica S.A.
(3) Ownership in Telefonica Data Brasil Holding is held 53.66% by Telefonica DataCorp and 40.32% by Telefonica Internacional S.A.
(4) EMERGIA S.A. is held directly by Telefonica S.A.
(5) Ownership in Sogecable is held 1.60% by Telefonica S.A. and 22.23% by Telefonica de Contenidos.

Our principal executive offices are located at Gran Via, 28, 28013 Madrid, Spain and our telephone number is (34) 91-584-03-06.

Capital Expenditures and Divestitures

We have invested over (euro)11,400.1 million in capital expenditures (consisting of additions to property, plant and equipment, which we refer to as "tangible investments", and additions to intangible assets, which we refer to as "intangible investments") since January 1, 2002. Of this amount, (euro)3,768.1 million was invested in 2004, (euro)3,705.8 million was invested in 2003 and (euro)3,926.2 million was invested in 2002. Losses on property, plant and equipment, which we refer to as "tangible (property and equipment) divestitures", and losses on intangible assets, which we refer to as "intangible asset divestitures", in 2004 were not material. Tangible (property and equipment) and intangible asset divestitures in 2002 were material, principally due to our write-downs of the values of our UMTS licenses and other intangible assets in Germany, Austria and Switzerland, which amounted to (euro)9,526.2 million.

Year Ended December 31, 2004

In 2004, capital expenditures increased by 1.7% from 2003, principally due to expenditures by Telefonica Moviles on network and technology for our mobile businesses in Spain, Brazil, Argentina and Mexico and investments by Telefonica Latinoamerica to further develop our broadband network for our Latin America fixed line business. Our principal capital expenditures in 2004 included:

- intangible investments ((euro)594.1 million)
- tangible investments made by Telefonica Latinoamerica ((euro)680.6 million)
- tangible investments made by Telefonica de Espana ((euro)965.4million)
- tangible investments made by Telefonica Moviles ((euro)1,352.3 million)
- tangible investments made by Atento ((euro)19.9 million)

Year Ended December 31, 2003

In 2003, capital expenditures decreased by 5.6% from 2002, due to a more controlled and conservative investment policy implemented in 2003. Each of our principal business lines has maintained a policy of reduced capital expenditure compared to the prior year, with the exception of our worldwide wireless communications services as a result of the roll-out of GSM networks in Mexico and Chile. Telefonica de Espana and Telefonica Latinoamerica have maintained their policy of focusing on capital expenditures on the development of broadband technology while maintaining the necessary capital expenditures for their traditional business. Our principal investments in 2003 included:

- intangible investments ((euro)806.5 million)
- tangible investments made by Telefonica Latinoamerica ((euro)504.5 million)
- tangible investments made by Telefonica de Espana ((euro)1,084.4million)
- tangible investments made by Telefonica Moviles ((euro)996.9 million)
- tangible investments made by Telefonica Empresas ((euro)100.3 million)
- tangible investments made by Atento ((euro)10.4 million)

Year Ended December 31, 2002

Our principal capital expenditures in 2002 were investments made by Telefonica de Espana in the development of its broadband services. Capital expenditures in 2002 were substantially reduced due to the freeze of the

development of UMTS licenses in Europe and the reduction of investments in Spain and Latin America. In 2002, capital expenditures decreased by 53.4% from 2001 and included:

- intangible investments ((euro)1,106.6 million)
- tangible investments made by Telefonica Latinoamerica ((euro)628.5 million)
- tangible investments made by Telefonica de Espana ((euro)1,262.9 million)
- tangible investments made by Telefonica Moviles ((euro)684.3 million)
- tangible investments made by Telefonica Data ((euro)146.5 million)
- tangible investments made by Atento ((euro)12.7 million)

Financial Investments and Divestitures

Our principal financial investments in 2004 were made by Telefonica Moviles ((euro)3,997.9 million, which included (euro)3,252.5 million from the acquisition of certain BellSouth companies) and Telefonica, S.A. ((euro)530.8 million, which included (euro)475.1 million from additional acquisitions of Portugal Telecom shares. Our principal financial divestitures in 2004 were the sale of Lycos, Inc. and Pearson Plc by Terra Networks S.A. and Telefonica Contenidos, respectively.

Our principal financial investments in 2003 were made by Telefonica, S.A. ((euro)1,528.5 million, which included (euro)1,029.6 million from acceptances to our tender offer for Terra Networks shares), Telefonica de Contenidos ((euro)708.6 million) and Telefonica Moviles ((euro)567.4 million). Our principal financial divestitures were the overall divestiture of our interest in Antena 3 TV and the sale of our interests in Sonda, 3G Telecommunications and Inmarsat by Telefonica Internacional, Telefonica Moviles and Telefonica de Espana, respectively.

Our principal financial investments in 2002 were made by Telefonica Moviles ((euro)712.4 million), Telefonica de Contenidos ((euro)488.6 million) and Telefonica, S.A. ((euro)264.0 million). Our principal financial divestitures in 2002 were divestitures by Telefonica de Contenidos of 100% of its holding in Grupo Uniprex Onda Cero, Cadena Voz de Radiodifusion and Azul Television, and its sale of 4.11% of its interest in Hispasat, S.A. Additional divestitures were made by Telefonica Datacorp, SAU, and Terra Networks of their interests in European Telecom International, GmbH Lycos Korea and Sympatico Lycos.

Public Takeover Offers

On May 28, 2003 we launched a tender offer for 100% of the outstanding shares of Terra Networks that we did not own. The CNMV approved the prospectus for the tender offer on June 19, 2003. The offer price was (euro)5.25 per share, payable in cash. Following the tender offer we held 71.97% of the outstanding shares of Terra Networks. In December 2003 the Board of Directors of Terra Networks approved the acquisition of 4.41% of its shares owned by Citibank N.A. as the agent bank for the stock option plans assumed by Terra Networks following its merger with Lycos, Inc.

On February 23, 2005 the Boards of Directors of Telefonica and Terra Networks approved a merger plan which provides for the merger of the two companies, with the termination through dissolution without liquidation of Terra Networks and the en bloc transmission of all of its assets to Telefonica, which through universal succession will acquire the rights and obligations of Terra Networks. The exchange ratio was set at two ordinary shares of Telefonica for every nine ordinary Terra Networks shares.

On May 25, 2003 Telesp Celular Participaco?s S.A., or TCP, launched a tender offer for the common shares of Centro Oeste Celular Participaco?s S.A., or TCO, not owned by it. The acceptance period finished on November 18, 2003. As a result of the shares tendered, TCP acquired 72.2% of TCO's outstanding common shares for R$16.73 per 1,000 common shares. The total purchase price for the TCO shares acquired was R$538.8 million. At December 31, 2003 TCP held 86.6% of TCO's ordinary shares, representing a 28.29% interest in TCO. TCP also announced the intention to launch an exchange offer for the remaining shares of TCO through which TCP would have become

TCO's sole shareholder. This would have been followed by a merger of TCO into TCP. After the launch of the exchange offer, the Commissao de Valores Mobiliarios (Brazilian Securities Commission), raised questions as to the exchange offer's compliance with Brazilian law. Although TCP and TCO believed that the exchange offer complied with applicable law, TCP and TCO decided to terminate the exchange offer in January 2004.

In August 2004, Brasilcel launched tender offers for part of the outstanding shares of Tele Sudeste Celular Participaco?s S.A., or TSD, Tele Leste Celular Participaco?s S.A., or TBE, Celular CRT Participaco?s S.A., or CRT, and TCO directly and indirectly through its subsidiary TCP, which concluded in October 2004. As a result of the shares it acquired, Brasilcel's stakes in the mentioned companies' share capital have increased to: 90.9% in TSD, 50.6% in TBE, 67.0% in CRT and TCP's stake in TCO increased to 50.6%. The aggregate amount of consideration paid for such shares was approximately R$607 million for Brasilcel and approximately R$902 million for TCP.

For further information, see "Item 4--Business Overview--Telefonica Moviles--Telefonica Moviles Operations--Brazil".

Recent Developments

The principal events since the close of our financial year are set forth below.

- On March 29, 2005, Telefonica S.A. submitted a binding bid to purchase 51.1% of the equity in the Czech telecommunications company Cesky Telecom a.s., from the Czech government in an auction as part of a privatization process. The bid price submitted by Telefonica S.A. is 502 Czech korunas per share, representing a total value of (euro)2,745.9 million for the state's 51.1% of the share capital of Cesky Telecom a.s. The privatization commission formed by the Czech government for the privatization process issued a non-binding recommendation that the government of the Czech Republic accept the bid of Telefonica S.A.. On April 6,2005 the government of the Czech Republic declared officially that the bid of Telefonica, S.A. was the winner of the auction through which the privatization is being conducted. On April 12, 2005 we signed an agreement with the Czech government to purchase its 51% stake in Cesky Telecom a.s. The conclusion of this transaction is subject to several conditions and regulatory approvals and will require Telefonica to launch a mandatory bid to acquire the remaining 48.9% of the total share capital of Czesky Telecom a.s.

- On February 23, 2005 the Boards of Directors of Telefonica and Terra Networks approved a merger plan which provides for the merger of the two companies. See "Item 4--History and Development of the

Company--Public Takeovers."

- On February 16, 2005, the Board of Directors of Telefonica Publicidad e Informacion, S.A., or TPI, agreed to submit to its next general shareholders' meeting a proposal to distribute a dividend of (euro)0.30 per share, which amounts to a 20% increase from dividends paid in 2003. The proposed dividend would result in a dividend payout ratio of 97% for the TPI Group and 99% for TPI. The dividend will be paid after the amortization of treasury stock held by the company (7,212,147 shares, representing 1.96% of the share capital), previously held in connection with hedging arrangements for its stock options plan, which expired in November 2003.

- On January 26, 2005, Telefonica's Board of Directors approved the payment of a dividend to its shareholders of (euro)0.5 per share corresponding to fiscal year 2004 charged against both earnings and reserves. The Board of Directors also announced that it is their intention to maintain the same minimum dividend for fiscal year 2005. The dividends, which must be approved at Telefonica's general shareholders meeting, are to be distributed in two payments. The first interim dividend from 2004 net income of (euro)0.23 per share will be paid on May 13, 2005 and the second dividend from reserves of (euro)0.27 per share will be paid on November 11, 2005.

- In January 2005, Telefonica Moviles, S.A. acquired 100% of Comunicaciones Moviles de Chile, S.A., a wireless communications provider in Chile, for U.S.$532 million and 100% of Compania de Radiocomunicaciones Moviles S.A., a wireless communications provider in Argentina, for U.S.$988 million, which completed the acquisition of BellSouth's Latin American operations.

- In January 2005, a capital increase carried out by TCP was fully subscribed for an amount of approximately R$2.1 billion. The proceeds raised were used in part to finance TCP's increased stake in Tele Centro Oeste (TCO) and the remainder was used to partially repay short-term debt and improve the company's capital structure. As a result of the capital increase, Brasilcel's stake in TCP's share capital increased to 65.7%.

B. BUSINESS OVERVIEW

Spanish Fixed Line Business--Telefonica de Espana

Our Spanish fixed line business is managed by Telefonica de Espana. The principal services offered by Telefonica de Espana are:

- Traditional fixed line telecommunication services, including:
  - PSTN (public switched telephone network) lines;
  - ISDN (integrated services digital network) access, which provides high-speed transmission of voice and data through existing fixed line infrastructure;
  - Public telephone services including street phone booths and other facilities in locations such as airports, train stations, hotels and shops;

- o Local service, domestic long distance, international long distance and fixed-to-mobile communications services;
- o Supplementary services and value added services, such as (i) call waiting, (ii) call forwarding, (iii) three-party service, (iv) voice and text messaging, (v) advanced voicemail services, (vi) information services and (vii) conference-call facilities;
- o Intelligent network services, such as (i) free-phone service, (ii) televoting, (iii) premium rate services, (iv) universal number and (v) virtual private networks;
- o Ibercom: a wide range of advanced corporate communications services, based on the customer's premises-located switches and network facilities; and
- o Leasing and sale of terminal equipments, ranging from basic telephones to PABXs (private automatic branch exchanges).

o Internet and broadband multimedia services, including:

- o Narrowband switched access to Internet, including a range of pay per use and flat rate choices;
- o Telefonica.net: ISP (Internet Service Provider) services;
- o Retail and whole sale broadband access, through ADSL (asymmetrical digital subscriber line) and satellite technologies;
- o Residential-oriented value added services, such as (i) instant messaging, (ii) concerts and videoclips by streaming, (iii) e-learning, (iv) parental control, (v) firewall and (vi) anti-virus;
- o Terminal equipment related to Internet and broadband and multimedia services, including USB modems, wireless routers and personal computers;
- o Business-oriented value added services, such as (i) intranet, (ii) web, (iii) e-commerce, (iv) e-business and e-administration developing, (v) managing services and (vi) sector oriented solutions (e.g. for lawyers or other professionals);

23

- o Wireless access to broadband services, such as Wi-Fi hotspots for business customers or for public access such as hotels and convention centers; and
- o Multimedia, under the trade name Imagenio, providing TV, video on demand, Internet access and a wide range of leisure services.

o Data and business-solutions services, including:

- o Leased lines;
- o VPN (virtual private network) services, including X-25, Frame

Relay, ATM (Asynchronous transfer mode) and IP;

- Hosting and ASP (Application service provider) services, including Web Hosting, Managed Hosting, Content Delivery and application and security services;

- Outsourcing services including network management (CGP's) and desktop services; and

- System integration and professional services.

o Wholesale services for telecommunication operators, including:

- Domestic interconnection services;

- International wholesale services;

- Leased lines for other operators' network deployment;

- Co-location of operators infrastructures; and

- Local loop leasing, under the unbundled local loop regulation framework.

Operations

The following table shows the development of Telefonica de Espana's domestic telecommunications network and growth in usage of that network since 2002:

	At Dec	
	2002	200
Lines in service (in thousands)(1)	18,705.6	19,
Lines (RTB) (in thousands)	15,470.2	15,
Equivalent ISDN basic accesses (in thousands)	1,752.1	1,
Equivalent ISDN primary accesses (in thousands)	413.9	
2/6 digital accesses for switchboards and Ibercom (in thousands)	112.3	
Fully unbundled local loops (in thousands)		
ADSL connections (in thousands)	957.2	1,
Fixed-lines per each 100 inhabitants (total market)(2)	45.3	
Average time for the provision of the PSTN service (days)	10.1	
Lines in service per employee(3)	460.1	
Average consumption per line (minutes/day)	22.1	
Average consumption growth per line (%)	4.7	
Internet users (narrowband) (in thousands)	3,045	2
Growth of outgoing international traffic (%)	(22.4)	
Growth of incoming international traffic (%)	(5.1)	
Basic telephony lines set up (in thousands)	16,347.3	15,
Digitalization degree (%)	89.2	
Coaxial cable (km)	2,468	2

	At Dec	
	2002	200
Lines in service (in thousands)(1)......................................	18,705.6	19,
Lines (RTB) (in thousands)...	15,470.2	15,
Equivalent ISDN basic accesses (in thousands)............................	1,752.1	1,
Optical fiber cable (km)...	60,932	6
Copper cable in interurban links (km)....................................	56,753	5
Copper cable in subscriber networks (4)..................................	69,148	6

----

(1) Beginning on January 1, 2003, we have retroactively introduced a modification in our calculation formula for the lines in service. This criteria will apply to the following equivalencies: PSTN (x1), basic ISDN (x2), primary ISDN (x30), 2/6 digital access for switchboards and Ibercom x30), ADSL (x1) and unbundled loops. PSTN, or Public Switched Telephone Network, are lines that offer basic telephony services. ISDN, or integrated service digital networks, are lines that allow the integration of voice, data and video services through two 64kbits/s channels. ADSL, or asymmetrical digital subscriber lines, are lines that allow for voice and high speed data transmission. This new criteria introduces a difference in the manner in which we account for ISDN primary access and of the 2/6 digital access for switchboards and Ibercom, which will be multiplied by the number of access channels (30) instead of the extensions using it.

(2) Includes homogeneous lines in the total market. We have retroactively changed the calculations for 2002 and 2003 to reflect new population data published by the Spanish National Statistics Institute on August 19, 2004.

(3) For 2003 and 2004, this item includes employees per new perimeter and equivalent lines with unbundled loops.

(4) Thousands of kilometers - par. (Transmission cables in the subscriber networks contain a variable number of conducting filaments, which are insulated from each other and grouped in pairs. Each such pair is called a "par".)

In 2004, voice and Internet traffic decreased as a result of weak market conditions in the Spanish telecommunications sector and loss of market share by Telefonica de Espana due to increased competition. The number of minutes consumed in 2004 decreased by 6.7% to 123,026 million from 131,897 million in 2003. The decrease in minutes consumed in 2004 was mainly due to a 5.9% decrease in minutes per line per day from 19.7 in 2004 compared to 21.8 in 2003 and especially due to a decrease in the average minutes per day per line of traditional and narrow band Internet access services.

Outgoing traffic, which includes voice and Internet calls, accounted for 55.9% of Telefonica de Espana's total traffic in 2004. Outgoing traffic decreased by 14.9% to 68,787 million minutes in 2004 compared to 80,822 million minutes in 2003. During 2004, fixed line to wireless calls decreased 1.3% to 5,777 million minutes in 2004 from 5,855 million minutes in 2003. Calls for Internet access decreased by 22.5% to 21,453 million minutes in 2004 from 27,696 million minutes in 2003. Local calls decreased by 13.7% to 24,929 million minutes in 2004 from 28,882 million minutes in 2003. Provincial calls decreased 10.9% to 6,053 million minutes in 2004 from 6,796 million minutes in 2003. Interprovincial calls decreased 9.5% to 6,242 million minutes in 2004 from 6,894 million minutes in 2003. International outgoing calls increased 4.0% to 1,734 million minutes in 2004 from 1,667 million minutes in 2003. With respect to value added services, the number of voice mails used increased by

3.1% to 11.9 million compared to 11.5 million in 2003. Subscribers to caller identification increased by 10.0% to 7.5 million compared to 6.8 million in 2003. The number of text messages managed through fixed line telephones increased 217% to more than 50 million, of which 33 million were sent from fixed line telephones and the rest were sent from mobile telephones. Incoming traffic, which also includes voice and Internet calls, accounted for 44.1% of Telefonica de Espana's total traffic in 2004. Incoming traffic increased by 6.2% to 54,239 million minutes in 2004, compared to 51,075 million minutes in 2003.

During 2004, Telefonica de Espana continued offering different discount plans targeted to different client profiles. At December 31, 2004 the total number of subscribers for such discount plans was 3,329,797.

Digitalization

With respect to infrastructure, once the digitalization of 94.2% of the local exchanges was achieved, the upgrading of all remaining telephone exchanges was completed and as a result, Telefonica de Espana was able to provide basic digital services, such as itemized billing, to 100% of its customers. The digitalization of Telefonica de Espana's network also enables it to provide a broad range of digital services to satisfy customer demands. Telefonica de Espana's international switching exchanges and domestic and international transmission links are 100% digitalized.

During 2004, Telefonica de Espana continued to make progress in the Internet and broadband businesses. As a result of Telefonica de Espana's commitment to ADSL technology, at December 31, 2004 clients of this service in Spain numbered 2.5 million representing a 50% increase compared to 2003. Of the total number of ADSL clients, 1.6 million were retail ADSL clients, representing a 50.6% increase in retail ADSL clients compared to 2003.

Our variety of ADSL offerings has been well received by clients in 2004. Throughout the year, value added services were in high demand, with 1.2 million services sold. Total "ADSL solutions" amounted to 178,226 of which 169,145 refer to business services. Of these business services, 46,683 are Net LAN (remote access), which allow customers to create their own private virtual network. The ADSL security service has been successful with 347,198 customers at December 31, 2004. In addition, campaigns in order to market other value added services for wireless ADSL (Wi-Fi) are being intensified.

Regulation

Below is a description of the current Spanish telecommunications regulatory framework. This description should be considered in light of certain developments currently underway in the regulatory and competitive environment that will have a material impact on Telefonica de Espana's business and operations in future years.

Overview

Spain is a member state of the European Union. As such, it is required to enact E.U. legislation in its domestic law and to take E.U. legislation into account in applying its domestic law. European Union legislation can take a number of forms. "Regulations" have general application, are binding in their entirety and are directly applicable in all member states. "Directives" are also binding, but national authorities may choose the form and method of implementation. "Recommendations" are not binding, but Spanish courts are obligated to take them into consideration.

In order to strengthen free competition throughout its member states, the E.U. approved a new regulatory framework in 2002. This framework is composed of a series of directives aimed at strengthening competition in the electronic communications industry within the E.U., establishing mandatory minimum service standards for all users (universal service) and users' rights, improving licensing regimes and enhancing telecommunications data protection. These directives required that member states' regulatory frameworks be modified accordingly to comply with the E.U.'s telecommunications regulatory framework within 15 months.

The General Telecommunications Law

In compliance with the obligation to enact this new European legal framework, on November 23, 2003 the Spanish Parliament enacted Law 32/2003 (the "General Telecommunications Law"). This law replaced any other provisions of equal or inferior jurisdiction that were contrary to the provisions set forth in the new law.

The purpose of the General Telecommunications Law is to advance the liberalization of the provision of services and the installation and exploitation of electronic communications networks, and in this regard satisfy the principle of minimal government intervention. Accordingly, the provision of these services and the ability to exploit such networks is granted as a matter of law. In this regard, the law avoids "ex ante" control by regulators as a fundamental principle, removing the current regime of authorizations and licenses and substituting them with "ex post" controls, through market analyses mechanisms necessary to determine the existence of effective competition. Furthermore, in the absence of effective competition, a series of obligations are imposed upon operators with

"significant market power". Within this regulatory framework, the national regulatory authority has a leading role in the implementation of the "ex-post" controls.

Under the General Telecommunications Law, the Spanish government issued Royal Decree 2296/2004 on December 10, 2004 containing new regulations governing the electronic communications and network access markets. The General Telecommunications Law will continue to be implemented through a series of new rules and regulations. Until such new rules and regulations are enacted, existing provisions will remain in force, provided that they are not contrary to the new General Telecommunications Law. It is expected that during 2005 the Spanish government will approve new regulations governing installation of telecommunications services, the use of electronics networks, universal service obligations and other public service obligations.

The State Contract

Since 1991, we have provided telecommunications services through a contract signed with the Spanish government on December 26, 1991. However, under the new regulatory framework described above, all licenses and authorizations for the exploitation of telecommunications networks or for the provision of electronic communications services were extinguished once the new General Telecommunications Law came into force. However, in accordance with the first transitory disposition of the new General Telecommunications Law, the rights and obligations applicable to the individual licenses and general authorizations held by Telefonica de Espana will remain valid. Consequently, Telefonica de Espana must comply with the obligations established before new General Telecommunications Law came into force.

Fixed telephony

Telefonica de Espana is considered a market dominant operator in the provision of fixed line telephony services and leasing of circuits. As a market dominant operator, Telefonica de Espana has certain obligations regarding interconnection and access to public networks and the supply of universal service, as well as other obligations to provide public service.

Mobile telephony

Mobile telephony regulation concentrates on the management and control of the use of the radio-electric public domain, which is exploited by operators through the allocation of frequencies in the radio-electric public domain.

For the provision of mobile telephony services, Telefonica Moviles Espana is considered a market operator and is subject to the fulfillment of certain obligations in the interconnection services market.

Internet

Spanish law has attempted to remove legal uncertainties regarding the Internet as a transmission vehicle for diffusion and exchange of various types of information. Law 34/2002 established the concept of "information society services" which incorporates, among other things, the purchase of goods and services through electronic means and the supply of information through the Internet. Providers of such information services must supply certain basic information to their customers either on their website or through similar means, cease transmission of information if required by government agencies and retain certain information transmitted through their services for at least twelve months.

Service quality

The service quality parameters are established through a ministerial order, dated October 14, 1999, and through the universal service quality ministerial order, dated December 21, 2001. This regulatory framework sets forth the quality standards for telecommunications services, including fixed telephony, mobile telephony and Internet access.

Regulatory authorities

In accordance with General Telecommunications Law 32/2003, the national regulatory authorities in the telecommunications sector are:

- The Spanish Government;
- The senior and directive bodies of the Ministry of Economy on issues of price regulations (Government Deputy Commission for Financial Affairs);
- The Communications State Secretary for the Information Society, a member of the Ministry of Industry, Tourism and Trade;

- The Telecommunications Market Commission; and
- The State radio-communications agency.

Fixed telephony regulation

Telefonica de Espana S.A.U. is a dominant operator in the fixed telephony market and is subject to specific regulation in the different business areas where it operates.

Licenses and Concessions

Under the new General Telecommunications Law, anyone involved in the use of a telecommunications network or in the provision of electronic communication services should notify the Telecommunications Market Commission prior to the commencement of the activity. The Telecommunications Market Commission will register the telecommunications operator in the operator registry.

All licenses and authorizations for the use of telecommunications networks or for the provision of electronic communications services expired after the new General Telecommunications Law came into force. Nevertheless, the right to occupy public and private property should continue according to the relevant regulation.

Interconnection

The General Telecommunications Law requires owners of public telecommunications networks, which includes Telefonica de Espana, to allow competitors to interconnect with their networks and services under non-discriminatory terms and conditions. The General Law on Telecommunications provides that the conditions for interconnection are to be freely agreed among the parties in compliance with certain minimum conditions set by law for interconnection agreements. Where the parties are unable to reach an agreement, the Telecommunications Market Commission may impose the obligation to interconnect upon the conditions it dictates.

Until the regulations governing the telecommunications markets in Spain under the General Telecommunications Law are fully developed and an analysis is completed by the Telecommunications Market Commission the reference interconnection offer (RIO) applies. The RIO is an instrument created by Spanish law under which Telefonica de Espana sets forth the terms the general, technical and financial conditions through which Telefonica de Espana interconnects with other operators. The applicable regulations state that interconnection prices charged by Telefonica de Espana in its RIO must be based on cost rather than profit.

Telefonica de Espana's current RIO was approved the Telecommunications Market Commission on July 10, 2003 and is revised annually as permitted by law. On March 31, 2004 the Telecommunications Market Commission approved a new resolution modifying the RIO with respect to compensation to be paid to Telefonica de Espana for toll-free calls placed from public pay-telephones.

Network access

The General Telecommunications Law sets forth that the Telecommunications Market Commission can require an electronic communications public network operator to allow other operators to access its network. The Telecommunications Market Commission can establish the technical or operating requirements to ensure normal performance of such network. In the same manner as interconnection obligations, an operator may be declared to have significant market power, which imposes obligations regarding information transparency, non-discrimination, separation of accounts, access to specific network resources and price controls.

Under Royal Decree 7/2000 and Royal Decree 3456/2000, the "unbundling of the local loop" was established by setting forth the conditions under which the dominant operators of fixed line public networks must provide shared access to the local loop, with prices set by the Spanish government's Deputy Commission for Financial Affairs.

The Telecommunications Market Commission amended Telefonica de Espana's local loop offer for 2004 on March 31, 2004 by lowering the monthly rental fees charged for access to the local loop, on July 22, 2004 by adapting the local loop offer to new ADSL velocities at the retail level and on July 28, 2004 by modifying the local loop offer for massive migrations between different varieties for access to the local loop.

Selection of operator

Telefonica de Espana, as a designated dominant operator in the supply of connection to public telephone networks from a fixed location, must allow subscribers to place calls with any operator. Customers may pre-select any operator or choose another operator by dialing a three-digit code.

Royal Decree 1651/1998, regulated matters concerning call-to-call operator selection, pre-assignment of operator and safekeeping of numbers by subscribers, irrespective of the operator that provides the service. Royal Decree 7/2000 set forth a calendar for the implementation of pre-assignment in metropolitan calls.

Customers may keep their telephone number when changing access operators as long as they do not change their physical location.

Public service obligations

Universal service. The General Telecommunications Law provides that operators shall be subject rules of public service and other general public obligations in order to guarantee the existence and quality of electronic communications services.

"Universal service" is defined as a set of communication services guaranteed to all end users, irrespective of their geographic whereabouts, of a determined quality and at an affordable price. Such services must guarantee that all citizens can receive a connection to the fixed public network and access to the fixed line telecommunications services available to the public, a free telephone directory, a sufficient number of public telephones, equal access to fixed-telephony services for disabled persons or those with special social needs and functional Internet access.

In addition, Law 34/2002, governing e-commerce and information services over the Internet, provides that all subscribers to the rural telephone cellular access system (TRAC) that requested an Internet connection prior to December 31, 2004 could progressively be provided with a connection that allows them functional connection to the Internet.

The current obligation of Telefonica de Espana to provide universal service is imposed until 2005.

To finance the universal service, the General Telecommunications Law stipulates that the Telecommunications Market Commission must determine whether the net cost to provide universal services implies an unfair burden for the operators required to provide such service. The Telecommunications Market Commission has issued several resolutions relating to Telefonica de Espana's net costs for the provision of the universal service indicating that Telefonica de Espana does not have a right to be compensated by other operators as there is no competitive disadvantage or unfair burden. The Telecommunications Market Commission has not yet created. On March 25, 2004, the Telecommunications Market Commission recognized the existence of a net cost of (euro)110.0 million for Telefonica de Espana as a result of providing universal service, but provided no compensation since the amount was not considered an undue burden.

Competition

The following describes our current main competitors in the principal market segments in which the Telefonica de Espana Group operates. Since 1997, the supply of fixed line telephone services to the public has been open to all

possible competitors, subject to basic licensing requirements as provided for in the General Telecommunications Law, as well as the attainment of legal authorization for installment of such services.

In June 1997, Retevesion was granted a license to provide public fixed line telephone services in Spain, becoming the second operator after Telefonica de Espana to hold such a license. Retevision began operations in January 1998. During 2002, as part of a reorganization process undertaken by the Auna Group, Retevision merged with Aunacable (a cable operator for the Auna Group). The new name of this fixed line telephone company is Auna Telecommunicaciones S.A. The principal shareholders of the Auna Group are Endesa, Santander Central Hispano, Union Fenosa and ING, together with several savings banks.

In May 1998, the Lince consortium, comprised of France Telecom and Editel, S.A. (a consortium which includes Multitel Cable, S.A. and Ferrovial Telecommunicaciones), received the third license for the provision of fixed line telephone services in Spain. Lince commenced operations in December 1998 under the trade name Uni2. In July 2001, France Telecom reached an agreement with its partners in the Lince consortium to acquire their interests in the Lince group. As a result, France Telecom now owns 100% of Uni2, which, together with Al-Pi Telecommunicaciones (a subsidiary of Uni2 that serves corporate clients and professionals in Catalonia), comprises the Uni2 group.

Jazztel p.l.c., a company created in July 1998, received the fourth license for the provision of fixed line telephone services in Spain. Jazztel, p.l.c. is controlled by a consortium comprised of funds managed by Espirito Santo Bank, ING, and Fidelity Investments.

Pricing rules

On October 15, 1999, the Spanish government issued Royal Decree 16/1999 in order to address increasing inflation and promote a higher degree of competition within the telecommunications operators. This Decree established a price regulatory framework for fixed line telephony service and for lines to be leased by Telefonica de Espana based on maximum prices per year.

On December 22, 2004 the Spanish government's Deputy Commission for Financial Affairs (CDGAE) approved a new price regulatory framework for 2005.

This new regulatory framework provides greater flexibility for the introduction of new services and allows different pricing alternatives, which favors competition and innovation.

The most important aspects of the current price regulatory framework are the following:

- Price-caps for the following basic telephony services: local, provincial, interprovincial, international long distance and fixed-to-mobile communications, monthly subscription fees for individual telephone lines and circuits, monthly rental fees for leased circuits and maritime mobile telecommunications service.

- Any increase for monthly rental fees for individual telephone lines could not exceed 2% for 2005.

- Internet access calls, service packages, price plans, discount programs and new services may be offered 21 days after giving notice to the Ministry of Economy and Ministry of Industry, Trade and Tourism, the Telecommunications Market Commission and the Consumer and Users Council prior to initiation of sales.

- All tariffs must be identical throughout Spain.

- The tariff for a call from a fixed line to a mobile phone must be the same regardless of which mobile network receives the fixed line call.

- All other tariffs associated with fixed-telephone service are liberalized, except for the 11818 information services and the public telephone call rates.

The following table displays the variation in prices from the previous price regulatory framework.

Concept	Variation
Local	0.0%
Provincial	(36.4%)
Interprovincial	(45.6%)
International	(35.8%)
Fixed-to-mobile	(32.3%)
Information service	29.4%
Monthly rental fee	42.1%
Subscription fee	(53.4%)

Tariffs for main services

The tariffs for electronic telecommunication services for the three years ended December 31, 2004 (excluding applicable taxes) are provided below. These are the nominal tariffs set by Telefonica de Espana in accordance with the applicable price regulatory framework.

	At December 31,		
	2002	2003	2004

	(in euro)		
Subscription fee			
Individual lines and trunk lines	59.50	59.50	59.50
Integrated Service Digital Network			
Primary access	3,606.07	3,606.07	3,606.07
Basic access	168.28	168.28	168.28
Monthly subscription fee			
Individual telephone line(1)	11.67	12.61	13.17
Integrated Service Digital Network			
- Primary access	342.58	342.58	342.58
- Basic access(2)	22.84	23.78	24.81
Digital circuit 64kbits/s of 4 km	236.24	236.24	236.24

---

(1) After January 22, 2005 the tariff shall be (euro)13.43.

(2) After January 22, 2005 the tariff shall be (euro)25.31.

The following table displays the applicable rates for local, provincial and interprovincial traffic at December 31, 2004:

	Initial connection charge (euro cents)	Exemption (seconds without additional cost; only a flat rate is charged)	Three min (eu
			Peak(2)
Local	6.85	160	7.65
Provincial	8.33	0	19.85
Interprovincial	8.33	0	28.67

---

(1) Call establishment fee included.

(2) For local calls between 8 a.m. and 6 p.m. Monday to Friday. For provincial and interprovincial between 8 a.m. and 8 p.m. Monday to Friday.

(3) Other times and public holidays.

(4) Billing is done per second.

The following table displays the applicable tariffs from fixed-line to mobile calls at December 31, 2004. The first minute is billed in full, and subsequent minutes are billed per second.

Initial connection charge	Tarif
(euro cents)	(euro

Vodafone	6.85	16

	Initial connection charge	Tariff C(3)	Tarif
	(euro cents)	(euro cents	
Telefonica Moviles Espana (Movistar)	6.85	15.70	15
Amena	6.85	19.14	19

----

(1) Tariff A: Monday to Friday from 8 a.m. to 8 p.m.

(2) Tariff B: Monday to Friday from midnight to 8 a.m. and from 8 p.m. to midnight and at all times on weekends and public holidays.

(3) Tariff C: Monday to Friday from 8 a.m. to 8 p.m.

(4) Tariff D: Monday to Friday from 8 p.m. to 10 p.m.

(5) Tariff E: Monday to Friday from midnight to 8 a.m. and from 10 p.m. to midnight. Weekends and public holidays during the entire day.

The following tables show the applicable tariffs for international long-distance calls at December 31, 2004:

Fixed line to fixed line

	Initial connection charge	Flat rate for a three minute call
	(euro cents)	
Western European Countries(1)	11.87	47.87

----

(1) Germany, Austria, Belgium, Denmark, Finland, France, Greece, Ireland, Italy, Luxembourg, Holland, Portugal, United Kingdom, Sweden, Andorra, Monaco, San Marino, Vatican, Switzerland and Liechtenstein.

Fixed-line to mobile calls:

	Initial connection charge	Flat rate for a three minute call
	(euro cents)	
Western European Countries(1)	11.87	116.97

----

(1) Germany, Austria, Belgium, Denmark, Finland, France, Greece, Ireland, Italy, Luxembourg, Holland, Portugal, United Kingdom, Sweden, Andorra, Monaco, San Marino, Vatican, Switzerland and Liechtenstein.

Fixed-line to fixed-line or mobile calls:

	Initial connection charge	Flat three
	(euro cents)	
Iceland and Norway	11.87	
Rest of Europe(1) and part of North Africa(2)	11.87	
Byelorussia, Macedonia and Tunisia	11.87	
United States	11.87	
Canada and part of the Caribbean	11.87	
Bolivia, Colombia and Paraguay	11.87	
Puerto Rico and Dominican Republic	11.87	

	Initial connection charge	Flat three
	(euro cents)	
Rest of Latin America(3)	11.87	
Rest of America	11.87	
Japan and Australia	11.87	
Rest of the World	11.87	from 17

----

(1) Czech Republic, Slovakia, Faeroe Isles, Hungary, Malta, Poland, Albania, Bosnia, Bulgaria, Croatia, Cyprus, Slovenia, Estonia, Latvia, Lithuania, Moldavia, Rumania, Russia, Turkey, Ukraine and Yugoslavia.

(2) Morocco, Libya, Algeria and Western Sahara.

(3) Argentina, Brazil, Costa Rica, Chile, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Peru, Venezuela.

On July 10, 2003 the CDGAE agreement modified the maximum surcharge to be applied to calls made from public telephones to 51.56%, compared to 35% under the previous price regulating framework.

The following table shows the applicable tariffs for switched traffic at December 31, 2004:

	Peak(1)	Off peak(2)
	(euro cents per second)	
Local	0.71	0.42
Metropolitan	0.95	0.57
Single transit	1.05	0.63
Double transit	2.14	1.29

----

(1) Monday to Friday 8 a.m. to 8 p.m.

(2) Weekends and public holidays and Monday to Friday from 8 p.m. to 8 a.m.

The following table shows the applicable tariffs for transit services at

December 31, 2004:

	Peak(1)	Off peak(2)
	(euro cents per second)	
Unicentral	0.15	0.09
National	1.21	0.73
National with local ext	1.60	0.96
Intranodal transit	0.44	0.26

(1) Monday to Friday 8 a.m. to 8 p.m.

(2) Weekends and public holidays and Monday to Friday from 8 p.m. to 8 a.m.

The following table shows the applicable tariffs for interconnection by capacity mode at December 31, 2004:

	Tariff per 64 Kbps circuit(1)	Tariff per Mbps link(2)
	(in euro per month)	
Local	44.20	1,326.11
Metropolitan	62.32	1,869.63
Single transit	73.77	2,213.00
Double transit	106.20	3,186.00

(1) Kilobytes per second.

(2) Megabytes per second.

Prices of local loop

By a resolution dated March 31, 2004 the Telecommunications Market Commission Resolution approved the modification of the tariffs charged by Telefonica de Espana for access to the local loop. The tariffs are the following:

Unbundled access

Pair sign-up fee...
Sign up fee for vacant pair terminated in a building with connection in accordance with RDL 1/1998 (ICT) requiring a single bridge in the main registration................
Sign up fee for vacant pair terminated in a building with connection in accordance with RDL 1/1998 (ICT) requiring a second bridge at the distribution point...............

Shared access

Pair sign-up with co-location..
Pair sign-up with remote co-location..

Indirect access	Without splitter installation	With installa of plain teleph servic splitt
	(in eu	
Indirect access sign-up...	41.83	82.
Change from shared access to indirect access........................	32.89	64.
Change of operator in indirect access...............................	18.43	49.
Simultaneous change of operator and dial-up connection speed in indirect access..	24.41	55.
Disconnection in indirect access....................................	26.66	26.

Monthly rental fee according to modes

Form	Subscription fee
	(in euro)
O...	22.32
B...	25.90
J...	44.18
C...	74.85
N...	84.88
L...	122.64
M...	188.20
P...	249.18

Comparison to other European Operators

The following table displays the tariffs charged by Telefonica de Espana at December 31, 2004 compared to other European operators. Applicable rates during normal business hours have been used.

	Telefonica de Espana	Deustsche Telecom	France Telecom	Tel It
			(in euro)	
Residential monthly rental fee................	13.17	13.50	10.87	
Business monthly rental fee...................	13.17	13.50	13.10	

	During Business Hours			
	Telefonica	Deustsche	France	Tel

	de Espana	Telecom	Telecom	It
			(in euro)	
3 minute calls				
Local	0.08	0.10	0.13	
Long-distance national	0.28	0.31	0.27	

Source: Eurodata, Tarifica and operators.
Interconnection prices

Customer Service

One of our main priorities is to satisfy customer needs by improving the quality of our customer service. We have continued our strategy of segmenting our customers in order to tailor our services to best meet the specific needs of each customer segment. In addition, in order to increase our ability to distribute our products and services we have signed agreements with large department stores to complement our traditional channels of distribution.

The corporate customer service model developed by Telefonica de Espana, which is aimed at achieving the highest degree of efficiency in customer service, features the following:

- A 24-hour personal customer service line for purchasing any type of product and service and handling customer queries;

- The Tiendas Telefonica ("Telefonica stores") where customers can test and buy products marketed by Telefonica;

- Telefonica's "virtual" store, accessible by Internet, which offers the ability to order and purchase online the majority of services and products offered by Telefonica; and

- A sophisticated customer service system for companies, ranging from a telephone help line, which for small companies is based on client portfolio criteria, to the creation of equipment for customer care and multidisciplinary activity sectors sales or individual company sales for larger clients.

In addition, we have continued to develop our product portfolio especially in broadband services. For instance, customers now have the option to finance the acquisition of desktop or portable computers from us as part of our ADSL offerings. We also launched the Imagenio service in 2004. Imagenio is a leisure and communication service, including pay-TV with a broad range of content, from regular television channels to movies, documentary films and music concerts, and featuring Videoclub, an advanced video on demand service. Imagenio includes broadband Internet access, though there is a way for customers to access the service through a digital television connection.

We have also continued to develop products previously introduced including our "combinados" plans that combine access and traffic, allowing each client to optimize its consumption according to calling destination and calling time profile. We have also initiated new access offers including "holiday line" and "young line" in order to better satisfy client needs.

Subsidiaries of Telefonica de Espana

Telefonica Data Espana

Telefonica Data Espana was acquired by Telefonica de Espana on June 30,

2004. Telefonica Data Espana is a company that provides large companies with the following services:

- o Internet and data services including connectivity services that lets the client share information between different company locations (RPVs with X-25 technology, Frame Relay, ATM, IP), Internet access services including information access, applications and Internet publishing and wholesale traffic services and communications outsourcing; and

- o Hosting and applications services based on "Telefonica Internet Centers" including web hosting, managed hosting, content delivery, security services and applications.

Telefonica Soluciones

Telefonica Soluciones was acquired by Telefonica de Espana on June 30, 2004. Telefonica Soluciones is responsible for developing our systems integration, outsourcing and consultancy business inside the Telefonica Group.

Telefonica Telecomunicaciones Publicas ("TTP", formerly known as Cabinas Telefonicas, S.A., "Cabitel")

TTP is a wholly owned subsidiary of Telefonica de Espana, S.A., which focuses on the commercialization, installation, management and maintenance of public telephony as well as the advertising use of any base, outlet or service capable of supporting this activity.

Telefonica Cable

Telefonica Cable provides digital television services through ADSL lines as part of the Imagenio project. Other multimedia services such as digital audio and broadband Internet through both television and PC and video on demand are also included in the Imagenio project but are provided by Telefonica de Espana. In April 2004, Telefonica Cable initiated operations in Madrid, Barcelona and Alicante.

Telyco Group

The Telyco group is comprised of the two following entities.

- o Telyco S.A.U. is a wholly owned subsidiary of Telefonica de Espana, S.A., which sells telecommunications equipment directly through its stores and authorized dealers, as well as through wholesale distribution. Telyco has a commercial network that covers Spain through its direct channels (stores and direct sale) and indirect channels (associated commercial group - Telyco stores and wholesale channel).

- o Telyco Maroc S.A. is a 54% owned subsidiary of Telyco S.A.U. located in Morocco, which supplies mobile telephone products to Medi Telecom.

Telefonica Soluciones Sectoriales

The Telefonica Soluciones Sectoriales Group is comprised of the two following entities:

- Telefonica Soluciones Sectoriales, a wholly owned subsidiary of Telefonica de Espana, S.A., serves as an investment vehicle for information technology and telecommunications projects through shareholdings in related companies. Additionally, Telefonica Soluciones Sectoriales participates on the boards of trustees of five foundations.

- Interdomain, wholly owned subsidiary of Telefonica Soluciones Sectoriales. Interdomain's main activity is related to registering Internet domains at a national and international level.

Mobile Business--Telefonica Moviles

We conduct our worldwide mobile business through Telefonica Moviles, which is a leading provider of wireless communications services in Spain and Latin America in terms of managed customers. Telefonica Moviles estimates, based on information made public by its competitors, local regulatory authorities and data collected from interconnection fees charged and paid, that it is one of the five largest global providers of wireless communication services based upon managed customers at December 31, 2004. Telefonica Moviles offers a broad range of wireless services, including voice services, enhanced calling features, international roaming, wireless internet and data services, wireless intranets and other corporate services.

At December 31, 2004, Telefonica Moviles provided wireless services through its operating companies and joint ventures, to approximately 74.4 million managed customers in territories with a population of approximately

509 million. Managed customers include all customers from companies which we directly control but excludes the customers of companies in which we have a financial interest but do not control. Telefonica Moviles has operations in Spain, Mexico, Peru, El Salvador, Guatemala, Venezuela, Colombia, Panama, Nicaragua, Ecuador, Uruguay, Argentina and Chile and, through its joint ventures with Portugal Telecom, it also provides wireless communication services in Brazil and Morocco. Telefonica Moviles' strategy is to focus on consolidating its market leadership position in Spain and Latin America and on increasing its profitability and cash flow in the medium term by optimizing its investments and operating efficiencies while assessing the potential for growth in new markets reinforcing its market leadership position in Spain and Latin America.

In March 2004, Telefonica Moviles signed an agreement with BellSouth Corporation to acquire its Latin American operations. During October 2004, Telefonica Moviles closed on the acquisition of 8 of the 10 operators (Venezuela, Colombia, Ecuador, Peru, Guatemala, Nicaragua, Uruguay and Panama). The acquisition of the remaining two operators (Argentina and Chile) closed in January 2005.

Telefonica Moviles will continue to analyze the possibility of selective acquisitions and strategic agreements that complement its business. Telefonica Moviles believes that growth in its markets will be driven by (i) increased customer usage of its wireless services, including both voice and data services, (ii) the introduction of new wireless data and Internet services, and (iii) increased penetration rates in its Latin American markets.

Telefonica Moviles also has licenses to provide UMTS services. (Universal Mobile Telephone System, which allows wireless multimedia voice and data transmission speeds of up to 384 kbits/s), in Switzerland through its wholly owned subsidiaries, in Germany through its 57.2% interest in the Group 3G UMTS Holding GmbH consortium, or Group 3G, and in Italy through its 45.59% interest in the IPSE 2000 consortium. Telefonica Moviles has, however, restructured its operations in these countries. See "Item 5 - Operating and Financial Review and Prospects - Operating Results - Overview - Presentation of Financial Information - Other Events Affecting the Comparison of our Results".

The following table provides a summary overview of our operating companies and those companies in which we have non-controlling minority interests at December 31, 2004.

Country	Name of Company	Ownership Interest (1)	Population in service territory
			(in millions)
Spain	Telefonica Moviles de Espana	92.5%	44.0
Morocco	Medi Telecom	29.8%	31
Brazil	Brasilcel(2)	46.2%	131.5
Argentina	Telefonica Comunicaciones Personales	90.5%	38.7
Peru	Telefonica Moviles Peru	90.6%	27.6
Peru	Comunicaciones Moviles del Peru	92.3%	27.6
Mexico	Telefonica Moviles Mexico(3)	85.1%	104.7
El Salvador	Telefonica Moviles El Salvador	84.8%	6.7
Guatemala	Telefonica Centroamerica Guatemala	92.5%	12.7
Guatemala	Telefonica Moviles Guatemala y Compania	92.5%	12.7
Chile	Telefonica Movil Chile(4)	92.5%	15.4
Panama	Telefonica Moviles Panama	92.1%	3.2
Nicaragua	Telefonica Celular Nicaragua	92.5%	5.6
Venezuela	Telcel	92.5%	26.0
Colombia	Telefonica Moviles Colombia	92.5%	45.3
Ecuador	Otocel	92.5%	12.9
Uruguay	Abiatar	92.5%	3.4
Total			508.7

----
(1) Represents the ownership interest of the Telefonica Group.

37

(2) Jointly controlled and managed by Telefonica Moviles and Portugal Telecom. Through its 50% interest in Brasilcel at December 31, 2004, Telefonica Moviles indirectly held 45.45% of Tele Sudeste, 26.42% of Celular CRT, 25.3% of Tele Leste Celular, 32.56% of Telesp Celular and 10.74% of Tele Centro Oeste Celular.

(3) Telefonica Moviles Mexico, S.A. de C.V. holds interests in 100% of Baja Celular Mexicano, 90.0% of Movitel del Noroeste, 100% of Telefonica Celular del Norte, 100% of Celular de Telefonica, S.A. de C.V. and 100% of Pegaso PCS. Through its 92.0% interest in Telefonica Moviles Mexico, S.A. de C.V., as of December 31, 2004, Telefonica Moviles indirectly holds 92.0% of Baja Celular Mexicano, 82.8% of Movitel del Noroeste, 92.0% of Telefonica Celular del Norte, 92.0% of Celular de Telefonica, S.A. de C.V. and 92.0% of Pegaso PCS.

(4) The acquisition of 100% of the shares of Telefonica Movil Chile, the mobile telephone operator in Chile, from CTC Chile closed on July 23, 2004.

Services and Products

Telefonica Moviles' operating companies offer a wide variety of wireless and related services and products to consumer and business customers. Although the services and products available vary from country to country, the following are Telefonica Moviles' principal services and products:

- Wireless Voice Services. Telefonica Moviles' principal service in all of its markets is wireless voice telephony, which has gained increased usage as a result of Telefonica Moviles' increased customer base and increased market penetration rates.

- Value Added Services. Customers in most of Telefonica Moviles' markets have access to a range of enhanced calling features including voice mail, call hold, call waiting, call forwarding and three-way calling.

- Wireless Internet. As part of Telefonica Moviles' strategy to become a leader in the wireless Internet sector, it offers Internet access in an increasing number of areas, mainly through the e-mocion brand, which allows its clients to access a wide range of mobile Internet services through voice, WAP or GPRS CDMA 1XRTT or code division multiple access (a broadband transmission system for wireless networks allowing for speeds of up to 144 kbits/s), or UTMS. GPRS, or general packet radio service, is an evolution of GSM or global standard for mobile, towards 2.5G, allowing wireless voice and higher-speed data transmission. WAP, or wireless application protocol, is a standard protocol allowing for wireless Internet access. Telefonica Moviles' operators in Brazil, Mexico, Argentina, Peru, El Salvador, Guatemala and Morocco have launched Movistar-emocion or services similar in content under other brands, such as "Vivo ao Vivo" in Brazil. Through wireless Internet access, Telefonica Moviles' customers are able to send and receive e-mail, browse web pages, download games, purchase goods and services in m-commerce transactions and use our other data services. Current data services offered include short messaging services, or SMS, and Multimedia Messaging Services, or MMS, which allows customers to send messages with images, photographs, sounds and videoclips. Customers may also receive selected information, such as news, sports scores and stock quotes. Telefonica Moviles also provides wireless connectivity for devices such as laptops and personal digital assistants. Technological advances, which include the development of GPRS and UMTS, facilitate the development of these services by increasing the speed at which data is transmitted and making it possible to expand the offer of services and reduce their cost. Telefonica Moviles Espana launched its "Oficin@ Movistar UMTS"GPRS/UMTS data card, the first third generation service offered in Spain by a mobile operator offering high-speed data transmission of up to 384 kbits/s, to its corporate customers in February 2004 and in May 2004 extended the service to all residential and prepaid customers in conjunction with launching the first UMTS videophone services in the Spanish market.

- Corporate Services. Telefonica Moviles provides business solutions, including wireless infrastructure in offices, private networking and portals for corporate customers that provide flexible on-line billing. Telefonica Moviles Espana offers corporate services through Movistar Corporativo 2000, and other advanced solutions for data, developed for specific sectors.

- Roaming. Telefonica Moviles has roaming agreements that allow its customers to use their handsets when they are outside of their service territories, including on an international basis. In 2002, Telefonica Moviles extended international roaming services to pre-paid customers. It has also implemented intelligent network

technology using the CAMEL standard for its customers in Spain. This allows Telefonica Moviles' customers to use their mobile telephones in European countries where a roaming agreement has been reached as if they were in their home country, for example, by not having to dial customary roaming prefixes. Through the FreeMove alliance with T-Mobile International, Telecom Italia Mobile and Orange, Telefonica Moviles Espana delivers an enhanced, seamless roaming service for customers of the four companies when traveling abroad through its "Virtual Home Environment" and new service propositions to international customers. In Brazil, Mexico and Argentina, Telefonica Moviles' roaming agreements allow its customers to make and receive calls throughout the national territories of these countries.

- Trunking and Paging. In Spain and Guatemala, Telefonica Moviles provides digital wireless services for closed-user groups of clients and paging services.

- M-payment. Through its subsidiary Telefonica Moviles Espana, Telefonica Moviles has an interest of 13.36% in MobiPay Espana, whose other shareholders include Vodafone Espana, Amena and several financial institutions and processing companies. MobiPay Espana is a company incorporated to develop micro-payments. Telefonica Moviles also has a 50.0% interest in MobiPay International, aimed at expediting payments through mobile phones in an international setting. In addition, on February 26, 2003 Telefonica Moviles announced its participation in the new MPSA (Mobile Payment Services Association). The association, which is comprised of Vodafone, Orange, T-Mobile and Telefonica Moviles, will operate under the brand name Simpay. For further information see "--Wireless Internet and Data Initiatives--M-Payment".

- Other Services. Telefonica Moviles also has the technology available to provide other value added wireless services such as location-based services and telematics. Location-based services permit the precise location of the handset to be determined by the wireless network, which will permit users to receive and access information specific to such location. Telefonica Moviles believes that this technology will be widely used in fleet management, logistics and security monitoring. Telematics applications permit the delivery of data to machines, such as automobiles and vending machines.

Telefonica Moviles' Operations

Telefonica Moviles' operations currently are conducted in three distinct geographic areas:

- Spain;

- Morocco; and

o Latin America.

The following is a description of the markets in which Telefonica Moviles operates and includes information on its market share by geographic location. Customer information on the wireless markets in which Telefonica Moviles operates, including its market share, are estimates that Telefonica Moviles has made based on information made public by its competitors or by local regulators in the respective markets. With respect to its operations in Morocco, this information is also based on data collected from interconnection fees charged and paid.

Spain

Telefonica Moviles offers wireless services in Spain through Telefonica Moviles Espana, the leading wireless operator in Spain in terms of total number of customers at December 31, 2004. Telefonica Moviles Espana had approximately 19.0 million customers at December 31, 2004, representing an estimated 48.5% market share.

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Telefonica Moviles' operations in Spain:

	At December 31, (in millions)		
	2002	2003	2004
Total customers (1)	18.4	19.7	19.0
Pre-paid customers (1)	11.9	11.7	9.7
Population in service territory	42	43	44

Source: Telefonica Moviles

----
(1) Telefonica Moviles Espana has determined that it will no longer include 1.3 million inactive prepaid SIM cards in its reported customer base. This adjustment was made from April 1, 2004 and all operating metrics corresponding to 2004 have been calculated taking this adjustment into account.

Telefonica Moviles Espana has offered wireless services in Spain since 1982 with the launch of analog wireless services under the brand MoviLine. Digital wireless services, using GSM 900 MHz technology, were launched in 1995 under the Movistar brand name, which has since become one of the most widely recognized brands in Spain. In 1997, Telefonica Moviles Espana launched the first pre-paid wireless service in Spain under the Movistar Activa brand name, and, in January 1999, Telefonica Moviles Espana launched the GSM 1800 MHz service. In March 2000, having achieved the highest rating in the award process, Telefonica Moviles Espana was awarded a third generation wireless, or UMTS, license covering the Spanish national territory for (euro)131 million. Telefonica Moviles launched its UMTS service on a pre-commercial basis in October 2003 and extended the service during 2004.

Market

With an estimated population of approximately 44 million people, Spain is the fifth largest wireless market in Western Europe with approximately 39.2 million wireless customers at December 31, 2004. This customer base represents a penetration rate of 89.1%. The Spanish market grew 4.4% in 2004.

The Spanish wireless market has shown increasing growth as a result of a decline in wireless handset prices and per minute call rates, and the introduction of pre-paid tariffs. At December 31, 2004, Telefonica Moviles Espana had approximately 19.0 million customers including 0.6 million new customers added during 2004 but excluding 1.3 million inactive prepaid SIM cards after April 2004.

Network and Technology

Telefonica Moviles Espana's licenses and concessions in Spain permit it to operate digital networks and analog networks. Since December 31, 2003 Telefonica Moviles Espana has not operated an analog network, having migrated its analog Moviline subscribers to its digital GSM Movistar services. Telefonica Moviles Espana also holds one of four nationwide licenses for UMTS services in the country, having launched UMTS services commercially in 2004.

Telefonica Moviles Espana's digital network in Spain is based upon the GSM standard, which is one of the most widely used standard systems for wireless communication. The prevalence of the GSM standard, together with Telefonica Moviles Espana's international roaming agreements, enables its Movistar customers to make and receive calls throughout Western Europe and in almost 200 countries worldwide. Telefonica Moviles Espana's GSM-based network provides its customers with access to many of the most advanced wireless handsets and a full panoply of services and products.

Telefonica Moviles Espana's licenses entitle it to 40 MHz of spectrum in the 900 MHz band and 2x24.8 MHz of spectrum in the DCS 1800 MHz band. Under the terms of its UMTS license, Telefonica Moviles Espana is authorized to operate using two paired, or two-way, 15 MHz channels plus one unpaired, or one-way, 5 MHz channel.

In 2002, 2003 and 2004, Telefonica Moviles Espana invested approximately (euro)1,669 million in building out and enhancing its networks in Spain, developing its technological platforms and information systems. At December 31, 2004, Telefonica Moviles Espana's GSM/GPRS digital network in Spain, which consisted of 115 switching centers and more than 16,200 base stations, provided coverage to approximately 99% of the population. The amounts invested in 2002, 2003 and 2004 have been used to enhance the quality of its coverage of high-density areas, to permit more intensive use of its wireless services within buildings in an urban environment, further enhancing the

appeal of wireless communications and to introduce new technologies. In addition, Telefonica Moviles Espana has continued in 2004 to roll-out its UMTS network, complying with its obligations under its UMTS license. At December 31, 2004 Telefonica Moviles Espana's UMTS coverage represented 40% of the population, with 3,800 base stations in approximately one hundred cities.

The Spanish wireless market has been receptive to new wireless services, such as SMS and wireless Internet. Telefonica Moviles Espana has offered GPRS services, with increased speed and efficiencies versus existing GSM networks, since 2001. Multi-media messaging services, or MMS, which allow customers to send and receive messages combining color photographs and images with voice, sound, animations or text, have been offered by Telefonica Moviles Espana since

2002, bringing customers closer to the potential of third generation, or 3G, services while still utilizing existing technology such as GPRS. In all, Telefonica Moviles Espana continues to demonstrate its commitment to be a leader in technological innovation in Spain and to make the most innovative services available to its customers, as can be seen with the development of the following various new services and data applications in 2004:

- GPRS technology continued developing significantly in 2004. Telefonica Moviles Espana estimates that close to 3.8 million of its customers were web browser users with GPRS technology by December 2004, almost 2.4 million more than in December 2003. After the launch of i-mode services in June 2003, in collaboration with NTT DoCoMo, Telefonica Moviles Espana became the first operator in the Spanish market to provide i-mode navigation services. At December 31, 2004 almost 700 thousand of Telefonica Moviles Espana's web browser users used its i-mode service.

- The use of multimedia messaging services (MMS) increased significantly in 2004, with almost 1.5 million users at December 31, 2004 compared to 0.5 million at December 31, 2003. Almost one half of the handsets sold by Telefonica Moviles Espana in 2004 were equipped with MMS technology.

- After the pre-commercial launch of UMTS services in October 2003, on February 13, 2004, Telefonica Moviles Espana launched its "Oficin@ Movistar UMTS" GPRS/UMTS data card, the first third generation service offered in Spain by a mobile operator with high-speed data transmission up to 384 kbits/s, to its corporate customers. This service was extended to all Telefonica Moviles Espana residential and prepaid customers on May 24, 2004, initially in Madrid and Barcelona, and gradually extended to the rest of Spain. On that same date, Telefonica Moviles Espana also launched the first UMTS videophone services in the Spanish market.

- Telefonica Moviles Espana began offering additional services and products in 2004 targeted to the corporate and professional segments such as Movistar desktop, Blackberry(R) Professional Mail, and the TSM 520 handset including the Windows(R) Mobile Smartphone 2003 system.

In general, Telefonica Moviles Espana's strategy is to use a variety of suppliers based on the quality and rates of their services and products. In Spain, Ericsson, Motorola and Nokia have supplied the majority of Telefonica Moviles Espana's GSM and GPRS network. Ericsson supplied the majority of the infrastructures for the first phase of the roll-out of its UMTS Network, and Ericsson and Siemens are supplying the infrastructure for the second phase of the roll-out.

Sales and Marketing

Since Telefonica Moviles Espana began providing wireless services in Spain, its sales and marketing strategy has been to generate increased brand awareness, customer growth and increased revenues. As the Spanish market continues to mature, Telefonica Moviles Espana's focus has been shifting from customer acquisition to management of its customer relationships and continuation of profitable growth through customer loyalty and new products and services.

Telefonica Moviles Espana utilizes all types of marketing channels, including television, radio, exterior signage, telemarketing, direct mail and Internet advertising. Telefonica Moviles Espana also sponsors a leading motorcycle grand prix racing team and cultural and sporting events in order to increase its brand recognition. Its advertising emphasizes its image as the market leader and characteristics such as quality, convenience and reliability, with

specific campaigns based on price or new product offerings. For example, campaigns for its pre-paid service, Movistar Activa, emphasize the simplicity and mobility of the pre-paid service with a focus on the younger segment of the market. For its contract customers, Telefonica Moviles Espana markets Movistar Plus, which emphasizes exclusivity and value with specific offers of new services, and a loyalty program based on points earned.

For purposes of sales and distribution, Telefonica Moviles Espana divides the Spanish market into the consumer market and business market. At December 31, 2004, Telefonica Moviles Espana had approximately 8,500 points of sale for the consumer market. In addition, Telefonica Moviles Espana uses approximately 100 points of sale that are owned by our Group.

In the wireless business sector, Telefonica Moviles Espana uses its distributors to market to small and medium sized enterprises and uses its own corporate sales force to target large business customers. Telefonica Moviles Espana offers a variety of plans, ranging from volume discounts to specifically tailored service contracts.

Telefonica Moviles Espana offers several different pricing options for wireless services. At December 31, 2004, more than 49% of Telefonica Moviles Espana's total customer base are contract customers, and 51% are pre-paid (Movistar Activa).

During 2004, Telefonica Moviles Espana continued encouraging customer migration from its pre-paid plans to its contract plans, in line with the process that started in March 2002, when the contract plans of Telefonica Moviles Espana changed such that they no longer contained a monthly fee, but instead required a minimum usage commitment. At December 31, 2004, prepaid to contract migrations stood at over one million, improving the proportion of contract customers to total customers by 8.5% from December 31, 2003.

The competitive tariffs and quality of services provided by Telefonica Moviles Espana, along with its success in encouraging migration to its contract plans, have led to improvement in the usage and spending pattern of its customers. Total traffic increased to 30.4 million minutes, a 12% increase compared to 2003. In addition, data and content services are becoming increasingly important methods by which wireless customers in Spain communicate. All of this contributed to a significant increase in data revenues which totaled almost (euro)1 billion in 2004 (an increase of 16.1% compared to 2003). The increase in average revenue per user from data services was primarily due to a substantial growth of non-SMS data services, which gave rise to an increase in non-SMS related revenues, out of total data revenues, of 4.5%.

In 2004, Telefonica Moviles Espana experienced growing commercial pressure from competitors as a result of mobile phone number portability offers in the residential market and aggressive pricing in the corporate market. As a result, the amount spent by Telefonica Moviles Espana to acquire and retain customers as a percentage of net sales was 8.6% in 2004, compared to 7.5% in 2003. These cost increases were partially offset by certain cost reduction measures taken by Telefonica Moviles Espana to take full advantage of its economies of scale.

Regulation

Licenses and concessions. Under the new General Telecommunications Law, anyone interested in the exploitation of a telecommunications network or in the provision of electronic communication services should notify the Telecommunications Market Commission prior to the commencement of the activity. The Telecommunications Market Commission will register the telecommunication operator in the Operator Registry.

Under the new regulatory framework, all licenses and authorizations for the exploitation of telecommunications networks or for the provision of electronic communications services were extinguished once the new General Telecommunications Law came into force. However, in accordance with the first transitory disposition of the new General Telecommunications Law, the rights and obligations applicable to the individual licenses and general authorizations held by Telefonica Moviles Espana will remain valid. Consequently, Telefonica Moviles Espana must comply with the obligations established before new General Telecommunications Law came into force.

Telefonica Moviles Espana holds the following concessions for the use of spectrum which terms and conditions are associated with the former licenses now extinguished:

Concession Type (licenses)	Concession Duration	Ending Date	Ex
GSM 900	15 years	February 3, 2010	
DCS--1800	25 years	July 24, 2023	
UMTS	20 years	April 18, 2020	
Paging	20 years	September 24, 2012	
(8) Analogic Trunking	20 years	June, 2014	
(4) Analogic Trunking	20 years	November, 2016	

Interconnection. Because Telefonica Moviles has been classified by the Telecommunications Market Commission as a market dominant operator in the wireless and interconnection markets, Telefonica Moviles Espana must provide cost oriented interconnection rates on a non-discriminatory, transparent and proportional basis based on objective criteria based on costs. The technical and financial conditions under which Telefonica Moviles Espana provides interconnection services to itself or to its subsidiaries must be offered under the same conditions to other operators. This obligation principally relates to the quality of services, delivery schedule and the terms and conditions for the provision of interconnection services. Likewise, Telefonica Moviles Espana must provide relevant information on the technical and functional specifications of the interconnection points to any operator that requests interconnection.

Every year Telefonica Moviles Espana must file separate accounts with the Telecommunications Market Commission for its interconnection related activities. The accounts must include the interconnection services that Telefonica Moviles Espana provided to itself and to its subsidiaries or affiliates as well as the services provided to other operators. Telefonica Moviles Espana must also file every year an externally audited statement of interconnection costs with the Ministry of Economy, the Ministry of Industry, Trade and Tourism and with the Telecommunications Market Commission.

The Telecommunications Market Commission initiated a procedure on September 11, 2003 to determine Telefonica Moviles Espana's termination interconnection prices. On October 7, 2004, the Telecommunications Market Commission established the average maximum price for Telefonica Moviles Espana's interconnection termination service at (euro)0.13 per minute, beginning on October 31, 2004.

Number Safekeeping. Since November 2000, mobile telephony users are able to keep their telephone number whenever they switch mobile operators.

Tariffs. The mobile operators that provide mobile telephone services may generally set the tariffs they charge to their customers. However, the General Telecommunications Law states grants the Government's Deputy Commission for Financial Affairs the authority to set transitory maximum and minimum prices, as well as fixed prices. As of the date of this Annual Report, the Deputy Commission for Financial Affairs has not regulated rates of digital wireless services.

Telefonica Moviles Espana can freely set the rates for the services provided to its customers and must only communicate the rates to the regulatory authorities and to the consumer and customer organizations.

Competition

Telefonica Moviles de Espana currently has two competitors in the Spanish market for wireless communications service: Vodafone Espana, a subsidiary of Vodafone PLC, and Retevision Movil S.A., which operates under the brand name Amena.

In early 2000, the Spanish government awarded four third generation wireless, or UMTS, licenses, which cover the entire country of Spain. Telefonica Moviles Espana was awarded one of these licenses, while the others were awarded to Retevision Movil, Vodafone and the Xfera consortium.

Morocco

Telefonica Moviles provides wireless services in Morocco through Medi Telecom, S.A., in which it holds a 32.18% interest and shares management responsibilities with Portugal Telecom, which also holds a 32.18% interest.

Medi Telecom also has local minority shareholders. Medi Telecom is the second largest wireless operator in Morocco with over 2.7 million customers at December 31, 2004. Medi Telecom commenced offering wireless services in Morocco in March 2000, eight months after it was awarded a GSM license covering the Moroccan national territory.

Telefonica Moviles has entered into a shareholders' agreement with other shareholders of Medi Telecom under which it has the right to appoint the chief executive officer of Medi Telecom. In addition, as of April 2003, the sale or transfer of shares in Medi Telecom triggers a right of first refusal with a priority for Telefonica Moviles and Portugal Telecom. The shareholders' agreement also requires specified majority votes to approve most corporate actions.

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Medi Telecom:

	At December 31, 2002	2003	2004
Total wireless customers (in millions at period end)	1.6	2.1	2.7
Pre-paid customers (in millions at period end)	1.5	1.9	2.6
Population in service territory (in millions at period end)	30	30	31

Source: Telefonica Moviles, except population
Population: Pyramid Research

Licenses

In July 1999, Medi Telecom was awarded a GSM license in the 900 MHz band. This license allows Medi Telecom to provide wireless services in all of Morocco. The license is valid for a period of 15 years from August 2, 1999 and may be renewed for one five-year period, subject to the fulfillment by the operator of certain terms and conditions. In March 2005, however, Medi Telecom reached an agreement with Moroccan regulators to extend their GSM license for an additional ten years (until August 2024). In order to qualify for this additional ten year extension, Medi Telecom must pay to the government 1% of all revenues obtained from providing GSM services beginning in August 2014. In order for this agreement to become effective, an official decree must be issued.

Network and Technology

Medi Telecom's network in Morocco is based upon the GSM standard. Its license entitles it to 50 MHz spectrum in the 900 MHz band. In 2002, 2003 and 2004, Medi Telecom invested a total of approximately (euro)252 million in building out and enhancing its digital network in Morocco. At December 31, 2004, Medi Telecom's digital network in Morocco consisted of 13 switching centers and 1,689 base stations giving coverage to over 96% of the population. Medi Telecom plans to make new investments to increase the coverage of its network.

Competition

Medi Telecom currently competes with Maroc Telecom, the former state monopoly provider of all telecommunications services in Morocco.

Brazil

Telefonica Moviles and Portugal Telecom are 50-50 shareholders in Brasilcel, N.V., or Brasilcel, a joint venture which combines Telefonica Moviles' and Portugal Telecom's wireless businesses in Brazil. This joint venture is the leading wireless operator in Brazil in terms of total number of customers at December 31, 2004. At December 31, 2004 Brasilcel had a total of 26.5 million customers, of which 5.2 million are contract customers. Brasilcel had an estimated average share in its markets of operations of approximately 51% and of 41% in Brazil at December 31, 2004, based on information provided by its competitors and regulatory authorities. All of the operating companies participating in the joint venture have been operating under the brand name "Vivo" since April 2003. The licensed areas of Brasilcel include 19 states in Brazil and its federal capital, with a population of approximately 131.5 million, and representing 85.5% of Brazil's gross domestic product at December 31, 2004.

The following table shows the different states where service is provided by Brasilcel's operators in 2004:

Company	State
Telesp Celular....................	Sao Paulo
Tele Sudeste......................	Rio de Janeiro and Espirito Santo
Global Telecom	Parana and Santa Catarina
CRT Celular.......................	Rio Grande do Sul
Tele Centro Oeste.................	Acre, Goias, Mato Grosso, Mato Grosso do Sul, Rondonia, Tocantins, Distrito Federal, Amazonas, Para, Amapa, Roraima and Maranhao
Tele Leste........................	Bahia and Sergipe

The following table presents, at the dates and for the periods indicated, selected statistical data relating to the operations of Brasilcel:

	At December 31,		
	2002	2003	2004
Total customers (in millions at period end)(1)....................	13.7	20.7	26.5
Pre-paid customers (in millions at period end)(1).................	10.1	15.8	21.4
Population in service territory (in millions at period end)........	97	130	131.5

Source: Telefonica Moviles, except population data
Population: Pyramid Research

----

(1) Total customers and prepaid customers in 2004 reflect the customers of Brasilcel. Total customers and pre-paid customers in 2003 reflect the customers of Brasilcel, including TCO from May 2003. Total customers and pre-paid customers for 2002 reflect the customers of Tele Leste Celular, Tele Sudeste Celular, Telesp Celular and Celular CRT.

Regulation

The wireless telecommunications companies that operate pursuant to licenses and concessions are subject to general obligations set forth by the National Agency for Telecommunications, or Anatel, and to obligations pursuant to each license concerning quality of services, network expansion and modernization.

Licenses and Concessions. On December 4, 2002 ANATEL authorized the contribution to Brasilcel of the wireless assets in Brazil of both Portugal Telecom and Telefonica Moviles and allowed the migration of Brasilcel's operators to a new licensing regime, Personal Mobile Service, or the SMP regime. Accordingly, Brasilcel's operators replaced all their old licenses with new SMP licenses. The old licenses were concessions granted under the Cellular Mobile Service, or the SMC regime. The new SMP licenses include the right to provide cellular services for an unlimited period of time but restrain the right of using the spectrum according to the schedules listed in the old licensing titles (Celular CRT until 2007, Telerj Celular until 2005, Telest Celular until 2008, Telebahia Celular and Telergipe Celular until 2008, TCP until 2008 or 2009 (for the cities of Ribeirao Preto and Guatapara), Global Telecom until 2013, TCO until 2006 (for Brazil's Federal District), Teleacre Celular, Teleron Celular, Telemat Celular and Telems Celular until 2009, Telegoias Celular until 2008 and Norte Brasil Telecom until 2013).

The renewal of all these licenses must be solicited 30 months before its expiration. The companies listed above with licenses expiring within 30 months have already applied for the renewal of their licenses. For the renewal of these licences, the operators will have to make a payment for the use of the spectrum in the amount of 2% of gross revenues. This payment has to be made two years after obtaining the license. This payment is already guaranteed, although for the moment we do not pay for the use of the Spectro.

Interconnection. Resolution 40/98 approved the general interconnection regulations. Interconnection is mandatory for all telecommunications operators. Conflicts arising from the negotiations between operators are

45

resolved through the arbitration by Anatel. Existing regulations state that operators that offer general public services (fixed line services, personal mobile services and specialized mobile services such as trunking and cable TV) must publish the terms and conditions for interconnection with their networks.

Rates. The rates that wireless service providers may charge their customers are regulated by the SMP regime. The SMP regime allows operators to freely negotiate their interconnection rates with other operators. In addition, under the SMP rules, the retail rates charged to customers for fixed-to-mobile calls cannot be less than the sum of the interconnection fees charged on the fixed and mobile call terminations.

Network and Technology

The licenses granted to Brasilcel's operating companies allow operations in CDMA, CDMA 1XRTT, CDMA EVDO and TDMA networks. Brasilcel offers both analog and digital services in the 800 MHz band. TDMA, or time division multiple access, is a digital mobile phone technology that allows several calls to share a single channel without interfering with one another. CDMA 1XRTT or code division multiple access, is a broadband transmission system for wireless networks allowing for speeds of up to 144 kbits/s. Additionally, in 2004 Brasilcel also launched CDMA EVDO, a technology that increases data capabilities allowing speeds of up to 2.4 mbits/s.. We believe Brasilcel has differentiated itself in Brazil by offering more innovative and advanced products and services, in part because of its new networks with the high technological capacity of CDMA 1XRTT and EVDO, which provide a significant competitive advantage for Brasilcel.

Brasilcel's operators that offered services in CDMA Networks (TCP, TeleSudeste Celular, Global Telecom and TeleLeste Celular) have upgraded their networks by the layout of CDMA-1XRTT and EVDO and the companies which offered services based on TDMA Networks (Celular CRT and TCO) are selectively introducing CDMA-1XRTT and EVDO. In 2004, there has been a significant increase of CDMA 1XRTT coverage, reaching 3,700 base stations and covering over 800 municipalities in its areas of operation by year-end.

In 2004, the usage of data services increased, principally due to an increase in SMS and data-enabled handsets. Brasilcel continued to develop its data transmission services business in Brazil through the use of its CDMA 1XRTT and EVDO network.

During the three years ended December 31, 2004 Brasilcel invested approximately (euro)278 million in the development of the networks of its companies in Brazil.

Sales and Marketing

The consolidation of the different brands of Brasilcel into the Vivo brand in 2003 has helped Brasilcel to operate under a unified commercial strategy.

The Brazilian market expanded strongly in 2004, with high commercial activity and increased competitive pressure from all operators. In this context, Vivo has lead customer growth, maintaining its leadership position in the market with a commercial strategy focused on increasing both the customer base and revenues.

Loyalty programs that were established for both contract and prepaid customers in 2003 experienced high growth during 2004. Under these programs, contract customers accrue the right to a handset upgrade based on the revenues that the customers generate, and prepaid customers have access to handsets at a competitive price. Additionally, prepaid to contract migrations were actively promoted in 2004.

Brasilcel is actively managing its distribution channels, which consisted of 7,998 points of sale at the national level in 2004. Additionally, Brasilcel's prepaid customers were provided access to a wide range of points for "recharges". The recharges can also be made by electronic transfers through the commercial banking network.

As of December 31 2004, approximately 20% of Brasilcel's customers were contract clients and the remaining 80% were prepaid customers.

46

Competition

The growth of the Brazilian market has been considerable during the past years and was accompanied by an increase in competition due to the introduction of two new competitors (TIM and Oi) and the expansion of Claro's operations. TIM, Oi and Claro, together with Brasilcel's companies operating under the Vivo brand, represent the principal operators in Brazil.

Peru

Telefonica Moviles has been providing wireless services in Peru through Telefonica Moviles, S.A.C., or Telefonica Moviles Peru, since 2001.

In March 2001, Telefonica, S.A. transferred an approximately 16.5% interest in Telefonica del Peru S.A.A. to Telefonica Moviles in exchange for 65,939,564 ordinary shares of Telefonica Moviles. In accordance with the resolution of the shareholders of Telefonica del Peru to divide the company along business lines, Telefonica del Peru spun off its wireless operations in June 2001 in the form of shares of Telefonica Moviles, S.A.C. and its data operations. Telefonica Moviles agreed with other members of the Telefonica Group who were shareholders of Telefonica del Peru to exchange, following such spin-offs, the shares of such data operations that they received in the spin-off, as well as the shares they held in Telefonica del Peru, for the shares in Telefonica Moviles, S.A.C. that they received in the spin-off. Following the spin-off, share exchanges and additional share purchases, Telefonica Moviles held a 97.97% interest in Telefonica Moviles, S.A.C. and did not hold any interest in such data operations or Telefonica del Peru.

With the acquisition of 99.85% of Comunicaciones Moviles del Peru from BellSouth in October 2004, Telefonica Moviles consolidated its leadership in the Peruvian market with an approximately 69% market share at December 31, 2004. At December 31, 2004 the Telefonica Moviles Peru's and Comunicaciones Moviles del Peru's combined customer base totaled approximately 2.9 million (Telefonica Moviles Peru: 2.1 million customers; Comunicaciones Moviles del Peru: 0.7 million).

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Telefonica Moviles Peru.

	At December 31,		
	2002	2003	2004(1)
Total customers (in millions at period end)	1.2	1.5	2.9
Pre-paid customers (in millions at period end)	1.0	1.2	2.3
Population in service territory (in millions at period end)	26	27	27.6

Source: Telefonica Moviles, except population
Population: Pyramid Research

----

(1) Customer data for 2004 includes the subscribers of Comunicaciones Moviles del Peru, acquired from BellSouth by Telefonica Moviles in October 2004.

Regulation

The Telecommunications Act approved in 1993 (DS 13-93-TCC), and the General Regulations approved in 1994 (DS 6-94-TCC 1994), are the legal framework for the telecommunications sector in Peru.

In 1991, Telefonica del Peru's government-owned predecessor, Compania Peruana de Telefonos S.A., was granted a license for the provision of wireless services in Lima and Callao. Entel Peru S.A. was granted a license in 1992 for the provision of wireless service nationwide. In 1995, Entel Peru was merged into Compania Peruana de Telefonos and the surviving entity changed its name to Telefonica del Peru. Each license is valid for a term of 20 years. They expire on May 24, 2011 and February 1, 2012, respectively. Each license may be renewed for twenty year periods by filing an application at least two years prior to the expiration date. The renewal process requires the license holder to fulfill certain terms and condition.

Telefonica Moviles S.A.C. holds the following licenses:

- Wireless. Licenses to provide wireless services through Sub bands Band A of the 800 MHz band.

- Paging. License to provide paging services in the 450 MHz band

- Long distance. License to provide long distance, international and domestic carrier services, granted in December 2001 for a twenty year period.

After receiving regulatory approval, Telefonica Moviles acquired Comunicaciones Moviles del Peru from BellSouth on October 28, 2004. On January 5, 2005 Telefonica Moviles Peru requested authorization from the Ministry of Transport and Communications to transfer Telefonica Moviles Peru's licenses to Comunicaciones Moviles del Peru and such authorization was granted in April 2005.

Comunicaciones Moviles del Peru holds the following licenses:

- Wireless. License to provide wireless services through Sub band B of the 800 MHz band.

- Long Distance. Licenses to provide long distance international, domestic and local carrier services. The licenses for local carrier services expire between 2016 and 2022. The licenses for domestic and international carrier services expire on February 5, 2019.

- Fixed Line. License to provide local fixed telephony services for Lima and Callao. This license was granted on August 11, 1999 and may be renewed for successive twenty year periods at the request of the holder.

Comunicaciones Moviles del Peru was granted a license for the provision of wireless services in Lima and Callao in 1991 and was granted a license to provide such services in the provinces in 1998. Each license is valid for a term of 20 years. They expire in 2011 and 2018, respectively. Each license may be renewed for twenty year periods by filing an application at least two years prior to the expiration date. The renewal process requires the license holder to fulfill certain terms and condition, such as as compliance with public service obligaions and expansion targets and compliance with antitrust law and interconnection rules as well as OSIPTEL regulations.

Interconnection. Telefonica Moviles Peru is obliged to interconnect with other concession holders who request access to the network. Interconnection rates can be negotiated among wireless operators in Peru. Nevertheless, there is a maximum rate fixed by the Organization for Supervision of Private Investment in Telecommunications (OSPITEL) for termination rates of local calls. This rate is calculated by OSIPTEL based on market information and projections.

Rates. Rates charged by wireless providers to their customers have been subject to a free tariff regime supervised by OSPITEL. Operators freely establish their rates for telephone calls by fixed line users to wireless service, and vice versa. Currently, the two tariffs in force are "the wireless user pays" and "the calling party pays." In June 2004, however, OSPITEL issued a resolution proposing a reduction of rates for calls by fixed line users to wireless users of 60% by December 2005.

Interconnection rates can be negotiated among wireless operators in Peru. Nevertheless, there is a maximum rate fixed by OSPITEL for termination rates of local calls. This rate is calculated by OSPITEL based on market information and projections.

Network and Technology

Telefonica Moviles Peru operates both analog and digital networks. Its digital network is based upon the CDMA/CDMA 1xRTT standard. It has roaming agreements enabling Telefonica Moviles Peru's contract customers to make and receive calls in over 180 countries, including most of the Americas.

Telefonica Moviles Peru's licenses entitle it to 25 MHz of spectrum in the 800 MHz band.

Telefonica Moviles Peru invested approximately (euro)119 million in building out and enhancing its network in 2002, 2003 and 2004. In 2004, the amounts invested have been used to increase the switching capacity of the network and to roll-out the CDMA1xRTT network.

48

At December 31, 2004, Telefonica Moviles Peru's network consisted of the CDMA1xRTT network and the Motorola Analog-Digital Network. The CDMA1xRTT network consisted of 4 switching centers and 273 base stations. The Motorola Analog-Digital Network consisted of 6 dual capacity switching centers, 291 analog base stations and 334 digital base stations.

Telefonica Moviles Peru has been the first wireless operator in Peru to launch CDMA1xRTT technology, which offers its clients a better quality in voice transmission and a higher speed in data transmission. Moreover, this technology permitted the launch of Movistar Multimedia, the platform of access to a wide range of services like video downloads, single- and multi-user games, MMS, chat, ringtones and location services, among others.

Competition

According to Telefonica Moviles' estimates, Telefonica Moviles Peru is the leading operator in the Peruvian market. Telefonica Moviles Peru currently has two competitors: Stet Mobile Holdings which obtained a GSM/PCS license in March 2000 and subsequently launched its services under the TIM brand, and Nextel Peru.

Argentina

Telefonica Comunicaciones Personales S.A. is the third largest wireless operator in Argentina with approximately 3.4 million customers at December 31, 2004, representing an approximately 26% market share.

In January 2001, Telefonica, S.A. transferred to Telefonica Moviles 15.1% of the common stock of Telefonica de Argentina S.A. in exchange for 174,863,364 ordinary shares of Telefonica Moviles. In accordance with the resolution of the shareholders of Telefonica de Argentina S.A. to divide the company along business lines, in November 2001 Telefonica de Argentina S.A. spun-off its wireless operations in the form of shares of Telefonica Comunicaciones Personales S.A. and its data operations. Telefonica Moviles previously had agreed with other members of the Telefonica Group who were shareholders of Telefonica de Argentina S.A. to exchange, following such spin-offs, the shares of such data operations that Telefonica Moviles received in its spin-off, as well as the shares Telefonica Moviles holds in Telefonica de Argentina S.A., for the shares of Telefonica Comunicaciones Personales that they receive in the spin-off. Following the spin-offs and share exchanges, Telefonica Moviles held a 97.93% interest in Telefonica Comunicaciones Personales S.A. and did not hold any interest in the data operations of Telefonica de Argentina S.A.

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Telefonica Comunicaciones Personales.

	At December 31,		
	2002	2003	2004
Total customers (in millions at period end)......................	1.6	1.8	3.4
Pre-paid customers (in millions at period end)....................	1.1	1.2	2.1
Population in service territory (in millions at period end)........	38	38.2	38.7

Source: Telefonica Moviles, except population
Population: Pyramid Research

Telefonica Comunicaciones Personales provides wireless services in each of Argentina's three service regions: Greater Buenos Aires; Southern Argentina; and Northern Argentina. In Greater Buenos Aires, the Telefonica Group commenced offering analog wireless services in 1993 under the Miniphone brand name through a company that it owned jointly with Telecom Argentina, an affiliate of France Telecom and Telecom Italia. In 1994, Miniphone launched digital wireless services in Greater Buenos Aires. In 1999 Telefonica Comunicaciones Personales and Telecom Argentina divided Miniphone's assets, including customers, between them and entered into an agreement which allows Telefonica Comunicaciones Personales and Telecom Personal to continue to operate in Greater Buenos Aires separately. The Telefonica Group launched pre-paid wireless services in Greater Buenos Aires in October 1997.

49

In Southern Argentina, the Telefonica Group launched wireless services through Telefonica Comunicaciones Personales in 1996 under the Unifon brand and launched prepaid wireless services in Southern Argentina in May 1999.

In Northern Argentina, Telefonica Comunicaciones Personales began offering wireless services in May 2000 following receipt of personal communication service, or PCS, licenses covering all three service regions. After launching its services in Northern Argentina, Telefonica Comunicaciones Personales became a nationwide provider of wireless services.

On March 5, 2004 Telefonica Moviles agreed to acquire BellSouth's operating companies in Latin America, including Compania de Radiocomunicaciones Moviles, or CRM, in Argentina. The acquisition of CRM closed on January 7, 2005.

Regulation

The National Telecommunications Law No. 19798 of 1972 (Ley Nacional de Telecomuicaciones) and the specific regulations for each service (including Governmental Decree 264/98) liberalized the telecommunications market in Argentina.

Licenses. Telefonica Comunicaciones Personales S.A.'s licenses for the provision of wireless services include the following:

- PCS licenses and corresponding authorizations for use of spectrum for Northern Argentina, Southern Argentina and Greater Buenos Aires;

- Licenses and corresponding authorizations for use of spectrum for wireless telephone services for Greater Buenos Aires and Southern Argentina; and

- Licenses for trunking, or closed user group, services for the greater Buenos Aires area and other provinces.

In Argentina, regulatory authorities approved the acquisition of CRM subject to the return of certain bandwidth such that the combined operations of Telefonica Comunicaciones Personales and CRM would not hold bandwidth of more than 50 MHz in any one service region.

CRM's licenses for the provision of telecommunication services include the following:

- PCS licenses and corresponding authorizations for use of spectrum for each of Northern Argentina, Southern Argentina and Greater Buenos Aires;

- Licenses and corresponding authorizations for use of spectrum for wireless telephone services for Greater Buenos Aires; and

- Licenses for trunking, or closed user group, services for the Buenos Aires area.

- Fixed Telephony nationwide.

Licenses do not expire, but may be cancelled as the result of an operator's failure to comply with the terms of its license.

An authorization from the Secretariat of Communications allowing for use of spectrum is required before a telecommunications operator may provide wireless services. No wireless service provider may hold a bandwidth of more than 50 MHz in any one service region.

Telefonica Comunicaciones Personales' operating licenses require it to comply with the coverage and service provision undertakings contained in those licenses, but they in turn allow Telefonica Comunicaciones Personales to freely set the tariffs to be charged to its customers, as long as tariffs are applied on a non-discriminatory basis.

Licenses granted to mobile cellular radio-communications service, mobile telephony service and PCS operators do not preclude them from offering any other telecommunication services on a competitive basis although each of these operations are subject to specific regulations.

Interconnection. Interconnection agreements are freely negotiated between operators. If they fail to reach an agreement, each operator may call upon the Secretariat of Communications to determine the terms and conditions of interconnection between the relevant operators.

Operators with "significant market power" (defined as operators with more than 25% of total gross revenues generated by wireless operations) and market-dominant operators (operators with more than 75% of total gross revenues) must provide cost-oriented interconnection prices. Market-dominant operators must provide interconnections with other operators through a "reference interconnection offer."

The "calling party pays" system is in the process of being slowly introduced in Argentina. This system has not yet been introduced for mobile-to-mobile calls or for payphone to mobile calls. Nevertheless, mobile companies have signed private agreements beginning in 2003 that provide for traffic termination fees from the second quarter of 2003. Resolution 623/2002 established the benchmark rate for fixed-to-mobile termination under the calling party pays system. This benchmark takes into account the weighted average revenues and average traffic for all mobile operators.

Rates. Rates charged to customers are not regulated in Argentina.

Network and Technology

Telefonica Comunicaciones Personales operates both analog and digital networks. Its digital network is based upon the TDMA standard and GSM. It has roaming agreements enabling its customers to make and receive calls in more than 170 countries worldwide.

Telefonica Comunicaciones Personales' licenses entitle it to 12.5 MHz of spectrum in the 800 MHz band and 30 MHz of spectrum in the 1900 MHz band in Greater Buenos Aires, 25 MHz of spectrum in the 800 MHz band and 20 MHz of spectrum in the 1900 MHz band in Southern Argentina and 40 MHz of spectrum in the 1900 MHz band in Northern Argentina.

Telefonica Comunicaciones Personales invested a total of approximately (euro)109,4 million in building out and enhancing its digital network in Argentina in the three years ended December 31, 2004. The GSM network was launched in 2004, and by year-end consisted of 1,109 base stations, reaching a population coverage representing approximately 82% of national GDP and providing roaming-in service for international travelers.

At December 31, 2004, Telefonica Comunicaciones Personales' digital network in Argentina consisted of 47 switching centers and 2,099 base stations (including both digital and analog networks) giving coverage over 90% of the population. Telefonica Comunicaciones Personales' network has dual capacity so that the analog network has the same number of switching centers and base stations as the digital network.

Competition

Telefonica Comunicaciones Personales' currently has three competitors in the Argentine market for wireless communications service, each of which provides services on a nationwide basis: Telecom Personal, which is controlled by Telecom Italia through Telecom Argentina, CTI Movil which is controlled by America Movil, and Nextel, owned by NII Holdings Inc.

Mexico

Telefonica Moviles holds 92.0% of Telefonica Moviles Mexico, which is Mexico's second largest wireless operator, with over 5.6 million customers at December 31, 2004. Telefonica Moviles Mexico owns licenses covering all of Mexico.

The companies making up Telefonica Moviles Mexico were acquired by Telefonica Moviles in two steps:

(1) Acquisition of Northern Operators. Telefonica Moviles Mexico acquired its four Northern wireless operators (Bajacel, Movitel, Norcel, and Cedetel) from us in July 2001. We acquired such operators from Motorola, Inc. in exchange for an aggregate of $1,835.5 million in our shares and $10.5 million in cash and transferred them to Telefonica Moviles in exchange for approximately 203 million of its ordinary shares.

(2) Acquisition of Pegaso Telecomunicaciones, S.A. de C.V. and Formation of Telefonica Moviles Mexico. On April 26, 2002, Telefonica Moviles signed agreements to purchase 65.3% of Pegaso from Sprint, Leap Wireless, Qualcomm and other financial investors. Pegaso owns licenses to operate on a nationwide basis. In connection with this agreement, Telefonica Moviles also agreed with the Burillo Group, who held a 34.77% interest in Pegaso at the time of the acquisition, to contribute Telefonica Moviles' interests in Pegaso and its other Mexican operators and the Burillo Group's interest in Pegaso into a new holding company, Telefonica Moviles Mexico.

On September 10, 2002, having obtained authorization from the relevant Mexican authorities, Telefonica Moviles acquired a 65.23% holding in Pegaso for $92.9 million. In accordance with Telefonica Moviles' agreement with the Burillo Group, on September 10, 2002 Telefonica Moviles contributed its interest in Pegaso and its other Mexican operators (Bajacel, Movitel, Norcel and Cedetel) to Telefonica Moviles Mexico. On the same date the Burillo Group contributed its wireless interests to Telefonica Moviles Mexico.

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Telefonica Moviles' Mexican operators.

	At December 31		
	2002(1)	2003	200
Total customers (in millions at period end)........................	2.4	3.5	5.
Pre-paid customers (in millions at period end).....................	2.1	3.2	5.
Population in service territory (in millions at period end).........	102.0	103.3	104.

Source: Telefonica Moviles, except population
Population: Pyramid Research

----
(1) The figures for 2002 include our four Northern Mexican operators and Pegaso as from September 10, 2002.

Regulation

The provision of telecommunications services in Mexico is regulated by the Telecommunications Federal Law ("LFT"), enacted in 1995 (D.O.F.7/6/95), as well as specific regulations governing the different types of telecommunications services.

Regulatory authorities. The following governmental agencies oversee the telecommunications industry in Mexico::

- the Secretariat of Communications and Transportation (SCT), and
- the Federal Telecommunications Commission (COFETEL).

Licenses and concessions. In Mexico, authorization to provide mobile telephony services is granted through a concession. Telefonica Moviles's Mexican wireless operating companies have been granted the following concessions to operate mobile telephony services on Band A:

- Baja Celular Mexicana, S.A. de C.V., or Bajacel, operates in Region 1, which consists of the states of Baja California, Baja California Sur and the municipality of San Luis Rio Colorado in the state of Sonora;

- Movitel del Noroeste, S.A. de C.V, or Movitel, operates in Region 2, which consists of the states of Sinaloa and Sonora, except for the municipality of San Luis Rio Colorado, which is included in Region 1;

52

- Telefonia Celular del Norte, S.A. de C.V, or Norcel, operates in Region 3, which consists of the states of Chihuahua, Durango and the municipalities of Torreon, Francisco I. Madero, Matamoros, San Pedro and Viesca in the state of Coahuila; and

- Celular de Telefonia, S.A. de C.V, or Cedetel, operates in Region 4, which consists of the states of Nuevo Leon, Tamaulipas and Coahuila, excluding the municipalities of Torreon, Francisco I. Madero, Matamoros, San Pedro and Viesca.

Currently, only one Band A and one Band B service provider may provide mobile telephony services in each region. Each concession is granted for a period of twenty years, and may be renewed for additional twenty year periods, subject to the fulfilment by the operator of certain terms and conditions. These conditions are the fulfilment of the current obligations, solicitation of the renewal of the license before the expiration of the licensee, and accepting the new conditions that will be established by the SCT. The concessions to provide mobile telephony services awarded to the above operating companies each expire in 2010.

In July 2001, Telefonica Moviles acquired, through Cedetel, a 49% interest in Grupo de Telecomunicaciones Mexicanas, S.A. de C.V., or GTM, which holds a concession to provide radio link in the 7 GHz band. This concession expires in 2018, and may be renewed for additional twenty year periods. On June 5, 2003 GTM was granted a license to provide, among others, national and international long distance services for a 15 year period. This license may be renewed if GTM complies with certain conditions under Mexican federal communications law. In July 2004, GTM acquired a concession from Megacable to provide a point-to-point link in the 23 GHz. band. This concession was granted in 1998 and expires in 2018.

On April 26, 2002, Telefonica Moviles signed definitive agreements to purchase 65% of Pegaso. In 1998, Pegaso was awarded licenses to provide personal communication services until 2018. This license may be extended for additional twenty year periods, subject to the fulfillment by the operator of certain terms and conditions.

The concessionaires are subject to general obligations set forth by SCT and COFETEL, and to obligations pursuant to each concession concerning quality of service, network expansion and modernization.

On July 12, 2004 COFETEL called for an auction to grant concessions to provide fixed and mobile wireless access. The bidding process for certain wireless frequencies available in each of nine PCS regions began on January 11, 2005. Nextel, Telcel, Iusacell and Telefonica Moviles were participating in the bidding process. However, the auction was halted on February 9, 2005 due to a court order mandating that COFETEL allow UNEFON to participate in the auction. The bidding process was re-initiated on April 1, 2005.

Interconnection. Mexican legislation on telecommunications matters requires all network license holders to undertake interconnection agreements whenever another operator requests it. The terms of such agreements may be freely negotiated between parties on a non-discriminatory basis. In the event of any controversy, COFETEL must arbitrate between the parties. The interconnection agreements must be registered in the telecommunications register, and those that are signed with foreign networks require prior authorization from the SCT.

Under Mexican law, COFETEL can establish specific obligations for the concessionaires of public telecommunications networks who hold significant market power regarding prices, quality of service and the provision of information.

Since May 1, 1999, the Calling Party Pays system (CPP) has applied exclusively to local service (services established between exchanges of the same local area) although the user has the option of maintaining the Receiving Party Pays system. COFETEL has stated that it is considering extending CPP to national long-distance calls, which would require regulatory approval by the Federal Commission for Regulatory Improvement.

Rates. Rates charged to customers are not regulated. They are fixed by wireless operating companies and must be registered with COFETEL. Rates do not enter into force until confirmed by COFETEL.

Network and Technology

Telefonica Moviles Mexico offers both analog and digital networks. Its digital networks are based upon the CDMA and GSM standards. At December 31, 2004, Telefonica Moviles Mexico's digital network in Mexico consisted of 35 switching centers and 4,677 base stations, including both digital (GSM, CDMA1900 and 850) and analog (AMPS) base stations giving coverage to more than 52.5% of the population. In each of the regions in which Telefonica Moviles Mexico operates, it holds licenses of 20 MHz of spectrum on the 850 MHz band, and 30 MHz and 10 MHz of spectrum on the 1900 MHz band.

The launch of Telefonica Moviles Mexico GSM network on a nationwide basis started in 2003 and by the end of 2004 covered areas with a population representing 77% of Mexico's national gross domestic product at December 31, 2004. Telefonica Moviles Mexico has invested during the three years ended December 31, 2004 a total of (euro)970 million, principally during 2003 and 2004. on its GSM network.

Competition

Telefonica Moviles Mexico competes with various operators at a national level, most of which are subsidiaries of larger international telecommunications companies. The principal competitor of Telefonica Moviles Mexico is Telcel. The other competitors of Telefonica Moviles Mexico are Iusacell, Unefon, and Nextel.

Chile

Prior to 2004, Telefonica Moviles was party to a management agreement with Telefonica Movil Chile, a mobile phone operator in Chile and a subsidiary of Compania de Telecomunicaciones de Chile. On July 23, 2004, after the acceptance of a binding offer by Compania de Telecomunicaciones de Chile's Board of Directors, Telefonica Moviles acquired 100% of the shares of Telefonica Movil Chile.

Telefonica Movil Chile had approximately 3.3 million customers at December 31, 2004, which, according to Telefonica Movil Chile's estimates based on information provided by its competitors and regulatory authorities, accounted for 34.7% of the overall mobile telephony market. Since the launch of its GSM services in April 2003, Telefonica Movil Chile has approximately 1.5 million GSM customers, approximately 44% of its total customers.

The following table presents, at the dates and for the period indicated, selected statistical data relating to Telefonica Movil.

	Year ended December 31,		
	2002	2003	2004
Total customers (in millions at period end)........................	1.8	2.3	3.3
Pre-paid customers (in millions at period end).....................	1.4	1.8	2.8
Population in service territory (in millions at period end).........	15.2	15.4	15.4

Source: Telefonica Moviles, except population
Population: Pyramid Research

On March 5, 2004 Telefonica Moviles agreed to acquire BellSouth's wireless companies in Latin America, including BellSouth Comunicaciones and BellSouth Chile. The acquisitions of BellSouth Comunicaciones and BellSouth Chile closed on January 7, 2005.

Regulation

The General Telecommunications Law (No. 18,168) of 1982, as amended, established the legal framework for the provision of telecommunications services in Chile. The law established the rules for granting concessions and permits to provide telecommunications services and for the regulation of rates and interconnection.

Regulatory Authorities. The main regulatory agency of the Chilean telecommunication sector is the Ministry of Transportation and Telecommunications, which acts primarily through the Undersecretary of Telecommunications (SUBTEL).

Licenses and Concession. Telefonica Movil Chile holds the following concessions:

- Concession for the provision of wireless telecommunications services in the 800 MHz band:

  - For the Metropolitan Region and Region V, the concession was granted on November 11, 1998 for an unlimited period of time.

  - For Regions I to IV and Regions VI to XII, the concession was granted on August 3, 1989 for an unlimited period of time.

- Concession for the provision of wireless telecommunications services in the 1900 MHz band. The concession was granted for a thirty year period from November, 16, 2002, and may be renewed for successive thirty year periods at the request of the holder.

Chilean regulatory authorities approved the acquisition of BellSouth Comunicaciones and BellSouth Chile by Telefonica Moviles subject to certain conditions, such as the sale by auction of 25MHz of bandwidth in the 800MHz band by Telefonica Moviles within 18 months.

BellSouth Chile's concessions for the provision of telecommunication services include the following:

- Concession for the provision of wireless telecommunications services in the 800 MHz band:

  - For the Metropolitan Region and Region V, the concession was granted for a fifty- year period from January 27, 1982 and may be renewed for successive fifty year periods at the request of the holder.

  - For Regions I to IV and Regions VI to X, the concession was granted on February 6, 1990 for an unlimited period of time.

  - For Regions XI and XII, the concession was granted July 26, 1993 for an unlimited period of time.

- Concession for the provision of wireless telecommunications services in the 1900 MHz band:

  - for the provision of wireless service nationwide with a bandwidth of 10 MHz, the concession was granted for a thirty year period from April 3, 2003 and may be renewed for successive thirty year periods at the request of the holder.

- BellSouth Chile also holds a concession for fixed line long distance services nationwide granted March 16, 1994 for an unlimited period of time.

Interconnection. The Telecommunications Law requires that holders of public telecommunications service licenses to interconnect their networks to other networks providing the same type of service. This requirement is intended to ensure that subscribers and users of telecommunications services are able to communicate with each other, both inside Chile and abroad. The same requirement applies to holders of intermediate service licenses, who are required to interconnect their networks to the local telephone network. SUBTEL sets the applicable tariffs for services provided through the interconnected networks, in accordance with the procedures established in Section 25 of the Telecommunications Law. The structure, level and indexing of these interconnection rates are fixed by a tariff decree by the Chilean Ministries of Economy and Transport and Telecommunications.

The tariffs are set every five years. Starting on February 13, 2004, the new interconnection charges for the 2004-2009 period became effective for both Telefonica Movil and BellSouth Chile. The new interconnection charges have decreased by an average of 27.4% for the 2004-2009 from the average tariffs in

Chilean pesos as of December 31, 2002. The new tariff scheme stipulates three time slots defined as "peak", "reduced" and "night".

Rates. Calling Party Pays was implemented on February 23, 1999. Under this tariff structure, local telephone companies pay to mobile telephone companies an access charge for calls placed from fixed networks to mobile networks. Local telephone companies may pass this interconnection charge on to their customers. Under this tariff structure, local telephone companies pay to mobile telephone companies an access charge for calls placed from fixed

networks to mobile networks. Under the Calling Party Pays system, a fixed network costumer calling a mobile telephone pays the local telephone company a rate comprised of a local tariff that is part of the basic local telephone service plus a fee for interconnecting from the fixed network to the mobile network. Mobile telephone customers can choose not to have the Calling Party Pays system apply to their mobile-telephone accounts and thus continue to pay for incoming calls.

Network and Technology

Telefonica Movil Chile maintains a fully digitalized nationwide TDMA mobile network of 25 MHz in the 800 MHz frequency. In 2002 Telefonica Movil Chile also acquired through an auction two nationwide bands of 10 MHz each in the 1900 MHz mobile frequency (PCS), which it is developing with GSM/GPRS technology. In April 2003, Telefonica Movil Chile launched its GSM service, which has the benefit of operating over the only GSM/GPRS network covering all of Chile. In 2004, Telefonica Movil Chile continued to make improvements to its GSM/GPRS network's quality and coverage of voice services nationwide.

In 2003, with the addition of the GSM/GPRS network, Telefonica Movil Chile began to deploy new services such as multimedia messaging (Movil Image), game downloads (Movil Game) and ring-tone downloads (Movil Music). In July 2003, a new data transmission service, the GPRS mobile Internet, was launched. In October 2003, the installation of the new "enhanced data rates for global evolution", or EDGE, high-speed data network made Chile the fourth country worldwide and the first country in Latin America that is able to provide its citizens with third generation (3G) services.

In March 2004, Telefonica Movil became the first operator in Chile to launch mobile TV services providing its customers with local TV programs on their mobile phones. In April 2004, a new broadband mobile service was launched offering customers a "always on" connection with a transfer speed of up to 474 kbits/s. In October 2004, Telefonica launched a photo log service that lets customers create their own web pages to send images or SMS from their mobile phones.

The GSM/GPRS network extended roaming services to more than 160 countries. Since early 2004, Telefonica Movil Chile's contract clients can use the GPRS roaming service in Spain, the U.S., Argentina and Mexico, allowing them access to data services when they are abroad.

In the three years ended December 31, 2004, Telefonica Movil Chile invested a total of approximately (euro)170 million in building out and enhancing its network in Chile. At December 31, 2004 Telefonica Movil Chile's digital wireless network consisted of 14 switching centers and 1,435 base stations giving coverage to over 98% of the population.

Competition

Telefonica Movil Chile currently has two competitors in the Chilean market for wireless communication service: Entel PCS and Smartcom.

Central America

Telefonica Moviles provides wireless services in El Salvador and Guatemala through TES Holdings, S.A. and TCG Holding, S.A., respectively. These holding companies own interests in Telefonica Moviles El Salvador, S.A. de C.V., and Telefonica Centroamerica Guatemala, S.A. de C.V.

Telefonica Moviles manages Telefonica Moviles El Salvador and Telefonica Centroamerica Guatemala in exchange for an annual fee of 9% of the operating profits of each operating company.

In August 2001, Telefonica Moviles entered into an agreement with Mesotel de Costa Rica, S.A., a subsidiary of Mesoamerica Telecom, to acquire its direct and indirect interests in Telefonica Moviles El Salvador, Telefonica Centroamerica Guatemala, Telca Gestion, S.A. and Telca Gestion Guatemala, S.A., and other companies in which Telefonica Moviles and Mesoamerica Telecom were shareholders, in exchange for approximately 21.9 million of Telefonica Moviles' ordinary shares. In January 2002, Telefonica Moviles amended this agreement and acquired one-third of Mesotel de Costa Rica, S.A.'s interests in exchange for 7.3 million of Telefonica Moviles' ordinary

shares. The remaining two-thirds of Mesotel de Costa Rica, S.A.'s interests were purchased by Telefonica Moviles in July 2002 for 14.6 million Telefonica Moviles' ordinary shares. As a result of these transactions, Telefonica Moviles held. a 91.75% interest in Telefonica Moviles El Salvador and a 100% interest in Telefonica Centroamerica Guatemala at December 31, 2004.

On March 5, 2004 Telefonica Moviles agreed to acquire BellSouth's wireless companies in Latin America, including Bellsouth y Cia, S.C.A. in Guatemala. The acquisition of Bellsouth y Cia, S.C.A. closed in October 2004.

El Salvador

Telefonica Moviles provides wireless services in El Salvador through Telefonica Moviles El Salvador, the third largest of four wireless operators in El Salvador, with approximately 384,300 customers at December 31, 2004, representing 23.7% of the market.

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Telefonica Moviles' operations in El Salvador:

	At December 31,		
	2002	2003	2004
Total customers	230,856	255,300	384,300
Pre-paid customers	160,266	186,309	294,000
Population in service territory (in millions)	6.5	6.6	6.7

Source: Telefonica Moviles, except population
Population: Pyramid Research
(1) Includes both fixed wireless lines and wireless operations.

Telefonica Moviles El Salvador commenced offering digital wireless services in El Salvador in December 1998 under the Movistar brand name. In addition to wireless services, Telefonica Moviles El Salvador also provides Internet, cable TV and telephone services through Telefonica Multiservicios, a joint venture between Telefonica Moviles El Salvador and Amnet, an international communications provider in El Salvador.

Regulation

Concessions for the provision of telecommunications services are granted for a thirty year period. The concession may be renewed for successive thirty year periods. Telefonica El Salvador holds a concession to provide public telephone service, including wireless services, throughout El Salvador until January 1, 2028.

Concessions for use of spectrum are granted for terms of twenty years and may be renewed for successive twenty year periods. Telefonica Moviles El Salvador holds the following concession for use of spectrum:

o concession to use 25 MHZ of spectrum in the 800 MHz B band; and

o concession to use the following frequencies for multi-channel connections, including the delivery of wireless services: 5 GHZ, 11 GHz; and 23 GHz.

A concession may be revoked only when a concession holder does not supply telecommunications services within two years after the concession has been granted or if it commits three serious infractions described in the relevant law within a period of three years. Concessions may be renewed by filing a new application with the General Superintendency of Electricity and Telecommunications. Concessions are renewed depending on the fulfillment of certain terms and conditions by the holder of the concession. Applications for renewal of the concession must be sought one year before its expiration or the regulatory authority will hold an auction to sell the concession to other operators.

57

Network and Technology

The digital network of Telefonica Moviles in El Salvador is based upon the CDMA and GSM standard. During the three years ended December 31, 2004 Telefonica Moviles El Salvador invested a total of approximately (euro)38 million in building out and enhancing its networks in El Salvador. At December 31, 2004 the digital network of Telefonica Moviles in El Salvador consisted of two switching centers shared by the fixed line and mobile networks and 252 base stations giving coverage to over 50% of the population.

Competition

Telefonica Moviles El Salvador currently competes in the El Salvador market for wireless communications service with Telemovil, CTE Telecom and Digicel.

Guatemala

Telefonica Moviles provides wireless services in Guatemala indirectly through its wholly owned subsidiary Telefonica Centroamerica Guatemala. We also provide wireless services through TEM Guatemala y Cia after its acquisition from BellSouth by Telefonica Moviles in October 2004. At December 31, 2004, Telefonica Moviles' total customer base in Guatemala was approximately 751,000 (Telefonica Moviles Guatemala: 376,000 and TEM Guatemala y Cia.: 375,000).

The following table presents, at the dates and for the periods indicated, selected statistical data relating to Telefonica Moviles' operations in Guatemala:

	At December 31,		
	2002	2003	2004(1)
Total customers	97,089	156,868	750,554
Pre-paid customers	48,865	113,551	562,051
Population in service territory (in millions)	12.0	12.0	12.7

Source: Telefonica Moviles, except population
Population: Pyramid Research

(1) Customer data for 2004 includes TEM Guatemala y Cia.'s subscribers acquired by Telefonica Moviles from BellSouth in October 2004.

Telefonica Centroamerica Guatemala commenced offering digital wireless services in Guatemala in October 1999 under the Movistar brand name. Telefonica Centroamerica Guatemala also provides fixed line public telephone service, data and long distance services and paging services through its subsidiary Tele Escucha with 7 thousand customers as of December 31, 2004.

Regulation

In Guatemala, a telecommunications services provider does not require a governmental concession to provide such services, but does require an authorization to use the spectrum. These authorizations are called "titles." Telefonica Centroamerica Guatemala, S.A. holds titles, obtained in a public auction in March 1999, to use two 15 MHz channels in the 1900 MHz band for the provision of wireless services until 2014. Titles are granted for a fifteen-year term and may be renewed for subsequent fifteen-year terms at the request of the holder. The renewal process is based on the fulfillment by the operator of certain terms and conditions.

Network and Technology

In Guatemala, Telefonica Centroamerica Guatemala operates a digital network, which is based upon the CDMA and GSM standards. Telefonica Centroamerica Guatemala's license entitles it to 30 MHz of spectrum in the 1900 MHz band. In the three years ended December 31, 2004 Telefonica Centroamerica Guatemala invested a total of approximately (euro)34 million mostly in building out and enhancing its network in Guatemala. At December 31, 2004, Telefonica Centroamerica Guatemala's digital wireless network consisted of three switching centers and 421 base stations giving coverage to over 81% of the population.

Competition

Telefonica Moviles currently has two competitors in the Guatemala wireless market: Telgua and Comcel.

Other operations

Other Latin American companies acquired from BellSouth

At December 31, 2004, the customer base of the six other wireless operators acquired from BellSouth in Latin American totaled 9.9 million (Telefonica Moviles Colombia: 3.3 million; Otecel (Ecuador): 1.1 million; Telefonia Celular de Nicaragua: 286,000; BellSouth Panama: 626,000; Abiatar (Uruguay): 203,000 and Telcel (Venezuela): 4.3million). Commercial activity of these newly acquired companies under the management of Telefonica Moviles in the last two months included primarily Christmas campaigns aimed at acquiring new prepaid customers.

Puerto Rico

NewComm Wireless Services Inc. was organized on January 29, 1999 to operate a personal communication services (PCS) license in Puerto Rico as a joint venture agreement between Telefonica and Clearcomm and commended commercial operations in late September 1999.

Newcomm Wireless entered into a management contract with Telefonica Moviles when it commenced operations. In September 2004, the management contract was cancelled and Clearcomm took charge of the management of Newcomm Wireless. Telefonica Moviles decided to write-off the value of certain convertible notes issued by Newcomm Wireless to Telefonica Moviles, which are convertible into an approximately 49% interest in Newcomm Wireless, as of December 31, 2004 in light of the continued competitive environment in Puerto Rico.

Since the cancellation of the management contract, Wireless Services Inc.'s customer base is no longer included in our managed customer base.

Wireless Internet and Data Initiatives

Wireless Internet and Data

We believe that the convergence of data communications and voice communications represents a new and important opportunity to create value in the mobile communications sector in the near future. An important component of our strategy is broadening uses of wireless communications, currently dominated by voice services, to include more widespread use of wireless Internet and data services. By diversifying our services, we are seeking to capture the value created by these new services. Revenue from data transmission services increased to almost (euro)1 billion in 2004 primarily due to the increased use of other data services other than traditional SMS service.

We anticipate the demand for wireless Internet services will grow as network transmission speeds increase through the roll-out of GPRS (general packet radio service), CDMA 1XRTT, EDGE and UMTS services, allowing wireless voice and higher-speed data transmission.

Telefonica Moviles offers GPRS services in Spain commercially with the same coverage as its GSM network. Regarding UMTS, after the pre-commercial launch of UMTS services in October 2003, on February 13, 2004 Telefonica Moviles Espana launched its "Oficin@ Movistar UMTS"GPRS/UMTS data card, the first third generation service offered in Spain by a mobile operator with high-speed data transmission up to 384 kbits/s, to its corporate customers.

This service was extended to all Telefonica Moviles Espana residential and prepaid customers on May 24, 2004, initially in Madrid and Barcelona, and gradually extended to the rest of Spain. On that same date, Telefonica Moviles Espana launched the first UMTS videophone services in the Spanish market. We believe that any large-scale launch of UMTS technology will ultimately be determined by the availability of UMTS compatible handsets that are small, reasonably priced, and have adequate battery life.

In other markets such as Brazil and Peru, Telefonica Moviles has already launched high speed data services based on technologies such as CDMA 1XRTT. During 2004, Telefonica Moviles continued expanding the CDMA 1xRTT network in Brazil, reaching 3,700 base stations and covering over 800 municipalities in its areas of operation

at December 31, 2004. Additionally, in 2004 Brasilcel also launched CDMA EVDO, a technology that increases data capabilities allowing speeds of up to 2.4 megabytes per second. In Peru, Telefonica Moviles commercially launched the CDMA 2000 1xRTT network on November 27, 2003, and by December 2004, the CDMA1xRTT network consisted of 273 base stations.

In addition, GSM/GPRS cellular services have been offered in Mexico and Chile since 2003, and were launched in Argentina, Guatemala and El Salvador in 2004. In Mexico, GSM/GPRS coverage reached 247 cities by December 2004, a level of population representing 77% of Mexican GDP; and EDGE technology was rolled-out on its GSM network in July 2004, providing speeds of up to 240 Kb/s and offering services such as video streaming, web browsing and high-speed data transmission capabilities. In Argentina, one year after its launch, the GSM network reached a population coverage of approximately 82% of national GDP.

In June 2000, Telefonica Moviles launched Movistar e-mocion, its wireless Internet service provider in Spain. Most of Telefonica Moviles' operating companies have launched Movistar e-mocion or similar services under different brands, such as Vivo in Brazil.

Currently Movistar e-mocion has several content groups in Spain, including mobile banking, media, news, portals, ticketing, m-commerce, travel, entertainment, health and yellow pages, among others. Telefonica Moviles has signed agreements with more than 250 content providers to provide links through Movistar e-mocion for products and services in Spain, including: Terra Mobile, Yahoo!, Telefonica Paginas Interactivas, Reuters, LaNetro, Banco Bilbao Vizcaya Argentaria, La Caixa, Santander Central Hispano, Unicaja, Serviticket, AVIS, Globalia Group, Antena 3, CNN, ABC, La Vanguardia and Infojobs. Customers can also access Movistar proprietary services, such as e-mail and itemized call information. Telefonica Moviles' wireless data services include SMS, MMS and Internet access via personal computers and PDAs, as well as the ability to receive information such as general news, sport scores and stock market information. Telefonica Moviles is focusing on consolidating its position in the corporate segment (where it has a strong position in terms of market share) with a view to introducing and marketing new wireless data services and applications.

In June 2003, Telefonica Moviles launched i-mode services in Spain, integrated with its Movistar e-mocion mobile portal, which can be accessed through a diverse range of terminals. In addition, in November 2001, Telefonica Moviles Espana, together with Ericsson, Hewlett Packard and the regional government of Cataluna created Tempos21, Innovacion en Aplicaciones Moviles, S.A., or Tempos21, with the objective of conducting research and development on wireless services and applications based on the GSM, GPRS and UMTS standards or other technologies that may be developed. Tempos21, which began operations in 2002, is developing, implementing and managing wireless Internet related products and other wireless services and applications for enterprises (B2B and B2B2C). Tempos21 also provides consulting services and develops integrated solutions for the aforementioned sectors. Telefonica Moviles Espana holds a 38.5% interest in Tempos21.

Telefonica Moviles' wireless Internet access services in Spain are currently billed on the basis of connection time, at a discount to voice rates, for WAP (wireless access protocol) CDS services, and on the basis of the volume of data sent, for WAP GPRS services, and, in each case, depending on the content. Telefonica Moviles also offers premium services, under which access to premium content is available at an extra charge, which it shares with the content providers. Telefonica Moviles receives 100% of the revenues derived from wireless airtime induced by Movistar e-mocion. It also receives a percentage of the m-commerce revenues of its partners.

M-Payment

Telefonica Moviles initially began developing this business in conjunction with Banco Bilbao Vizcaya Argentaria as a 50-50 joint venture. At the same time, Banco Santander Central Hispano, a major Spanish bank, and Vodafone were jointly developing a separate mobile payment system. On May 30, 2001, Telefonica Moviles, Banco Bilbao Vizcaya Argentaria, Banco Santander Central Hispano and Vodafone agreed to integrate their respective mobile payment systems to form a single mobile payment standard. The new payment system is an open system, which other financial institutions, wireless operators (such as Amena) and payment processing companies in Spain have joined. This system is being developed in Spain through MobiPay Espana, S.A. and outside of Spain through MobiPay International S.A.

60

The MobiPay initiative became more widely accepted in 2004. At December 31, 2004 there were approximately 2,600 on-line stores, including FNAC, Halcon Viajes, MundoHogar, Seguros Winterthur and Air Europa, which had included MobiPay as a method of payment. In February 2004, an agreement was reached with Kilowatt to implement the mobile payment standard in services offered by Kilowatt such as vending machines.

In addition, on February 26, 2003, Telefonica Moviles, Orange, T-Mobile and Vodafone signed an agreement for the creation of the Mobile Payment Services Association which will operate under the brand name Simpay. The objective of the association is to promote an open solution under one common brand for payments through mobile phones that would be compatible with the networks of the different operators. This system would be available in several countries and would complement other systems that already exist in the telecommunications sector.

In February 2004, Simpay presented its first product based on payments in amounts less than (euro)10. The product will be commercially available in 2005. Now that the design of the product and of the infrastructure has been completed, Simpay and the founding companies will invite other mobile operators to join the partnership. European mobile telephony operators such as 3, Debitel, KPN Mobile, Elisa (previously Radiolinja), Mobilkom, Optimus, O2, SFR, TeliaSonera and TMN have expressed interest in joining Simpay.

In February 26, 2003, Telefonica Moviles entered into an alliance with three other European mobile operators, T-Mobile International, Telecom Italia Mobile, or TIM, and Orange. This alliance adopted the brand name FreeMove in March 2004 to represent its joint offering. This alliance is using its collective scale, strength and expertise to deliver an enhanced, seamless service for customers of the four partners when traveling abroad through its "Virtual Home Environment" as well as new service offerings to international customers. This alliance has also resulted in economic benefits to the operators from joint handset procurement as well as preferred supplier agreements with Siemens and Motorola.

Latin American Fixed Line Business--Telefonica Latinoamerica

Our Latin American fixed line business is conducted through Telefonica Latinoamerica. The following tables set forth information with respect to the fixed line telecommunications services provided by the principal telecommunications operators that are members of the Telefonica Latinoamerica group. Information is given as of December 31, 2004, unless otherwise specified.

Company	Country	Population at December 31, 2004(1)	Principal Fixed-Line Services Provided	
Telecomunicacoes de Sao Paulo-Telesp	Brazil	39.0	Basic telephony, domestic and international long distance, public telephony, Internet access, value added services	All ser ope com
Compania de Telecomunicaciones de Chile	Chile	15.4	Basic telephony, domestic and international long distance, public telephony, Internet access, value added services	All ser ope com
Telefonica de Argentina	Argentina	38.7	Basic telephony, domestic and international long distance public telephony, Internet access, value added services	All ser are com

Company	Country	Population at December 31, 2004(1)	Principal Fixed-Line Services Provided	
Telefonica del Peru	Peru	27.6	Basic telephony, domestic and international long distance public telephony, Internet	All ser ope com for

			access, value added services, Cable TV	whi awa exc thr
Telefonica Larga Distancia de Puerto Rico	Puerto Rico	4.0	Long-distance services	Ope com

----

Source: Pyramid Research.

(1) Population in millions of coverage area.

The following table sets forth ownership and management information as of December 31, 2004 regarding the principal telecommunications operators that are members of the Telefonica Latinoamerica group.

Company	Year Acquired	Interest	Mana
Telecomunicacoes de Sao Paulo-Telesp	1998	87.5%	Telefonica Latinoa Telesp pursuant to contract
Compania de Telecomunicaciones de Chile	1990	44.9%	Telefonica Latinoa majority of the me of Directors
Telefonica de Argentina	1990	98.0%	Telefonica Latinoa Telefonica de Arge stake in COINTEL. Telefonica Latinoa Telefonica de Arge management contrac
Telefonica del Peru	1994	98.2%	Telefonica Latinoa majority of the me of Directors and m del Peru pursuant contract
Telefonica Larga Distancia de Puerto Rico	1992	98.0%	Telefonica Latinoa majority of the me of Directors

Brazil

Telecomunicacoes de Sao Paulo--Telesp

Telesp provides fixed line and other telecommunications services in the Brazilian state of Sao Paulo under concessions and licenses from Brazil's federal government. We acquired our initial interest in Telesp in 1998 as part of a consortium that acquired a majority interest in Telesp in connection with the restructuring of Telebras, the former Brazilian state-owned telecommunications monopoly. In mid-2000, we completed an exchange offer for the Telesp shares and ADSs held by minority investors. In July 2000, we agreed to exchange our interest in Portelcom Participacoes S.A., the holding company which controls Telesp Celular, for Portugal Telecom's minority interest in SP

Telecomunicacoes S.A., the holding company through which we control Telesp and paid an aggregate of approximately U.S.$60 million to Portugal Telecom pursuant to the terms of the agreement. In December 2001, we acquired an additional 3.5% of SP Telecomunicacoes S.A. from Iberdrola.

At December 31, 2004, Telesp managed approximately 13.3 million access lines in service, representing an increase of 4% from 12.8 million in 2003 due to a 1.3% increase in the number of traditional telephone lines and a 70.6% increase in broadband services. In 2004, the digitalization of Telesp's network increased to 98.67% and its productivity ratio increased to 1,865 lines in service per employee at December 31, 2004 from 1,792 lines in service per employee at December 31, 2003, principally due to an increase in lines in service (Traditional and ADSL lines). At December 31, 2004, Telesp had 826,000 ADSL lines, a 70.6% increase from the 484,000 lines in 2003, and 85.6% of Telesp's network had ADSL coverage.

Under a management contract between Telefonica Latinoamerica and Telesp, Telefonica Latinoamerica provides Telesp with management and technical support in exchange for management fees equivalent to 0.2% of Telesp's revenues, as defined in the management contract. The management contract expires in December 2005. Telesp and Telefonica Latinoamerica intend to renew the contract.

The following table provides information with respect to Telesp's fixed line telecommunications network at and for the periods indicated.

	At December 31			Increa (Decre
	2002	2003	2004	2003-2
Lines installed (in thousands)................	14,356	14,249	14,231	(0
Lines in service (in thousands)(1)............	12,839	12,781	13,289	4
Traditional lines in service..................	12,506	12,297	12,463	1
ADSL lines....................................	333	484	826	70
Penetration rate in Sao Paulo.................	32.9%	31.6%	31.7%	0
Lines in service per employee.................	1,349	1,792	1,865	4

----

(1) Beginning on January 1, 2003, we have retroactively introduced a modification in our calculation formula for the lines in service. This criteria will apply to the following equivalencies: PSTN (x1), basic ISDN (x2), primary ISDN (x30), 2/6 digital access for switchboards and Ibercom x30) and ADSL (x1). PSTN, or Public Switched Telephone Network, are lines that offer basic telephony services. ISDN, or integrated service digital networks, are lines that allow the integration of voice, data and video services through two 64kbits/s channels. ADSL, or asymmetrical digital subscriber lines, are lines that allow for voice and high speed data transmission. This new criteria introduces a difference in the manner in which we account for ISDN primary access and of the 2/6 access for switchboards and Ibercom, which will be multiplied by the number of access channels (30) instead of the extensions using it.

Regulation

In 1997, the Telecommunications General Law was passed in Brazil (Law

9472/97) creating a National Agency for Telecommunications, or Anatel.

Concessions and Authorizations. Concessions and licenses to provide telecommunications services are granted under the public regime, while authorizations are granted under the private regime. Companies that provide services under the public regime, or public regime companies, are subject to certain obligations as to quality of service, continuity of service, universality of service, network expansion and modernization. Companies that provide services under the private regime, or private regime companies, are generally not subject to the same requirements regarding continuity or universality of service. However, they are subject to certain network expansion and quality of service obligations set forth in their authorizations. Public regime companies, including Telesp, can also offer certain telecommunications services in the private regime, including data transmission services.

Fixed-line Services--Public Regime. Telesp's current concession agreement expires December 31, 2005, and, subject to satisfactory completion of certain network expansion, modernization and service quality obligations, contemplates a full renewal for an additional 20 years or revocation. Telesp formally notified Anatel of its intention to renew its concession agreement on June 30, 2003. Subject to its satisfaction of the network expansion, modernization and service quality obligations set forth in the current concession agreement through December 2005, Telesp's renewed concession agreement will become effective on January 1, 2006. While the basic form of the

renewed concession agreement has been finalized by Anatel and subject to extensive public comment, certain regulatory terms and conditions that will, or may be incorporated, into the renewed concession agreement remain pending. In order for the concession agreement renewal to take place Telesp must fulfill certain quality and universalization targets set forth in the current concession agreement that expires December 31, 2005. The universalization targets refer to deadlines for networks expansion and modernization for individual and collective access service availability. The quality targets refer to measured quality service on the services rendered to customers.

Act No. 25.120, enacted on April 25, 2002, allowed Telesp to provide local and interregional services in Regions I and II and Sector 33 of Region III, and international long distance services in Regions I, II and III.

Fixed-line Services--Private Regime. The Brazilian telecommunications regulations provide for the introduction of competition in telecommunications services by requiring Anatel to authorize private regime companies to provide local and intrarregional long-distance service in each of the three fixed-line regions and to provide intrarregional, interregional and international long-distance services throughout Brazil. Anatel has already granted authorizations to private regime operators to operate in Region III, Telesp's concession region.

Interconnection. Under the General Telecommunications Law, all fixed line telecommunications service providers must provide interconnection upon the request of any other fixed line or mobile telecommunications service provider. Telesp has interconnection agreements with other telephone service providers, including Embratel, Intelig and Telesp Celular. The interconnection agreements are freely negotiated among the service providers, subject to a price cap in compliance with regulations established by Anatel. If a service provider offers to any party an interconnection tariff below the price cap, it must offer the same tariff to any other requesting party on a nondiscriminatory basis. If the parties cannot reach an agreement on the terms of interconnection, including the interconnection tariff, Anatel can establish the terms of the interconnection.

Rates. For local network usage (TURL) and the interurban network (TU-RIU), rates are regulated by Anatel and an inflation index formula is included in the concession contract. Concession agreements also establish a price cap for annual rate adjustments, depending upon the type of service provided. Rates for international services are not required to follow the price cap.

In June 2003, Anatel prescribed new rates for Telesp's concession area. However, based on an injunction issued by a federal court, Telesp charged lower rates than those prescribed by Anatel. After the final decision regarding the legal injunction with the reincorporation of the IGP-DI as the index, the approved increases were applied in addition to the approved tariffs in June 2003. The increase was divided in two installments, the first one effective after September 1, 2004 and the second installment effective after November 1, 2004.

On June 29, 2004 Anatel approved new rates for Telesp's concession areas starting in July 2004. The approved increases were applied in addition to the tariffs determined by the legal injunction.

Competition

In addition to evolving regulatory considerations, Telesp's business is affected by competition from other telecommunications providers. Telesp began to face competition in its region in July 1999 and anticipates that competition will contribute to declining prices for fixed-line telecommunications services and increasing pressure on operating margins. Telesp's future growth and results of operations will depend significantly on a variety of factors, including:

- Brazil's economic growth and its impact on the greater demand for services;
- the costs and availability of financing; and
- the exchange rate between the real and other currencies.

Telesp is subject to competition for local telephone services from a "mirror" license holder, who was granted rights similar to those granted to Telesp as part of the privatization of Telebras. It is subject to competition for

interprovincial long distance services from a "mirror" license holder, Embratel and Embratel's "mirror" license holder.

Network and Technology

In 2003, Telesp began to offer international and interregional long distance telecommunication services known as "Super 15.". Since 1999, Telesp has made significant investments to develop its broadband access business through ADSL technology under the brand "Speedy." Telesp also offers wireless broadband connectivity to their clients through Wi-Fi.

Chile

CTC Chile

Compania de Telecomunicaciones de Chile, or CTC Chile, a company in which we held a 44.89% stake at December 31, 2004, is the leading telecommunications operator in Chile based on number of customers, according to information provided by its competitors and regulatory authorities. As of December 31, 2004, CTC Chile owned approximately 73% of all telephone lines in Chile, according to its estimates. CTC Chile provides a broad range of telecommunications and other services throughout Chile, including local telephone service, domestic and international long distance service, broadband access and services, dedicated lines, public telephone service, interconnection services, Internet access for corporate customers and security systems services. These services are complemented by the sale and rental of telephone equipment and a broad range of value added services that enhance the communications experience of its customers, such as voice mail, call-waiting, call-forwarding, caller-ID, outbound traffic control, CiberRing (call-waiting notice for Internet users) and access to information and entertainment services.

On July 23, 2004, CTC Chile sold to Telefonica Moviles a 100% interest in shares of Telefonica Movil Chile, a mobile telephone operator in Chile. The total amount paid for the acquisition was approximately (euro)1.1 billion.

CTC Chile managed approximately 2.63 million lines in service at December 31, 2004 and the access line penetration rate for the market in Chile was approximately 22.0% at that same date. CTC Chile's productivity ratio increased to 856 lines per employee in 2004 from 794 lines per employee in 2003, principally as a result of an increase in lines in services and workforce reductions. At December 31, 2004, CTC Chile had 200,700 ADSL connections in service compared to 125,200 in 2003. In 2004, the degree of digitalization of CTC Chile's network reached 100% and 87.8% of its network had ADSL coverage.

Regulation

The regulatory framework of Chile, defined in the General Telecommunications Law (Ley General de Telecommunications), was enacted in 1982. This law introduced competition in the telecommunications services sector in Chile (Law 18168/82 amended by Decree 1/87, Laws 19091/91 and 19302/94) and dictated provisions on licenses and permits for operating telecommunications services, rate regulation and network interconnection. Those provisions were later amended or replaced by subsequent modifications.

Regulatory authorities. The following regulatory authorities exist in Chile:

- the Under-Secretary of Telecommunications (SUBTEL);
- the Ministry of Economy, Infrastructure and Reconstruction;
- the Ministry of Transport and Telecommunications; and
- the Antitrust Commission.

Licenses and Concessions. Under Law No. 18,168, companies must obtain licenses in order to provide telecommunications services. Licenses granted for public and intermediate services generally have 30-year terms and may be renewed indefinitely for 30-year periods at the request of the operator (although certain licenses held by CTC Chile have longer terms).

A license may be terminated, after notice of noncompliance with the applicable technical regulations, by executive decree of the Ministry of Transport and Telecommunications, if the operator is in violation of the law or does not comply with the terms and conditions to which the license is subject. If a license is terminated, the holder is barred from applying for any license for a period of five years.

CTC Chile holds the following licenses:

- Local Telephony Public Service. CTC Chile holds licenses for local telephone service in all regions of Chile for a 50-year period beginning as of December 1982.

- Multicarrier Long Distance Licenses. CTC Chile, through Telefonica Mundo and Globus, respectively, holds 30-year licenses granted in April 1993 and licenses for an indefinite term to provide domestic and international long distance services through central switches and cable and fiber-optic networks nationwide.

- Data Transmission. CTC Chile, through Telefonica Empresas, holds, as of March 1987, nationwide public service data transmission licenses for an indefinite term.

Telecommunications services in Chile are provided on a competitive basis, although access rates (for network use), must be set by the Ministry of Transport and Telecommunications and the Ministry of Economy, according to article 25 of the General Telecommunications Law.

Interconnection. Interconnection is obligatory for all license holders of public telecommunications services and intermediate services that provide long distance services. The Exempt Resolution No. 1007/95 sets the procedures and deadlines to establish and accept interconnections between networks of public telephone service and intermediate services.

Rates. Under the General Telecommunications Law, maximum tariffs for telephony services are set every five years by the Ministry of Transport and Telecommunications and the Ministry of Economy. The Antitrust Commission may subject any telephony service to price regulation, except for mobile telephone services to the public that are expressly exempted under the General Telecommunications Law.

Each maximum tariff takes into account the relevant cost components associated with providing the regulated service, and is adjusted monthly in accordance with a tariff index. A distinct tariff index exists for each individual regulated service that reflects the different theoretical cost components associated with each such service.

On October 13, 2003 the Antitrust Commission issued Resolution No. 709, approving CTC Chile's request for local telephony services tariff flexibility and the ability to offer alternative plans within a framework of conditions specified by the regulator. On February 26, 2004 a framework regarding how CTC Chile may offer the mentioned alternative tariff plans was published. One relevant aspect is that no previous authorization is required to offer such plans. Plans are not subject to maximum levels or predetermined structures and may include joint offers with other telecommunication and non-telecommunication services.

On May 4, 2004 a new tariff decree was proposed by the Ministry of Transport and Telecommunications. CTC Chile and other operators filed appeals to the tariff decree and subsequently the Ministry resubmitted the decree to the Chilean General Controller in September 2004, and again in December 2004 with slight modifications to the document submitted in May 2004. On February 11, 2005, Tariff Decree No. 169 was published in the Official Gazette. CTC Chile will apply the new tariffs to its customers retroactively as of May 6, 2004.

Argentina

Telefonica de Argentina

Telefonica de Argentina is a leading provider of fixed line public telecommunications services and basic telephone services in Argentina based on number of customers, according to information provided by its competitors

and regulatory authorities. Telefonica de Argentina is licensed to provide local and domestic long distance and international services and domestic and international telex services throughout Argentina. Telefonica de Argentina's licenses do not expire but may be cancelled as a result of a failure to comply with the terms of the license. During 2000, we increased our stake in Telefonica de Argentina through a public exchange offer for Telefonica de Argentina shares and ADSs held by minority investors and our acquisition of a 50% interest in Compania de Inversiones en Telecomunicaciones (COINTEL), which held a 52.9% stake in Telefonica de Argentina. At December 31, 2004, we held a 98.03% interest in Telefonica de Argentina.

At December 31, 2004, Telefonica de Argentina's telecommunications network had approximately 4.52 million lines in service, including ADSL lines, an increase of 6.6% from approximately 4.24 million at December 31, 2003, and the access line penetration rate for the market in Argentina was 23.6%. At that date, Telefonica de Argentina's estimated market share for local telephony was 51.4%, its estimated market share for domestic long distance was 35.9% and its estimated market share for international long distance was 42.4%. Telefonica de Argentina's broadband operations expanded in 2004, reaching 189,000 ADSL users at December 31, 2004 while also developing the usage of wireless broadband technology (WIFI).

As of December 31, 2004, approximately 51% of Telefonica de Argentina's lines in service were in the Greater Buenos Aires metropolitan area, including 21% of Telefonica de Argentina's lines in service that were located within the City of Buenos Aires. Approximately 86% of Telefonica de Argentina's lines in service as of December 31, 2004, were residential, with the remainder being professional, commercial and governmental customers.

Telefonica Latinoamerica has a management contract with Telefonica de Argentina under which it has agreed to manage Telefonica de Argentina's business and provide services and expertise regarding Telefonica de Argentina's entire range of activities in return for a percentage of Telefonica de Argentina's operating revenues equivalent to 4% of its gross revenue prior to amortization and interest expense. This contract was renegotiated during 2003 and was extended through 2008 with a 5 percentage point reduction of our management fee. Under the management contract, Telefonica Latinoamerica manages Telefonica de Argentina's day-to-day operations.

Regulation

The basic legal framework is set forth in the National Telecommunications Law (No. 19,798) from 1972, and in the specific regulations governing each service. Through Decree 264/98 the telecommunications market in Argentina was deregulated.

On September 3, 2000, the Argentine government issued Decree No. 764/00, which approved rules for licenses for telecommunications services, interconnection, universal service and for the administration, management and control of the radio electric Sspectrum.

In January 2002, the Public Emergency Law introduced significant changes to the agreements executed by the Argentine government, including those regarding utilities, such as Telefonica de Argentina's tariff agreements. This law mandated the conversion of prices and tariffs in such agreements into pesos at a rate of one peso per one U.S. dollar without the possibility of adjusting such conversion rate or indexation of any kind. It also authorizes the Argentine government to renegotiate the above-mentioned contracts.

As an investor in Argentina through Telefonica Argentina, we commenced arbitration proceedings against the Republic of Argentina before the CIADI, (Centro Internacional de Arreglo de Diferencias relativas a Inversiones) based on the Reciprocal Protection of Investments Treaty between Spain and Argentina, for damages suffered by us because of the measures adopted by the Argentine Government. We submitted pleadings to the arbitration tribunal on December 6, 2004 and the Republic of Argentina submitted its answer in February 2005.

On October 21, 2003, Law No. 25.790 became effective, extending the term for the renegotiation of the concession or licensing agreements with public utilities until December 31, 2004. This law also established that the decisions made by the Argentine government during the renegotiation process shall not be limited by, or subject to, the stipulations contained in the regulatory frameworks currently governing the concession or licensing agreements for the respective public utilities. Renegotiated agreements may cover some aspects of concession or licensing agreements and may contain formulas to adjust such agreements or temporarily amend them. The law includes the

possibility of agreeing upon periodic reviews, as well as the establishment of conditions regarding the quality parameters applied to services. Law No. 25.972 extended the emergency renegotiation period until December 31, 2005.

Regulatory authorities. The provision of telecommunications services is regulated by the Secretary of Communications and supervised by the National Communications Commission, subject to the participation in certain cases of the Under Secretary of Competition, Deregulation and Consumer's Defense (the Sub Secretaria de la Competencia, la Desregulacion y la Defensa del Consumidor).

Licenses. The licenses, all granted for an unlimited period of time and held by Telefonica de Argentina S.A., and the regulations that govern them are:

- Decreto 2344/90: Licence to provide fixed line telecommunication services.

- Decreto 2346/90: License to provide international telecommunications services, including telex and data transmission.

- Decreto 90/99: License to provide local, long distance, international and data transmission telecommunication services in the northern region.

- Res 1995/95: License to provide international telex services.

- Resolucion SC 16/01: License to provide Internet access and international data transmission services.

- Res SC 59/01: License to provide data transmission.

- Res SC 225/03: License to provide transmission of television signals.

Interconnection. Decree No. 764/00 approved new rules for national interconnection and established interconnection standards and conditions to which telephone service providers must comply without affecting pre-existing agreements.

The rules for national interconnection set forth the basic principles to be taken into account regarding interconnection among operators such as who will be able to agree on tariffs and service terms and conditions on a non-discrimination basis, provided that they comply with certain minimum obligations.

The regulations also establish the obligation for dominant and significant power operators to unbundle their local loops (physical link and its capacity between the carrier's capacity and the clients' facilities) and to allow competitors the use them on the basis of technical reasonability. As of the date of this Annual Report, the working group in charge of setting reference rates for this service has not been created.

Rates. Decree No. 764/00 established that providers of telephone services may freely set rates and/or prices for their services, which shall be applied on a non-discriminatory basis. However, until the Secretary of Communications determines that there is effective competition for telecommunications services, the "dominant" providers in such areas, which include Telefonica de Argentina, must respect the maximum tariffs established in the general rate structure. Below the values established in such tariff structure, such providers may freely set their rates by areas, routes, long distance legs and/or customer groups.

The guidelines set forth in article 26 of Decree 1185/90 are still applicable for operators with significant market power. These established the information obligations that operators have with regard to the tariffs, both to clients as well as to the regulation authority. This decree also establishes the powers that said authority has to revise and oppose said tariffs.

The Public Emergency Law converted these tariffs into pesos at a rate of one peso per one U.S. dollar and provided that the Argentine government would renegotiate the tariff regime.

Competition

Telecom Argentina, Compania de Telefonos del Interior S.A., an affiliate of Telmex, and Compania de Telefonos del Plata S.A., an affiliate of Bell South, were awarded licenses to provide the same basic telephone services throughout Argentina as of October 10, 1999. Since November 2000, other principal competitors, including Impsat Corp. and AT&T, have also entered the market, as well as smaller regional competitors.

Peru

Telefonica del Peru

At December 31, 2004, Telefonica del Peru was the leading global telecommunications operator in Peru based on number of customers, according to information provided by its competitors and regulatory authorities. Telefonica del Peru offers fixed local and domestic and international long distance services throughout Peru as well as a wide range of other telecommunications services including public telephone, cable television and data communications.

On December 17, 2003, Telefonica del Peru's Board of Directors approved a resolution to apply for the delisting of Telefonica del Peru's ADSs from the NYSE. On March 1, 2004 Telefonica del Peru's delisting application was approved and the ADSs ceased trading on the NYSE. Following the delisting, holders of ADSs were given an opportunity to exchange their ADSs for the underlying ordinary shares at a ratio of ten ordinary shares for each Telefonica del Peru ADS. The Class B Shares trade on the Lima Stock Exchange.

In 2000, we completed an exchange offer for the Telefonica del Peru shares and ADSs held by minority investors. Following our acquisition in September 2001 of an additional 10% interest in Telefonica del Peru Holding from Wiese Telefonica S.A. and IGM Telefonos, S.A. for a total of (euro)227.3 million, we held an approximately 97.07% interest in Telefonica del Peru at December 31, 2004.

At December 31, 2004, Telefonica del Peru had approximately 96.4% of the local telephone lines in Peru, according to information provided by its competitors and regulatory authorities, or 2.4 million lines including broadband lines and public telephone lines operated by Telefonica del Peru. Additionally, Telefonica del Peru had 389,174 pay television subscribers.

Telefonica del Peru had 205,400 ADSL and cable modem subscribers at December 31, 2004, a 126.5% increase compared to 90,700 subscribers at December 31, 2003. The ADSL penetration rate for the market in Peru was 7.8% at December 31, 2004.

At December 31, 2004 the degree of digitalization of Telefonica del Peru's network reached 96.5%.

Under a management contract between Telefonica Latinoamerica and Telefonica del Peru, Telefonica Latinoamerica provides Telefonica del Peru with management and technical support in exchange for management fees equivalent to 1% of Telefonica del Peru's total revenues. This contract expires in 2014.

On April 15, 2003, OSIPTEL introduced the multicarrier dial-up service for the long distance market. This system allows callers to freely select the operator they want to use for each call. Each operator has a predetermined number that the caller dials as a prefix to the call. This service favored the entrance of new operators with lower long distance tariffs. In the domestic and international long distance market, in 2004 Telefonica del Peru had 72% and 58% estimated market shares, respectively, with AT&T and Americatel as its main competitors. Within the Lima metropolitan area, Telefonica del Peru had approximately 99% market share, according to its estimates, with AT&T its only competitor. Telefonica del Peru is the leading provider of public telephone service with AT&T and Bellsouth as its main competitors. In addition, Telefonica del Peru provides cable television in the Lima metropolitan area and seven other cities through its wholly owned subsidiary, Telefonica Multimedia S.A.C.

Regulation

The Telecommunications Act (Texto Unico Ordenado de la Ley de Telecomunicaciones) approved in 1993 (DS 13-93-TCC) and the General Regulations implementing the statute, approved in 1994 (DS 6-94-TCC 1994) are the legal framework for the telecommunications sector in Peru.

Licenses and Concessions. Telefonica del Peru provides telecommunications services based on concessions granted by the Ministry of Transport and Telecommunications. The concession term is for twenty years, which may be renewed totally or partially at Telefonica del Peru's request. Total renewal is for a further twenty year period. Partial renewal is for periods of up to five additional years. Once a regulated operator chooses either a partial or total renewal modality, they cannot switch. Telefonica del Peru selected a partial renewal modality, which will allow Telefonica del Peru to renew its term every five-years from the effective date, up to a maximum of 20 years. Under the terms of Telefonica del Peru's concession contracts, The Ministry of Transport and Telecommunications may choose not to renew or extend Telefonica del Peru's contracts if it has repeatedly not complied with the terms of its concessions contracts as determined by the Peruvian government. A partial renewal of five years was approved by Ministry Resolution No 272-92 dated June 21, 1999, extending the concession term until 2019.

In December 2003, Telefonica del Peru petitioned the government for a five-year extension of its concession contracts from 2019 to 2024. On June 2004, the Ministry of Transport and Telecommunications notified Telefonica del Peru of its recommendation not to renew the concession contracts for an additional five-year period. As of the date of this Annual Report a final decision has not been issued. If the request for extension is denied, then Telefonica del Peru may again petition for the additional five-year extension period from 2019 to 2024 in December 2008.

Rates. The tariffs of the services regulated following the period of limited concurrence must be approved by OSIPTEL in accordance with a price cap formula based on a productivity factor.

On July 19, 2004 OSIPTEL set the value of the productivity factor for the 2004 to 2007 period at an annual rate of 10.1% and 7.8% for local and international calls, respectively. The productivity factor set is applicable until August 31, 2007. A review process shall be put in place every three years.

Interconnection prices. The interconnection charges have displayed a decreasing trend. Except for charges for call termination in local fixed network, which are set on the basis of costs, charges were established using the international comparison method. However, OSIPTEL has initiated several administrative procedures to set new interconnection charges for several services.

Telefonica Larga Distancia de Puerto Rico

At December 31, 2004, we held a 98.0% interest in Telefonica Larga Distancia de Puerto Rico, Inc., or TLD, which provides long distance telephone services in Puerto Rico.

In 2004, TLD's customers consumed 180 million minutes from TLD network, a 14.6% decrease compared to 211 million minutes in 2003.

Other Investments

Infonet Services Corporation

At December 31, 2004 we held a 14.4% economic interest and a 17.1% voting interest in Infonet Services Corporation, a data telecommunications firm that uses telecommunications tools to electronically link offices within a multinational company and to speed the transfer of information between them.

On November 18, 2004 Infonet agreed to merge with British Telecommunications plc. Pursuant to the merger, we sold all our interests in Infonet for U.S.$138.8 million on February 25, 2005.

Atrium Telecomunicacoes Ltda.

On December 24, 2004 Telesp agreed to acquire 100% of the shares of Santa Genovese Participacoes Ltd. Holding, which owns 100% of the shares of Atrium Telecomunicacoes Ltda. for R$113.4 million (approximately (euro)31 million). Atrium is a provider of integral telecommunications services for businesses in the city of Sao Paulo.

Telefonica Empresas America

During 2004, we implemented certain measures to simplify our business lines by integrating the former Telefonica Empresas business line's operations into the Spanish and Latin American fixed line businesses. Pursuant to this reorganization, the operations of Telefonica Empresas America, or TEA, and Telefonica International Wholesale Services, or TIWS, are now conducted by Telefonica Latinoamerica. See "--History and Development of the Company--Overview".

TEA is a holding company for operations in Latin America focused on corporate communication services, including voice services, private virtual networks, Internet connectivity, International data services, hosting and other company solutions.

After the spin off in 2001 of the data transmission operations of the integrated telecommunications operators in Brazil, Argentina and Peru into TEA and together with its other operations in Colombia, Mexico and the United States, Telefonica Empresas America offers a unique network platform for the provision of corporate data transmission services to multinational clients in Latin America.

TEA's strategy in each country depends on the status of development of its network and its market share. In those countries in which our Group holds a leading position, TEA concentrates on offering "one-stop shopping" services and customized communications solutions to corporate customers, with particular emphasis on value added services, such as hosting, content delivery and e-solutions. We refer to these markets as TEA's "incumbent markets". In those countries where TEA is a new entrant, TEA offers a complete portfolio of IP services and packaged solutions to the most attractive market segments, such as small and medium-sized enterprises, Internet service providers and other Telefonica Group companies. We refer to these markets as TEA's "expansion markets".

Incumbent Markets

TEA's incumbent markets include Brazil, Argentina, Chile and Peru. TEA manages operations focused on significant clients of the Telefonica Group. At December 31, 2004 TEA had 40,429 end user connections in Brazil, and approximately 13,931 in Argentina, 5,330 in Peru and 54,020 end user connections in Chile.

Expansion Markets

TEA's future markets where it may seek to enter include Colombia, Mexico, Puerto Rico and the United States. At December 31, 2004, TEA had 5,826 end user connections in these expansion markets. Despite the commencement of operations at TEA data center in Miami in September 2001, which has enabled TEA to begin providing hosting services in the United States (principally in Florida), TEA's results of operations in these expansion markets were adversely affected by the decline of new technology companies and the economic recession in the United States.

Certain Agreements

In May 2003, TEA signed an agreement with Amadeus Data Processing to become their telecommunication partner supplier in the Latin American region. This agreement is based on a technological association principle by means both companies will benefits from sharing and developing business opportunities.]

In February 2003, Telefonica Data Brasil signed a 60-month agreement with Banco Santander to outsource its telecommunications services for voice, data and PABX for Banco Santander's 2,000 branches in the Brazilian territory.

Telefonica International Wholesale Services

In 2002, Telefonica Data's international network included the international data transmission services and the international services integrated in Telefonica DataCorp. During 2003, Telefonica DataCorp transferred its international network to Telefonica International Wholesale Services (TIWS), a new business line of the Telefonica Group. TIWS was created to become a global wholesale operator of data, voice and capacity.

Since 2003, TIWS is the business unit responsible for other telecommunications operators and for managing the Group's international services and the network which supports these services.

Internet Portal Business--Terra Networks

Our worldwide Internet portal business is led by the Terra Networks Group. The Terra Networks Group provides a leading Internet portal to Spanish and Portuguese-speaking markets throughout the world.

We created Terra Networks in December 1998 to operate the Spanish residential and small office/home office Internet access business carried on by the Telefonica Group since December 1995. In November 1999, Terra Networks, S.A. completed an initial public offering of approximately 30% of its ordinary shares. In 2000, Terra Networks, S.A. acquired 100% of Lycos, Inc. in a stock-for-stock exchange. On May 28, 2003, we launched a tender offer for 100% of the outstanding shares of Terra Networks, S.A. that we did not own. As a result of the tender offer, closed in July 2003, we owned 71.97% of the total capital stock of Terra Networks. In December 2003 the Board of Directors of

Terra Networks, S.A., approved the acquisition of 4.41% of the capital stock owned by Citibank, N.A., as the agent bank for the stock option plans assumed by the company as part of the integration of the Lycos, Inc. As a result, in December 2003, we held 75.29% of the total capital stock in Terra Networks. During 2004, we purchased 3,321,048 shares of Terra Networks in the open market. As of February 23, 2005 we directly held 75.87% of Terra Networks' outstanding share capital.

On February 23, 2005, Terra Networks S.A.'s Board of Directors approved our merger proposal which is now subject to approval by shareholders at the annual general shareholders' meeting of both companies. At the same meeting Terra Networks' Board of Directors also approved the proposal to pay a dividend in the amount of (euro)0.60 per Terra Networks share, subject to the approval by Terra Networks'shareholders at the annual general shareholders' meeting. Payment is expected to be made during the days following the annual general meeting and, in any event, before the merger of Telefonica and Terra is consummated.

Terra Networks offers a suite of Internet services in a variety of languages that provides its users throughout its core markets in Europe, Latin America and North America with:

- access to the Internet (in Spain and certain countries in Latin America);
- portal and network services that incorporate a wide variety of individually tailored content for each market and featuring enhanced functionality;
- a range of online advertising, marketing and e-commerce opportunities;
- multiple solutions for customers' Internet needs, such as web design and hosting and communication; and
- consulting services such as web audit, web rationalization and web maintenance.

Through its portals and network of websites and joint venture partnerships, the Terra Networks Group has one of the largest global footprints of any Internet portal or network, with portals in 27 countries. The Terra Networks Group currently holds a leading position in the following markets: Spain, Latin America and the U.S. Hispanic market. Through its joint ventures and other interests, the Terra Networks Group also holds an important position in Europe (Lycos Europe) on a pan-regional basis. The Terra Networks Group is also a leading interactive services provider in Spain and Latin America, offering Internet access and local language interactive content and services to more than six million pay customers in Spain, Brazil, Mexico, Peru, Chile, the United States and Central America. In 2004, the Terra Networks Group was one of the leading broadband services and content providers in Spain and Brazil. Terra Networks ended 2004 with a total of 1.8 million pay access subscribers, including 1.1 million ADSL subscribers, 66% more than the previous year.

In the first half of 2004, Terra Networks restructured its operation to provide for increased operational flexibility and enhance its ability to focus on its customers. As part of this restructuring, Terra Networks reduced its operations in countries in which Telefonica does not conduct significant operations, particularly the United States and Mexico. In connection with the restructuring, personnel expenses have been significantly reduced and headcount has been reduced from 2,255 at year-end 2003 to 1,606 at year-end 2004.

The Terra Networks Group's business model has changed over the years to suit prevailing market conditions in general and the Internet industry in particular. An example is its access business, which in 2001 abandoned its strategy of offering free access and began offering pay access. In 2002 and 2003, Terra Networks focused on ADSL and broadband access, particularly in Spain and Latin America.

In June 2004, Terra Networks approved the payment of a cash dividend of (euro)2.0 per Terra Networks share. The payment of (euro)1.1 billion was made on July 30, 2004.

In October 2004, Terra Networks, S.A. sold its interest in Lycos to the Korean group Daum Communications Corp. Prior to the sale, Lycos transferred to Terra Networks, among other assets, the shares it held in Terra Networks USA, LLP (a subsidiary concerned with operating the portal for Spanish speaking people in the United States) and its stake in Lycos Europe, N.V. The sale price of the Lycos assets sold to Daum Communications was U.S.$108 million.

Strategic Alliance with Terra Networks

On February 12, 2003 we and Terra Networks entered into a Strategic Alliance Framework Agreement to replace the strategic agreement dated May 16, 2000 to which Bertelsmann AG was also a party. Under this agreement, we guaranteed Terra Networks at least (euro)78.5 million per year through the purchase of advertising by members of the Telefonica group. In 2003 and 2004 we generated the minimum value per year under the agreement.

Affiliated Companies of Terra Networks

Banking--Uno-e (BBVA)

The BBVA Group and the Terra Networks Group hold interests in Uno-e Bank, S.A.'s share capital of 67% and 33%, respectively. See "--Other Lines of Business--International Strategic Partnerships--Our Strategic Alliance with Banco Bilbao Vizcaya Argentaria--Uno-e Bank".

Travel-Rumbo/One Travel (Amadeus)

In July 1999, Terra Networks agreed to create a 50-50 joint venture with Amadeus Global Travel Distribution, S.A., a global leader in the travel industry that operates travel reservation and distribution systems. The purpose of the joint venture is to develop a website for travel and tourism related services targeted at the Spanish and Portuguese speaking markets. In September 2000, Terra Networks launched Rumbo in Spain through this joint venture. In 2001, the Terra Networks Group launched Rumbo in Argentina, Brazil and Mexico, and in 2002, Terra Networks launched Rumbo in Chile, Colombia, Venezuela, Uruguay and Peru. In March 2003, Rumbo signed an agreement with Despegar.es, another Spanish travel website, to manage its website. At December 31, 2004 Terra Networks had investments of (euro)7.5 million in Rumbo and had provided financing in the form of loans in the amount of (euro)3.8 million. In February 2005, Terra Networks agreed to sell its entire 54.1% interest in One Travel.com, Inc., for U.S.$25.5 million, payable in specified installments over a one-year period.

Location services-Maptel Networks

In January 2001, Terra Networks acquired Maptel Networks, a leading provider of location and cartographic content in Spain. Maptel Networks develops web and wireless location-based solutions and provides consultancy services in different areas: Geomarketing, Geographical Information Systems (GIS), Fleet Management, and Customer Relationship Management (CRM). These services are based on Maptel's own cartography and technology, and are being used for a broad range of customers in different sectors of activity. At December 31, 2004 Terra Networks had invested a total of (euro)2.4 million and had provided financing in the form of loans in the amount of (euro)3.3 million to Maptel Networks.

E-learning-Educaterra

Educaterra, a wholly owned subsidiary of the Terra Networks Group, is the exclusive e-learning services provider of the Telefonica Group, providing solutions for the residential market and the corporate market. During 2002, Educaterra.com was launched as the Terra Networks Group's exclusive e-learning vertical channel.

73

Educaterra.com currently operates in Spain, Brazil, Mexico, Argentina and Uruguay, and Terra Networks plans to make it available in several other Latin American countries. The portal provides a wide range of e-learning content in languages, IT, tutoring support, "edutainment", parent school and officeware, and other areas, with more than 25,000 hours of content in Spanish. At December 31, 2004 Terra Networks had invested a total of (euro)6.3 and provided financing in the form of loans in the amount of (euro)0.5 million to Educaterra.

Recent Developments

In January 2005 Alestra (ATT) and Terra Networks reached an agreement pursuant to which Alestra would manage the Internet access service provided by Terra Networks in the Mexican market, while Terra Networks would continue to manage and market the portal www.terra.com.mx, and to provide e-mail and value added services to its Mexican access clients.

Content and Media Business--Telefonica de Contenidos (Formerly Admira)

Telefonica de Contenidos (formerly Admira) conducts our worldwide audiovisual content and media business. Telefonica de Contenidos develops and distributes audiovisual content through traditional media and new technology platforms.

During 2004, Telefonica de Contenidos continued divesting its non-strategic assets by selling its interests in Lolafilms, a Spanish motion picture production company, Rodven, a Venezuelan record company, Mediapark, a Spanish television channel production company, Radio Continental, an Argentine radio company owned by Atlantida de Comunicaciones, Radio Continental and is in the process of selling its interest in the company that holds the broadcasting rights for the Argentine national soccer league. On September 23, 2004 Telefonica de Contenidos sold its 5% stake in Pearson, p.l.c. for (euro)345 million.

Endemol Entertainment

In July 2000, we acquired 99.2% of Endemol Entertainment Holding N.V., or Endemol, one of Europe's leading television producers. Endemol develops and produces audiovisual programming for free-to-air television, pay television and the Internet. Endemol has produced reality television shows such as Big Brother, Fear Factor and "Operacion Triunfo".

Endemol has a very strong international network built by a combination of start-ups, acquisitions and joint ventures, with operations in 23 countries around the world.

With the further development of the Internet and increased capabilities of mobile telephony to provide new platforms suitable for delivering entertainment content that attract younger audiences (which are more appealing to advertisers) away from traditional television production, Endemol has refined its interactive strategy by focusing on brand development, bringing content to other channels by using Endemol TV brands and developing new content for other channels and platforms.

Endemol continues to develop its strategy of geographic diversification. During 2004, Endemol started operations in Russia and Chile and Endemol plans to expand into Asia.

Pay Television

On May 8, 2002, Telefonica de Contenidos entered into an agreement with Sogecable to integrate Via Digital with Sogecable.

On November 29, 2002, the Spanish government approved the merger of Via Digital with Sogecable, subject to the fulfillment of 24 general conditions and 14 conditions related to the exploitation of television broadcast soccer rights.

On January 29, 2003, Sogecable, Telefonica de Contenidos and we reaffirmed our commitment to the merger and signed a complementary agreement that adapts the May 2002 agreement to the conditions established by the Spanish government. Pursuant to this agreement, the conditions imposed by the government were accepted, although

in parallel the parties filed an appeal against five of the conditions. A plan implementing such conditions was agreed by the parties and was submitted to the Spanish government, who approved it on April 3, 2003.

Under the May 2002 and January 2003 agreements, the merger of Via Digital and Sogecable was structured as follows:

- A share capital increase of 23% in Sogecable has been offered to Via Digital's shareholders, which are principally Telefonica de Contenidos, Grupo Prisa and Groupe Canal + in exchange for 100% of their intests in Via Digital shares.

- After the share exchange, Telefonica de Contenidos held a higher stake than Grupo Prisa and Groupe Canal+ (16.4%). Telefonica de Contenidos agreed to suspend its voting rights for its shares exceeding 16.4% of Sogecable's shared capital. As a consequence, the corporate governance rights of the three reference shareholders in Sogecable will be equal.

- Telefonica de Contenidos has agreed not to dispose of its 16.4% stake in Sogecable also during the three year period following the share exchange.

- Telefonica de Contenidos, Grupo Prisa and Groupe Canal+ will have equal representation on the Board of Directors of Sogecable with the same number of members. Grupo Prisa proposed that the chairman of the board would be one of the board members appointed by Telefonica de Contenidos.

- Groupe Canal+ and Grupo Prisa agreed to maintain their existing shareholder agreement with respect to Sogecable, to which Telefonica de Contenidos will not be a party.

- Grupo Prisa, Groupe Canal+ and Telefonica de Contenidos, each underwrote and funded (euro)50 million of participative loans, for a total amount of (euro)150 million. These loans have a 10-year maturity and an 11% annual interest rate.

- Subordinated debt in an amount of (euro)175 million was offered to all of the Sogecable shareholders and we purchased (euro)172 million of such debt. This debt has a maturity of 9 years and the applicable interest rate is 10.3% per annum plus attached warrants equivalent to 1% of Sogecable's shares.

Following the merger on July 21, 2003, Sogecable, now integrated with Via Digital, launched its commercial offer under the brand "Digital+". At December 31, 2004, Sogecable had 2.1 million subscribers of which 0.4 were Canal+ analog subscribers.

Telefonica Servicios Audiovisuales and Hispasat

Through Telefonica Servicios Audiovisuales, we offer audiovisual transmission services, production services and systems integration services to the television industry. Telefonica de Contenidos also holds a 13.2% interest in Hispasat, a Spanish satellite communications system.

Antena 3

At our annual general meeting of shareholders held on April 11, 2003, our shareholders approved the distribution of up to 50,000,400 shares of Antena 3 held directly by us, representing 30% of the outstanding share capital of Antena 3. On April 30, 2003, our Board of Directors decided, as approved by the general meeting of shareholders held on April 11, 2003, to accept an offer made by Grupo Planeta for 25.1% of the Antena 3 shares for (euro)364.0 million. In November 2003 we sold our remaining 4.17% holdings in Antena 3 through a block trade for (euro)95.7 million. The Onda Cero Radio Network was also sold along with the sale of Antena 3.

Other Lines of Business

Directories Business--Telefonica Publicidad e Informacion (TPI)

Telefonica Publicidad e Informacion publishes, develops and sells advertising in telephone directories. In addition to printed directories, it offers directories online and in telephone-based format. Telefonica Publicidad e Informacion has operations in Spain, Brazil, Chile and Peru. In addition, Telinver is the Group's telephone directory subsidiary in Argentina. At December 31, 2004, we held a 59.9% interest in TPI. On April 7, 2005 TPI engaged in a capital reduction under which we increased our ownership interest in TPI to 61.1%.

Spain

Telefonica Publicidad e Informacion estimates its market share in the directory printing sector in Spain is 89%. Its core products are:

- Paginas Amarillas ("Yellow Pages"), an annual advertising directory containing certain information on companies, businesses and professionals in a particular geographical area, classified by sector, location and alphabetical order. The directory contained approximately 1.2 million listings and 295,600 paid advertisers at December 31, 2004. In 2004, 16 million copies were printed.

- In 2001, Telefonica Publicidad e Informacion introduced a new product known as Paginas Amarillas de Bolsillo ("Pocket Yellow Pages"), which has become TPI's most modern and manageable annual advertising directory. In 2004, a total of fifteen different pocket directories were published. This product is designed for use outside the home and permits the user to conveniently carry the directory.

- Paginas Blancas ("White Pages"), which includes residential, professional and business telephone numbers in a particular geographic area, classified by location and alphabetical order. The directory has been redesigned and new content and information has been added, offering information of general interest to users. During 2004, 60 different White Pages directories were published and 17 million copies printed. The number of advertisers in the White Pages reached 265,400 in 2004.

- Paginas Amarillas Online (PAOL) ("Yellow Pages Online") is one of the largest and most complete online databases of Spanish businesses in terms of number of listings. The number of advertisers in Paginas Amarillas Online reached 268,500 and the number of registered visits increased to 55.5 million in 2004. Paginas Amarillas Online also offers supplementary information, including job listings, international directory listings (with access to yellow page listings in other countries) and street guides to more than 400 Spanish cities.

- Servicio de informacion telefonica 11888 (operator-assisted directory assistance) is a directory assistance service launched in February 2003 that offers 24-hour operator-assisted information over the telephone for all companies, businesses, professionals, products and services located in the Yellow Pages. 11888 also include value added services, such as call completion and the ability to send information by fax or e-mail. In 2004, the company responded to 36.1 million calls compared to 22.3 million calls in 2003, an increase of 61.4% . Advertising revenues increased 14.7% to (euro)4.5 million. The services reached 259,000 advertisers.

- Business-to-Business Directories: In September 2004 a new vertical directory called Guia de la Hosteleria, was published specializing in listing Hotels & Catering businesses. In addition, the second edition of Guia de la Construccion, specializing in listing construction businesses, was published in December 2004.

- Europages, available in paper, CD-Rom and over the Internet, is the most comprehensive trans-European directory containing information on major European export companies, classified by activity and grouped by country of origin. The Europages are edited annually by Euredit. Telefonica Publicidad e Informacion is responsible for managing the advertising business and the distribution of the directory in Spain.

In May 1999, Telefonica Publicidad e Informacion entered into an agreement with Telefonica de Espana to publish, distribute, market and sell advertising in Paginas Blancas. Under this agreement, Telefonica Publicidad e

Informacion pays Telefonica de Espana a commission based on the revenues generated from advertising and is reimbursed for the costs associated with the Guias Basicas de Referencia ("Basic Guides").

Latin America

Brazil

Telefonica Publicidad e Informacion commenced its operations in Brazil in 1999. Telefonica Publicidad e Informacion published its first edition of yellow pages directories in 2001 under the name "GuiaMais" for the Brazilian cities of Sao Paulo, Guarulhos, Ribeirao Preto and Curitiba (Parana State), and, in 2002, it began publishing "GuiaMais" in Osasco-Barueri and the ABC region. In 2003, Curitiba's directories were not published because of short-term profitability concerns. In 2004, the first pocket directory in Sao Paulo city was launched. Telefonica Publicidad e Informacion also offers its directories online and in telephone-based format. According to our estimates, the website of GuiaMais is the most visited directory website in Brazil with 11.6 million registered visits in 2004, which is an 86.1% increase from 2003.

Telefonica Publicidad e Informacion also publishes a white pages directory in Sao Paulo. In July 2001, Anatel, the Brazilian telecommunications regulator, temporarily suspended Telesp's obligation to distribute printed copies of white pages directories to its customers as long as it offers an alternative service and its customers do not request a printed copy. In 2004, Telefonica Publicidad e Informacion Brazil published a reduced white pages edition for the state of Sao Paulo, which did not include the listings for the city of Sao Paulo because Telesp did not publish such listings in 2004.

Chile

In early 2004, Telefonica Publicidad e Informacion acquired the 49% of Impresora y Comercial Publiguias, S.A., or Publiguias, for U.S.$80.4 million.

Publiguias is the leader of the Chilean directories market, with a market share of 96%. Publiguias publishes 10 yellow pages and white pages directories, with more than 51,800 advertising clients and 7.1 million copies printed. Additionally, in 2004 Publiguias published its first business to business directory. Santiago is the most important directory with more than 23,800 advertisers. Internet revenues have increased strongly due mainly to the commercial strategy implemented in the last years. The number of registered visits to Publiguias' Internet directory increased 14.8% to 5.5 million in 2004.

In 2001, CTC and Publiguias renegotiated their contractual framework and entered into an agreement to publish, distribute, market and sell advertising in the white pages directories. Under this agreement, Publiguias pays a fee of total advertising sold in the white pages and receives from CTC the costs associated with listing the telephone numbers. Under this contract, CTC will provide billing and collection services for its sales of advertising and will receive a percentage of the revenues generated by Publiguias as a result of such sales. In addition, Publiguias will pay CTC a variable fee based on the number of individual updates to the to telephones numbers listings.

In early 2001, the Chilean regulatory authority modified the requirement to publish and distribute annually white pages directories to customers. As a result, white pages directories are only required to be published every two years with a supplement being distributed in the year of non-publication. Publiguias and CTC agreed that this new regulation applied only with respect to the distribution of residential white pages directories in Santiago, Chile. In 2003, Publiguias published an addendum to the Santiago residential white pages directories, and in 2004, it published a complete directory.

Peru

Telefonica Publicidad e Informacion purchased the directory publishing business of Telefonica del Peru in February 2002 for U.S.$36.3 million. Telefonica Publicidad e Informacion is the only publisher of directories in Peru due to the acquisition of Comunicaciones Moviles del Peru from BellSouth in October 2004. TPI Peru publishes white pages and yellow pages directories in Lima, and in central, northern and southern Peru. The twelve different directories published have over 34,400 advertisers with more than 20,800 in Lima's directory. Peru also

has an online version of its directories, the number of visits in 2004 increased 80,5% to 4.8 million. TPI Peru reached an agreement in 2002 with Telefonica del Peru to publish, distribute, market and sell advertising in the white pages directories. Under this agreement, TPI Peru pays a commission based on the revenues generated from advertising and receives the amount of the costs associated with the basic guides plus a margin for their management.

Argentina

Telinver edits, publishes, distributes and sells advertising in telephone directories (22 different directories of white and yellow pages) in every local area served by Telefonica de Argentina. The company also publishes an industrial yellow pages directory and 4 neighbourhood directories with shopping listings. Since 1997 has offered its directories on CD-ROM.

In addition, Telinver offers white and yellow directories and e-commerce services through the online portal of "Paginas Doradas," which received 9 million visits in 2004.

In August 2004 Telinver launched *2424, a live-operator directory service for mobile clients.

Call Centers--Atento

We formed Atento in 1999 to develop our call center business. Atento offers integrated telephone assistance services as well as sophisticated "customer relationship management" services such as the development and implementation of customer loyalty programs, telemarketing services and market research. In addition, Atento rents contact centers, and provides staff for such centers, to third parties. At December 31, 2004, Atento operated more than 40 contact centers and had 30,566 contact center personnel in 12 countries on three continents, including Europe (Spain), Latin America and Northern Africa (Morocco).

In December 2001, Banco Bilbao Vizcaya Argentaria agreed to transfer its domestic and international contact center business to Atento. In May 2002 we created Atento N.V. a new holding company for our contact center operations. We contributed to Atento N.V., our entire contact center business in Spain and overseas.

In October 2003 the Sociedad General de Participaciones Empresariales ("GPE"), a subsidiary of Banco Bilbao Vizcaya Argentaria, we and Atento N.V., reached an agreement to allow BBVA to participate in Atento N.V.'s share capital. Also, in October 2003 specific agreements were reached to provide services to the BBVA in Spain and Portugal. Following this agreement, in November 2003, Atento N.V. carried out a capital increase fully subscribed in cash by us and GPE, representing 8.65% of Atento N.V.'s share capital. Also in October 2003, BBVA and Atento N.V. signed a framework agreement for Atento to provide services for a four year period to BBVA.

International Strategic Partnerships

Portugal Telecom

On January 23, 2001, Telefonica Moviles, S.A., Portugal Telecom and its subsidiary PT Moveis agreed to create a joint venture to consolidate Telefonica Moviles' wireless businesses in Brazil with those of Portugal Telecom. On October 17, 2002, Telefonica Moviles, Portugal Telecom and PT Moveis entered into a Stockholders' Agreement and a Subscription Agreement that implemented the joint venture agreement signed in January 2001. Under this joint venture framework agreement, each of the Telefonica Group and the Portugal Telecom Group agreed to contribute to a 50-50 joint venture (Brasilcel) certain of its respective wireless businesses in Brazil, including interests in operating companies and holding companies.

During 2004 Telefonica, S.A. acquired an additional 52,820,862 shares of Portugal Telecom. Additionally, on December 29, 2004, Portugal Telecom reduced its capital by retiring 87,799,950 shares of treasury stock, representing 7% of its capital stock. As a result of these transactions, Telefonica increased its interest in Portugal to 9.58% at December 31, 2004.

Mobipay

Telefonica Moviles is jointly developing with other telecommunications companies a new, simple, fast, low cost and secure mobile payment system, under the Mobipay brand, to process automated transactions including vending machines, personal money transfers, micropayments and electronic invoicing. For a description of Mobipay and other m-pay initiatives, see "--Worldwide Wireless Communication Services--Telefonica Moviles--Services and products--M-payment".

Our Strategic Alliance with Banco Bilbao Vizcaya Argentaria

Uno-e Bank

In February 2000, we and Banco Bilbao Vizcaya Argentaria, S.A. entered into a strategic alliance agreement, which provided that the online bank, Uno-e, would be 49%-owned by Terra Lycos and 51%-owned by Banco Bilbao Vizcaya Argentaria, S.A. On May 15, 2002, Terra Networks, S.A. and Banco Bilbao Vizcaya Argentaria, S.A. agreed to merge Uno-e Bank, S.A. with Finanzia Banco de Credito, S.A. a wholly owned subsidiary of Banco Bilbao Vizcaya Argentaria, S.A. On January 10, 2003, Terra Networks, S.A. signed a liquidity contract that replaced a previous agreement. The liquidity contract grants Terra Networks a put option to sell its interest in the merged entity to Banco Bilbao Vizcaya Argentaria, S.A. between April 1, 2005 and September 30, 2007. The sale price will be the greater of (i) the value determined by an investment bank; or (ii) the value calculated by multiplying Uno-e's last year earnings by BBVA's price-to-earnings ratio (PER). Additionally, the contract provides that if Uno-e does not obtain the planned ordinary revenue and earnings before taxes, the aggregate market value of the shares Terra Networks, S.A. owns cannot be evaluated at less than (euro)148.5 million.

In an extraordinary general shareholders' meeting of Uno-e Bank S.A. held on April 23, 2003, Terra Networks, S.A. and BBVA unanimously approved (subject to the required approval by Banco de Espana) a capital increase in Uno-e Bank S.A. to be wholly subscribed by Finanzia Banco de Credito, S.A. (a wholly owned subsidiary of BBVA) through the contribution of its private consumer finance business. Finanzia Banco de Credito, S.A. also held an extraordinary general shareholders' meeting on the same date, which approved the contribution and subscription for shares in the capital increase. As a result of the capital increase in June 2003, the consumer finance business has been integrated into the shareholding structure of Uno-e Bank, and the respective stakes of the BBVA group and Terra Networks after the capital increase were 67% and 33%, respectively.

Seasonality

Our main business is not significantly affected by seasonal trends.

Patents

Our business is not materially dependent upon the ownership of patents, commercial or financial contracts or new manufacturing processes.

C. ORGANIZATIONAL STRUCTURE

Please see "--History and Development of the Company--Overview".

D. PROPERTY, PLANT AND EQUIPMENT

Spain

Fixed lines

In order to provide residential and other telecommunication services in Spain, we operate a full telecommunication services network. We benefit from an intensive capital investment plan carried out over the last decade, which focused on network expansion as well as network upgrading. As a result, we now have:

- A network consisting of fiber optical cable to the curb in every Spanish city with a population of more than 50,000 inhabitants.

79

- Switching including synchronous digital hierarchy.

o An asynchronous transfer mode rollout (ATM).

- System 7 signaling throughout (used for commutation circuits networks).

Our infrastructure development objective is to achieve a fully digital system which allows simultaneous voice, data, text, and image transmission, and which permits cost-efficient network management and maintenance. Consistent with this aim, we are moving towards a simplified two-level hierarchical network through the use of remote units, and we are presently increasing operational efficiencies through centralization of our network supervision and management functions. The local digitalization rate in our network has increased from 56.7% in 1995 to 94.2% as of December 31, 2004, and our long distance lines are now 100% digitalized.

In carrying out our infrastructure development program, we have increased the use of fiber optical cable in our network.

The following table shows the total length of the four basic types of cable used in our network:

	At December 31,		
	2004	2003	2002
Coaxial cable (Km.)	2,444	2,457	2,468
Optical fiber cable (Km.)	75,888	64,934	60,932
Copper cable in interurban links (Km. aerial cable)	59,324	56,492	56,753
Copper cable in subscriber networks (Km. per urban zone)(1)	70,361	69,854	69,148

----
(1) Transmission cables in the subscriber networks contain a variable number of conducting filaments, which are isolated from each other and grouped in pairs. Each such pair is called a "par".

The deployment of broadband infrastructure at December 31, 2004 is as follows:

	At December 31, 2004
ADSL connections (in thousands):	2,490.11
ADSL lines over BTN:	2,360.17
ADSL lines over ISDN:	129.9
Switchboards with ADSL over BTN:	6.5 (regular switchboards) and 9.8 (remote equipment)
Switchboards with ADSL over ISDN:	1.2
Degree of DSLAM equipment occupation (%):	92%
Avarage time of retail ADSL service provision in PSTN and ISDN 11.87:	11.87
ADSL lines subscribed per 100 inhabitants:	5.8%

Our number of ADSL lines subscribed per 100 BTN and/or ISDN access lines at December 31, 2004 were as follows:

	Lines	ADSL	Coverage
BTN (thousands)	148.38	236.01	15.9%
ISDN	931.90	129.94	13.9%
Total	157.70	249.01	15.8%

The Spanish demography and topography presents significant challenges regarding the provision of basic telephony services throughout the country, especially to rural areas. Our continuous plan of rural expansion has been partly fostered by the Spanish local authorities. We are capable of using alternative technologies in order to extend the provision of services to remote and underpopulated areas according to our universal service obligations. Wireless access services were established in areas in which wireless service could be provided at a lower cost per customer that fixed line telephony services.

Wireless Networks

Telefonica Moviles Espana's digital network in Spain is based on the GSM standard, which has been adopted by more than 130 countries worldwide, including all member countries of the European Union. The wide acceptance of the GSM standard, together with its international roaming agreements, enables Telefonica Moviles Espana's customers to make and receive calls throughout Western Europe and in more than 200 countries worldwide. Telefonica Moviles Espana's GSM-based network provides its customers with access to many of the most advanced wireless services and a full portfolio of services and products. In addition, in 2001 Telefonica Moviles Espana launched a general packet radio services, or GPRS, which permits faster-based technology for the transmission of data and improved networks utilization.

In addition to continue increasing the GSM network's capacity in order to improve the network coverage quality in highly populated areas and allow for a more intensive use of its network inside offices in urban areas, Telefonica Moviles Espana has continued during 2003 rolling-out its UMTS network complying with its obligations under its UMTS license. In October 2003 Telefonica Moviles was the first mobile operator in Spain to launch a pre-commercial service based on UMTS technology.

Argentina

Telefonica de Argentina's properties consist of transmission plants and exchange equipment. Most of Telefonica de Argentina's properties are located in and around the Buenos Aires region.

As of December 31, 2004, the telephony service has approximately 4.3 million lines in service with approximately 25.1 million lines in service per each 100 inhabitants in the southern region.

Telefonica de Argentina's long distance service was provided mainly through a microwave network using analog lines and switchboards. As of December 2004, Telefonica de Argentina has built approximately 5,305 kilometers of optical fiber network, out of which 17,187 kilometers are located in the northern region and are dedicated to the provision of national long-distance services between the main cities, and another optical fiber network for the transmission of long-distance services between switchboards.

Brazil

Network and Facilities

Telesp's network includes installed lines and switches, an access lines network connecting customers to switches and trunk lines connecting switches and long-distance transmission equipment. As of December 31, 2004, our regional telephone network included approximately 14.2 million installed access lines, including public telephone lines, of which 12.5 million access lines were in service. At that time, of the access lines in service, approximately 74.8% were residential, 20.1% were commercial, 2.6% were public telephone lines and 2.4%

were for our own use and for testing. intraregional long-distance transmission is provided by a microwave network and by fiber optic cable. Telesp's network strategy is to develop a broadband integrated network that is compatible with several types of telecommunications services and multimedia applications.

The following table sets forth selected information about our network in aggregate, at the dates and for the years indicated.

	At and for year ende		
	2004	2003	2002
Installed access lines (in millions).............................	14.2	14.2	14.4
Access lines in service (in millions)(1)..........................	12.5	12.3	12.5
Average access lines in service (in millions).....................	12.3	12.4	12.6
Access lines in service per 100 inhabitants.......................	31.7	31.6	32.9
Percentage of installed access lines connected to digital switches.	98.7	96.9	96.1
Number of public telephones (in thousands)........................	331.2	331.1	330.9

----

(1) Data includes public telephone lines.

Technology

We are currently implementing the necessary infrastructure for the offering of "Wi-Fi", which is a wireless Internet access connection that offers mobility to our Internet clients.

As of December 31, 2004, Telesp'snetwork was approximately 98.7% digital.

Peru

In order to provide telecommunication services in Peru, Telefonica del Peru operates a telecommunications multiservice network. Over the last decade, a number of significant capital investments were made in order to enlarge the telecommunication's infrastructure and to provide the telecommunications network with the latest generation technologies. As a result, we currently have:

- A solid optical fiber and coaxial cable network.
- A communications network interconnected through signaling protocol number 7.
- An ATM network.
- A transmission network including SDH technology (synchronous digital hierarchy).

The objective while developing Telefonica del Peru's infrastructure is to achieve a completely digital system that allows for simultaneous voice, video, data and text transmission, and therefore obtains network management and maintenance efficiencies. According to this, our network is simplified to a two level hierarchy network through the use of remote units. We are also increasing our operating efficiencies through effective management of network centralization.

Telefonica del Peru's network is 96.5% digititalized, long-distance transmission is 100% digital in Lima and Callao and Telefonica del Peru's provincial network is 91.3% digititalized.

Plant digitalization:..	96.5%
Number of fixed lines in service(1):............................	2,155,648
Number of fixed lines set-up:...................................	2,307,247

----
(1) Includes public phones but excludes cellular public telephones.

Telefonica del Peru has increased the number of ISDN lines. As of December 31, 2004, Telefonica del Peru had approximately 54,634 ISDN lines.

Telefonica del. Peru's infrastructure development plan has increased the use of optical fiber into its network:

	At Decem		
Description	2000	2001	20
Coaxial cable (Km.)...	5,585	5,697	5,7
Optical fiber cable (Km.).......................................	6,508	6,728	6,7
Subscriber network (thousand Km.-pair)..........................	5,196	5,270	5,3

Chile

The principal plant and equipment of CTC Chile consists of outside plant and switching equipment and operating units that are located throughout the country. The Company's land and buildings principally consist of its telephone exchanges and other technical, administrative and commercial properties. At December 31, 2004, the Company's telephone plants and equipment represented 86.6% of its gross fixed assets (including depreciation);

82

construction in progress represented 1.8 %, land and buildings represented 6.0%, and furniture, office equipment and other assets represented 5.4 %.

Substantially all of CTC Chile's telephone exchanges are situated within buildings owned by CTC Chile. CTC Chile also owns its corporate headquarters located at Avenida Providencia 111 in Santiago. This building, which houses CTC Chile's principal offices, was completed in October of 1996 and currently provides office space for the majority of the administrative and technical staff of CTC Chile and its subsidiaries. The assets of CTC Chile and its subsidiaries are insured, subject to standard deductibles and other terms and conditions, for all events of physical damage and loss of revenue resulting from service outages.

Wireless Networks

Telefonica Movile Chile owns, or controls through long-term leases or licenses, property consisting of plant and equipment used to provide wireless communication services.

Plant and equipment used to provide wireless communication consist of:

- o Switching, transmission and receiving equipment;
- o Connecting line (cables, wires, poles and other support structures, conduits and similar items);
- o Land and buildings;
- o Easements; and
- o Other miscellaneous properties (work equipment, furniture and plants under construction).

Satellite Communications

At present we have interests in two international satellite communications organizations or companies, including:

- o A 0.7% interest in Intelsat, the global satellite consortium; and
- o A 13.2% interest in Hispasat, the communications satellite company which carries the Digital + direct-to-home (DTH) satellite television service and operates a new satellite system in Brazil and Latin America (Amazonas).

We sold our 2.1% interest in Eutelsat, the European regional satellite company, in March 2004 to Nebozzo Sarl for (euro)44,833,236.

We sold our 0.7% interest in New Skies Satellites, the communications satellite company that was formerly part of Intelsat, in January 2005 to Zeus Holdings Limited for $7,839,088.

We have implemented a satellite IP-access platform, which has been in operation since February 2003. Telefonica currently provides broadband Internet and Intranet access with similar speed and performance as with the ADSL technology. This satellite platform is also providing VoIP services, which have been in operation since the second half of 2004.

Submarine Cable

We are also one of the world's largest submarine cable operators. We currently participate in 44 international underwater cable systems (13 of which are moored in Spain) and own 11 domestic fiber optic cables.

ITEM 5...OPERATING AND FINANCIAL REVIEW AND PROSPECTS

A. OPERATING RESULTS

Overview

We are involved in five principal lines of business:

- o Spanish fixed line business conducted through Telefonica de Espana;

- Mobile business conducted through Telefonica Moviles;
- Latin American fixed line business conducted through Telefonica Latinoamerica;
- Internet portal business conducted through Terra Networks; and
- Content and media business conducted through Telefonica de Contenidos.

Our two other lines of business are:

- Directories business conducted through Telefonica Publicidad e Informacion, S.A.; and
- Call center business in Europe (Spain), Latin America and Northern Africa (Morocco) conducted through Atento N.V.

In 2004, we improved many of our operating and non-operating line items, our customer base and net income increased and we achieved wider margins in most of our business lines. Our net income was (euro)2,877.3 million in 2004, (euro)2,203.6 million in 2003 and a net loss of (euro)5,576.8 million in 2002. Revenues from operations increased 6.8% to (euro)30,321.9 million in 2004 compared to (euro)28,399.8 in 2003 and (euro)28,411.3 in 2002. Operating profit in 2004 increased 14.3% from 2003, which had increased 25.8% from 2002. Operating profit before depreciation and amortization increased 4.9% from 2003, which had increased 7.5% from 2002. For further information on operating profit before depreciation and amortization, please see "Presentation of Financial Information--Non-GAAP Financial Information."

Our total managed client base increased 26.5% to 118.1 million in 2004 from 93.4 million in 2003, which was a 13.6% increase from 82.2 million in 2002. After the acquisition of Bellsouth's Latin American operators, our wireless operations had approximately 74.4 million managed customers at December 31, 2004, a 43.6% increase compared to 52 million managed customers in 2003. In addition, in 2004 our ADSL connections increased by 61% to 4.4 million, of which approximately 3 million are in Europe and the rest in Latin America. In 2003 our ADSL connections had increased by 81.8% to nearly 2.7 million.

Our results for the year ended December 31, 2002 were affected by the loss in value of the Argentine peso and of the Brazilian real, given the strong weight of both countries in our business. Notwithstanding the economic recovery in Argentina in 2003 and 2004, our business is exposed to risks inherent in operating and investing in Latin America. Our results for the year ended December 31, 2002 were also affected by the commencement of the restructuring of our non-profitable businesses, principally Terra Networks' acquisition of Lycos, Inc. and Telefonica Moviles' UMTS operations in Europe.

We believe that our improved results for the year ended December 31, 2004 were due to substantial commercial efforts made in each of our business lines. Our client oriented management has allowed us to grow organically in our operations and to strengthen our position in key markets, although competitive pressures continued to affect our operations in 2004.

Presentation of Financial Information

The information in this section should be read in conjunction with our Consolidated Financial Statements, and the notes thereto, included elsewhere in this Annual Report. Our Consolidated Financial Statements have been prepared in accordance with Spanish GAAP, which differ in certain respects from U.S. GAAP. Please refer to note 25 to our Consolidated Financial Statements for a discussion of these differences.

Non-GAAP Financial Information

Operating profit before depreciation and amortization is calculated by excluding depreciation and amortization expenses from our operating profit in order to eliminate the impact of generally long-term capital investments that cannot be significantly influenced by our management in the short-term. Our management believes that operating profit before depreciation and amortization is meaningful for investors because it provides an analysis of our operating results and our segment profitability using the same measure used by our management. Operating profit before depreciation and amortization also allows us to compare our results with those of other companies in the telecommunications sector without considering their asset structure. We use operating profit before depreciation and amortization to track our business evolution and establish operational and strategic targets. Operating profit before depreciation and amortization is also a measure commonly reported and widely used by analysts, investors and other interested parties in the telecommunications industry. Operating profit before depreciation and amortization is not a measure of financial performance under Spanish GAAP or U.S. GAAP and may not be comparable to other similarly titled measures for other companies.Operating profit before depreciation and amortization should not be considered an alternative to operating profit as an indicator of our operating performance, or an alternative to cash flows from operating activities as a measure of our liquidity.

The following table provides a reconciliation of operating profit before depreciation and amortization to operating profit for the Telefonica Group for the periods indicated.

	Year end
	2002
	(in mil
Operating profit before depreciation and amortization........................	11,724.16
Depreciation and amortization expense..	6,692.42
Consolidated Operating Profit..	5,031.75

Significant transactions that affect the comparability of our results of operations in the periods under review

During 2002, 2003 and 2004 various changes occurred in the composition of the Telefonica Group that affect the comparability of our historical operating results. Please see note 2 to our Consolidated Financial Statements for a discussion of the principles of consolidation and a detailed description of the principal changes in the composition of the group affecting our financial statements during the periods under review covered by the Consolidated Financial Statements. The most significant changes are summarized below.

Year ended December 31, 2004

Portugal Telecom

During 2004 Telefonica, S.A. acquired 52,820,862 shares of Portugal Telecom, S.G.P.S., S.A. for (euro)475.1 million, giving rise to consolidation goodwill of (euro)344.5 million. Additionally, on December 29, 2004, Portugal Telecom reduced its capital by retiring 87,799,950 shares of treasury stock, representing 7% of its capital stock. Following these transactions, our interest in Portugal Telecom was 8.55%. The ownership interest of the Telefonica Group was 9.58% at December 31, 2004. This company continues to be accounted for by the equity method.

Tele Sudeste, Tele Leste, CRT and TCO

In October 2004, Brasilcel N.V. and Telesp Celular Participacoes, S.A. (TCP) completed friendly tender offers for Tele Sudeste Celular Participacoes, S.A., Tele Leste Celular Participacoes, S.A., Celular CRT Participacoes, S.A and Tele Centro Oeste Celular Participacoes, S.A (TCO)which required a cash payment of approximately R$607 million for Basilcel, N.V. and of R$902 million for TCP.

At June 30, 2004 Brasilcel N.V. acquired from NTT DoCoMo, Inc. and Itochu Corporation their ownership interests in Sudestecel Participacoes, S.A., a holding company with a 10.5% interest in Tele Sudeste Celular Participacoes, S.A. for (euro)20.8 million. As a result of this transaction, Brasilcel, N.V. increased its controlling interest in Sudestecel Participacoes., S.A. to 100%. Tele Sudeste Celular Participacoes, S.A. continues to be fully consolidated in the financial statements of the Brasilcel Group , and which in turn is proportionally consolidated in our Consolidated Financial Statements.

Telefonica Movil de Chile

On July 23, 2004, 100% Telefonica Movil de Chile, S.A. was acquired by Telefonica Moviles from the Chilean Compania de Telecomunicaciones de Chile, S.A., a subsidiary of Telefonica Internacional, S.A. The total amount paid for this acquisition was $1,058 million. As a result of this transaction, the Telefonica Group increased its effective ownership interest in the capital stock of Telefonica Movil de Chile, S.A. from 44.89% to 92.46%. This company continues to be fully consolidated in our Consolidated Financial Statements.

Acquisition of BellSouth's Operations in Latin America

On March 5, 2004, Telefonica Moviles, S.A. reached an agreement to acquire the BellSouth Corporation's interests in its wirelessoperators in Argentina, Chile, Peru, Venezuela, Colombia, Ecuador, Uruguay, Guatemala, Nicaragua and Panama.

BellSouth's interests in the operators located in Ecuador, Guatemala and Panama were transferred on October 14, 2004 and its interests in the operators located in Colombia, Nicaragua, Peru, Uruguay and Venezuela were transferred on October 28, 2004. BellSouth's interests in the operator in Chile were transferred on January 7, 2005, and BellSouth's interets in the Argentine operator were transferred on January 11, 2005.

Under the transaction agreement, the operators were valued at $5,850 million. The total acquisition cost for Telefonica Moviles, adjusted for the acquired companies debt assumed by Telefonica Moviles, amounted to (euro)3,252.5 million in 2004 (excluding Chile and Argentina, which were acquired in 2005).

Following the closing of the acquisitions and pursuant to the terms of the transaction agreements, Telefonica Moviles launched public tender offers to acquire the minority shareholdings that remained outstanding. The price offered in these transactions was equal to the paid under the BellSouth trasaction agreements.

Sale of Pearson Plc

In 2004, Telefonica, S.A. sold 38,853,403 Pearson Plc shares representing 4.84% of its capital stock for approximately (euro)350 million, giving rise to a loss of (euro)33.23 million

Additional Acquisition of Impresora y Comercial Publiguias, S.A.

In 2004, Telefonica Publicidad e Informacion, S.A., acquired the remaining 49% of the shares of its Chilean subsidiary Impresora y Comercial Publiguias, S.A. for (euro)65.6 million, thereby increasing its ownership interest to 100%. A 9% holding was acquired from the Chilean company Compania de Telecomunicaciones de Chile, S.A., a Telefonica Group subsidiary.

Sale of Lycos Inc

On October 5, 2004, Terra Networks, S.A. and Daum Communications, Corp. reached an agreement for the sale of Lycos, Inc for $108 million, giving rise to a gain of (euro)26.2 million. Prior to the Lycos sale, as part of the agreement for this transaction, Lycos, Inc. transferred assets with a book value of (euro)332.9 million to Terra Networks, S.A.

Year ended December 31, 2003

Sale of Antena 3

On January 7, 2003, we and our subsidiary Telefonica de Contenidos exercised our call option rights to acquire 19,532,625 shares of Antena 3 de Television, S.A. from Banco Santander Central Hispano, S.A., representing 11.72% of its share capital. After this transaction, we held a 59.24% interest in the share capital of Antena 3 de Television.

Subsequently, we began a process of divesting our interests in Antena 3. On April 30, 2003, we sold 25.1% of the total share capital of Antena 3 to to the Planeta Group for (euro)364 million. On April 11, 2003, our shareholders approved a distribution of shares representing 30% Antena 3 de Television's share capital as a dividend in kind. In October and November of 2003, we sold all our remaining interests Antena 3 de Television on the market for (euro)95.72 million, resulting in a complete divestiture of our stake in Antena 3 de Television, S.A. These transactions have resulted in a recorded profit of (euro)392.29 million.

Tender Offer for Terra Networks

In July 2003, we concluded a tender offer for Terra Networks, S.A. by acquiring 202,092,043 of its shares for (euro)5.25 per share. Subsequently, Terra Networks acquired 4.41% of its capital stock owned by Citibank, N.A., as the agent bank for the stock option plans assumed by Terra Networks as part of its merger with Lycos, Inc. After these transactions we held 75.29% of the total capital stock in Terra Networks. During 2004, Terra Networks was fully consolidated in the Telefonica Group.

Acquisition of TCO

On April 25, 2003, Telesp Celular Participacoes, S.A. (TCP), which is 65.12%-owned by Brasilcel, N.V., acquired from the Brazilian company Fixcel 61.10% of the common voting stock of Tele Centro Oeste Celular Participacoes, S.A. (TCO), representing 20.37% of the TCO's total capital stock, for R$1,505.5 million. As a result of a subsequent tender offer TCP held 86.58% of the ordinary shares of TCO at December 31, 2003. In 2003, TCO was included in the consolidated financial statements of Brasilcel that, in turn, was included in the Telefonica Group using the proportional integration method.

Sogecable and Via Digital

In connection with the merger of Via Digital and Sogecable, S.A. in the first half of 2003, Telefonica de Contenidos, S.A. acquired interests representing 12.63% of the capital share of Via Digital for (euro)165.6 million. On July 2, 2003, Telefonica de Contenidos, S.A. subscribed to a capital increase of Sogecable, S.A., contributing the shares it owned in Via Digital and thereby acquired 22.23% interest in Sogecable. Via Digital, which was consolidated during financial year 2002 using the equity method, is no longer consolidated in our financial statements. In additionIn October of 2003, Telefonica, S.A. acquired 2,020,000 shares in Sogecable, S.A. for (euro)41.91 million, which increased our interest to 23.83%. These transactions resulted in a charge of (euro)607.23 million in amortization of goodwill. Sogecable, S.A. was consolidated in 2003 using the equity method.

Uno-e Bank

In 2003, our interest in Uno-e Bank decreased from 49% to 33% as a result of a capital increase by Uno-e Bank, which was fully subscribed by BBVA, Uno-e Bank's other shareholder. As a result of our decreased interest, Uno-e Bank was excluded from consolidation of the Telefonica Group in 2003.

Year ended December 31, 2002

Acquisition of Iberdrola

In March 2002, we completed our purchase of Iberdrola's interests in our Brazilian wireless operators, which we then subsequently contributed to Telefonica Moviles. The Brazilian wireless operators were fully consolidated in

87

our financial statements until they were contributed to Brasilcel, our joint venture with Portugal Telecom, after which they were consolidated under the proportional integration method

Sale of Prime Argentina

In June 2002, Telefonica de Contenidos sold its interest in Prime Argentina, which owned Azul Television, for U.S.$12 million, which resulted in extraordinary losses of (euro)162.8 million.

Acquisition of Pegaso

In September 2002, Telefonica Moviles acquired 65.23% of Pegaso PCS (Mexico) for (euro)92.9 million from the Burillo Group. Subsequently, Pegaso carried out a capital increase to which Telefonica Moviles subscribed for (euro)211.5 million, representing its proportionate 65.23% interest. Pursuant to the Pegaso acquisition, Telefonica Moviles agreed to combine its Mexican wireless operations with those owned the Burillo Group. Under the agreement, each of Telefonica Moviles and Burillo would combine their interests under a new holding company, Telefonica Moviles Mexico, with Telefonica Moviles holding 92% of the share capital and the remainder held by Burillo.

Sale of Uniprex and Cadena Voz

In September 2002, Telefonica de Contenidos, S.A. sold its interests in both Group Uniprex Onda Cero and Cadena Voz de Radiodifusion, S.A. Admira Group sold this equity to Antena 3 de Television Group, which gave rise to capital gains totaling (euro)35.8 million.

Incorporation of Brasilcel Joint Venture

On December 27, 2002, Telefonica Moviles and PT Moveis Servicos de Telecomunicacoes, SGPS, S.A. (PT Moveis), Portugal Telecom's affiliate, entered into a joint venture agreement under which each of Telefonica Moviles and Portugal Telecom contributed their Brazilian wireles operators to a newly formed company, Brasilcel. Under the joint venture agreement, Telefonica Moviles and Portugal Telecom agreed to purse their Brazilian wireless operations exclusively through Brazil incorporated Brasilcel, the 50/50 Joint Venture, by contributing 100% of their respective direct and indirect interests in the mobile communications companies in Brazil.

Other Events Affecting the Comparison of Our Results

Acquisition of UMTS licenses

In 2000 Telefonica Moviles, directly or through consortiums, with other international and local partners bid on and was awarded UMTS licenses in Spain, Germany, Italy, Austria and Switzerland. Most of these licenses were awarded in the second half of the year 2000. At the end of 2001 and in the beginning of 2002, although UMTS technology had not yet been developed to allow for commercialization of UTMS services, the prevailing conditions in these markets and the specific business plans for the development of these businesses allowed Telefonica Moviles to anticipate the recoverability of its investments already made and those planned for the future. Therefore, during the preparation of the year-ended 2001 financial statements, Telefonica Moviles compared the book value of the licenses to the financial projections included in the business plan and considered that it could recover the investments made up to that time.

However, Telefonica Moviles' business plans were based on assumptions that could not be realized in the future or would require adjustment. As a result of significant changes in the telecommunications market in 2002, Telefonica Moviles undertook to review its European strategy and to commission independent experts to assess its business plans of its UMTS operations in Germany, Italy, Austria and Switzerland.

Under US GAAP, according to SFAS 144, a long-lived asset (asset group) shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. In the case of Telefonica Moviles' investments in Germany, Austria and Switzerland, which it fully consolidates under Spanish and US GAAP, an impairment loss was recognized in 2002 based on the comparison between the carrying amount of each of the licenses and their respective fair values. Under US GAAP, the investments in these licenses were also considered not recoverable according to SFAS 144, their carrying value exceeded the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the licenses. These assessments were based on the carrying amount of the licenses at the date that they were tested for recoverability. The impairment loss was measured as the amount by which the carrying amount of each of the licenses exceeded its respective fair values.

With respect to Italy, Telefonica Moviles accounts for this investment under the equity method under Spanish GAAP and US GAAP.

General UMTS market conditions

During the first half of 2002 there were significant changes in the telecommunications market from a competitive, technological, financial and regulatory perspective. These changes caused Telefonica Moviles to review its European strategy and to commission independent experts to assess the business plans of its UMTS operations in Germany, Italy, Austria and Switzerland. The following is a summary of these changes:

- In a publication released in June 2002 from the European Commission on 3G technology, it became apparent that it was highly unlikely that there would be significant regulatory changes providing the conditions necessary to develop commercial applications for the UMTS licenses.

- As a result of the lack of commercial applications for the UMTS licenses, there was little incentive to build our the networks necessary to take advantage of 3G technology.

- The delay in commercial viability was also due to a delay in the availability of UMTS handsets. The availability of UMTS handsets was limited to a small number of prototype models with technical problems that made commercial distribution difficult. Problems with network equipment hardware and software also limited the viability of network coverage.

- Demand for 3G services was revised downwards as a result of a general decrease in demand for data services and ongoing delays in the availability of attractive applications using UMTS technology.

As the delay in commercially viable UMTS technology increased it also became apparent that incumbent operators's with strong established positions in the countries in which we had obtained UMTS licenseswould make it difficult for new market entrants, such as Telefonica Moviles, to attract customers and obtain market share.

Notwithstanding the foregoing, we believe that there are commercially feasible uses for UMTS technology, in makrets characterized by a reduced number of operators where we can obtain a minum market share in order to absorb the costs associated with the roll-out of 3G technology. Particularly as we have reduced our estimates of revenue per units served.

Telefonica Moviles' UMTS operations

Telefonica Moviles developed and implemented various initiatives directed at improving its business plans in the countries in which it was awarded UMTS licenses. These included, for example, roaming and network sharing agreements, non-recourse vendor financing and various commercial agreements. Telefonica also analyzed other strategic alternatives such as consolidation with other operators. Ultimately, it concluded that none of these alternatives were viable. As a result, Telefonica Moviles adopted the most appropriate decisions for each country as a function of the prevailing conditions in each market.

Germany. On the basis of the roaming and infrastructure sharing agreements with another German operator, Group 3G, our joint venture with Sonera, started operations as a GSM/GPRS virtual mobile operator, or VMO, at the end of 2001. GPRS, or general packet radio service, is the natural evolution of GSM towards 2.5G, allowing wireless voice and higher-speed data transmission. A VMO is a mobile operator that does not own a network and instead buys mobile minutes wholesale from existing network operators and sells them to its clients. Subsequently, and once the actual operational and financial results for two quarters of commercial operations as a 2/2.5G VMO in Germany became available, Telefonica Moviles realized that the results of Group 3G since the launch of commercial activity up to July 2002 were significantly lower than forecast. In addition, it was becoming apparent that the German wireless market was not growing as expected; the number of subscribers was forecasted to grow at less than

one percent in the first half of 2002. As a consequence, and after an in depth assessment of the expected evolution of these parameters with an independent third party report, it was concluded that continuing Telefonica Moviles' operations in Germany would not generate value for Group 3G's shareholders. Therefore, Telefonica Moviles and Sonera decided to halt all commercial operations in Germany.

Italy. After taking into consideration market conditions and given the differences in the regulatory environment in Italy, both with regard to compliance with coverage requirements included in the license and flexibility shown by the regulators, and the shareholder structure of IPSE 2000, in 2002 the shareholders of IPSE 2000 decided to postpone the launch of commercial operations and restructure the company.

Austria and Switzerland. In Austria and Switzerland, no relevant commercial agreements had been signed as of June 2002, including 2G roaming agreements, network sharing agreements and vendor financing; consequently, the activities of Telefonica Moviles' operations were substantially reduced in light of these circumstances, together with Telefonica Moviles' experience in Germany. Telefonica Moviles updated its business plans for both of these countries.

Based on the assessments obtained from independent experts, and taking into account that in Germany, Austria and Switzerland network coverage requirements included in the UMTS licenses would likely come into effect earlier than in Italy, and to ensure that its investments were correctly valued at all times, Telefonica Moviles decided to write down the entire amount of the book value of its investments in Germany, Austria and Switzerland.

The impact on our balance sheet as a result of the above-mentioned write-down was as follows:

Balance Sheet	Telefonica Group	Germany	Attributed to: Austria
		(thousands of euros)	
Book value before write-downs:			
Intangible assets (mainly licenses).....	9,445,386	9,278,565	128,963

Property, plant and equipment..........	87,559	60,943	6,428
Impairments:			
Intangible assets (mainly licenses).....	(9,445,386)	(9,278,565)	(128,963)
Property, plant and equipment..........	(84,296)	(57,843)	(6,364)
Book value after write-downs:			
Intangible assets (mainly licenses).....	0	0	0
Property, plant and equipment..........	3,263	3,100	64

With respect to Telefonica Moviles' investment in Italy, the UTMS license's terms and conditions made it possible to implement a business plan with lower investment than in the other countries and it was determined that the assignment of the right to use the 3Gspectrum was foreseeable. Consequently, Telefonica Moviles' did not fully write down its investment in IPSE 2000. Telefonica Moviles estimated the value of the UMTS license of IPSE 2000, S.p.A. to be (euro)300 million in 2002, (euro)136 million of which represented Telefonica Moviles' investment in IPSE 2000. As of December 31, 2004 Telefonica Moviles' investment in IPSE 2000 was valued at the same level.

Accordingly, at December 31, 2002 a net loss of (euro)5,049.8 million was recorded in Telefonica Moviles' combined financial statements associated with the write-down of assets and the restructuring of operations in these four countries. In our Consolidated Financial Statements this net loss was (euro)4,958.2 million.

Telefonica Moviles de Espana. Currently, Telefonica Moviles provides UMTS services in Spain through Telefonica Moviles Espana. On February 13, 2004, Telefonica Moviles Espana began offering to its corporate customers "Oficin@ Movistar UMTS". This service was extended to all Telefonica Moviles Espana customers in Madrid and Barcelona on May 24, 2004, and gradually extended to the rest of Spain. In addition, on May 24, 2004, Telefonica Moviles Espana launched the first UMTS video services in the Spanish market. We believe that to make large-scale launch of UMTS technology, UMTS compatible handsets that are small, reasonably priced, and have adequate battery life must become available.

The value of the UMTS assets on Telefonica Moviles Espana's balance sheet is not significant. It was awarded a license to provide UMTS services for (euro)131 million. The time required for Telefonica Moviles Espana to recover the value of its investments is significantly shorter than in other countries and the impact of the delay in the introduction of a commercially viable UMTS technology on Telefonica Moviles Espana's revenue forecasts is much lower than in other European countries.

Other markets. Considering the low level of maturity of the wireless industry in Latin America and Morocco and the adequacy of current technologies for servicing the communication needs of customers in the countries of these regions, we have not acquired UMTS licenses nor do we expect to introduce UMTS services in these other markets in the short term.

Economic situation in Argentina

Telefonica, like other telecommunications companies operating in Argentina, has been affected by the economic situation in Argentina. As of December 31, 2004, our total investment in Argentina amounted to (euro)989.2 million, including goodwill, intercompany financing and the assets assignable to our Argentine investments (includign losses attributable to our Argentine operations before the related tax effect).

As a result of the economic volatility in Argentina, our Consolidated Financial Statements for the year ended December 31, 2002 reflected an adverse impact on revenues from operations and on the "Stockholders' Equity--Translation Differences in Consolidation" caption of (euro)354.7 million and (euro)1,147.1 million, respectively, in 2002. No such adverse impact was recorded for the years ended December 31, 2003 and 2004.

Our operations in Argentina were affected by the devaluation of the Argentine peso, high inflation and other adverse macroeconomic conditions in Argentina and related legislative measures adopted by the Argentine Government in 2001 and 2002 to address the crisis, such as the Public Emergency Law enacted on January 7, 2002. During 2003 and 2004 the Argentine economy has stabilized and experienced signficant growth. Argentina's estimated GDP growth in 2004 was 8.8%, matching the growth rate in 2003. However, the effects of laws adopted during the economic crisis continue to affect the results of operations and financial condition of Telefonica de Argentina and Telefonica Comunicaciones Personales.

Our fixed line business in Argentina derives a majority of its revenues from regulated tariffs for telecommunication services. Prior to the enactment of the Public Emergency Law, those tariffs were linked to a rate per unit of usage expressed in U.S. dollars and could also be adjusted semiannually in accordance with variations in the U.S. consumer price index. However, the Public Emergency Law states that any tariff index clauses or any other index mechanism incorporated in the agreements executed by the Argentine government, including those agreements with telecommunication service providers, are void and not applicable. Any increase in inflation will thus result in a decrease in revenues from our fixed line business in Argentina in real terms, as tariffs are not adjusted for inflation. The consumer inflation rate increased by approximately 6.1%, below the target range of 7% to 11% established by Argentina's central bank, while wholesale prices rose by approximately 7.9% in 2004.

The Public Emergency Law also mandated "pesification" by stating that fixed line tariffs must be established in pesos using a Ps.1.00 per U.S.$1.00 exchange rate. Since our fixed line business in Argentina realizes substantially all of its revenues in pesos, any depreciation in the peso against the euro will negatively affect our results of operations since Telefonica de Argentina has not been allowed to alter its tarriffs in response to such depreciation. Exchange rates were stable in 2004. However, any future depreciation of the peso against the euro may have an adverse effect on our results of operations.

Telefonica Empresas

During 2004, we integrated the former Telefonica Empresas business line's operations into the Spain and Latin America fixed business lines. The operations of Telefonica Data Espana and Telefonica Soluciones are now conducted by Telefonica de Espana and the operations of Telefonica Data Latinoamerica and Telefonica International Wholesale Services (TIWS)are now conducted by Telefonica Latinoamerica. See "Item 4-- History and Development of the Company--Overview".

In order to facilitate comparison we have recalculated the analysis of certain results of our operations in 2003 and 2002 to account for the reorganization of our structure. The analysis and discussion of our results of operations for 2004 compared to 2003 uses the new structure and the analysis and discussion for 2003 compared to 2002 continue using the previous structure.

Significant Accounting Changes

In 2004 and 2003, there were no significant changes in the Group's accounting policies.

In 2002, under Spanish GAAP, pursuant to an ICAC resolution dated March 15, 2002, we recorded tax assets relating to tax relief and tax credits not yet taken for tax purposes but regarding which there is no doubt that they can be deducted in the future in accordance with generally accepted accounting principles. An asset of (euro)343.0 million was recorded as of December 31, 2002, pursuant to this resolution.

Critical Accounting Policies

Accounting for long-lived assets, including goodwill

Property, plant and equipment and intangible assets, other than goodwill (like licenses), are recorded at acquisition cost. If such assets are acquired in a business combination, the purchase price is the estimated fair value of the acquired property, plant and equipment or intangible assets. Property, plant and equipment are depreciated on a straight-line basis over their estimated useful lives, and licenses and other intangible assets are amortized based on the intangible asset's estimated capacity to generate revenues during the concession period.

Accounting for long-lived assets and intangible assets involves the use of estimates for determining: (a) the fair value at the acquisition date in the case of such assets acquired in a business combination, and (b) the useful lives of the assets over which they are to be depreciated or amortized.

When an impairment in the value of an asset occurs, nonscheduled write-downs are made. We assess the impairment of identifiable intangible and long-lived assets whenever there is reason to believe that the carrying value may exceed the fair value and where a permanent impairment in value is anticipated. The determination of whether the impairment of long-lived and intangible assets is necessary involves the use of estimates that includes but are not limited to the analysis of the cause of potential impairment in value, the timing of such potential impairment and an estimate of the amount of the impairment. We also consider technological obsolescence, discontinuance of services and other changes in circumstances that indicate the need to perform an impairment test. A significant change in the facts and circumstances that we relied upon in making our estimates may trigger the requirement of recording an impairment and may have a material adverse impact on our operating results and financial condition.

Goodwill in consolidation, which arises when the consideration paid for a subsidiary exceeds the subsidiary's underlying book value at the purchase date and such excess consideration is not directly allocable to the companies' assets, is amortized on a straight-line basis during the period in which such goodwill contributes to the obtainment of revenues by the company for which the goodwill was recorded.

Nonscheduled write-downs of goodwill are made when an impairment in the value of goodwill occurs. We review, on a regular basis, the performance of our subsidiaries. When there is reason to believe that the goodwill arising from the acquisition of that subsidiary is impaired and that the impairment is of a permanent nature, we compare the carrying amount of that subsidiary to its fair value. The determination of the fair value of a subsidiary involves extensive use of estimates and significant management judgment is involved. Methods commonly used by us for valuations include discounted cash flow methods.

A significant reduction in our estimate of the value of a subsidiary may result in the need to write down goodwill in consolidation which could have a material adverse affect on our operating results and financial condition.

We believe that the estimates we make to determine an asset's useful life are "critical accounting estimates" because: (1) they require our management to make estimates about technological evolution and competitive uses of

assets, and (2) the impact of changes in these estimates could be material to our financial position and results of operations. Management's estimates about technology and its future development require significant judgment because the timing and nature of technological advances are difficult to predict.

Deferred taxes

Management assesses the recoverability of deferred tax assets on the basis of estimates of our future taxable income. The recoverability of deferred tax assets ultimately depends on our ability to generate sufficient taxable income during the periods in which the deferred taxes are deductible. In making its assessment, our management considers the scheduled reversal of deferred tax liabilities, projected taxable income and tax planning strategies.

This assessment is carried out on the basis of internal projections which are updated to reflect our most recent operating trends. In accordance with applicable accounting standards, a deferred tax asset must be recognized when its future deductibility is more likely than not. Our current and deferred income taxes, and associated valuation allowances, are impacted by events and transactions arising in the normal course of business as well as in connection with special and non-recurring items. Assessment of the appropriate amount and classification of income taxes is dependent on several factors, including estimates of the timing and realization of deferred income tax assets and the timing of income tax payments. Actual collections and payments may materially differ from these estimates as a result of changes in tax laws as well as unanticipated future transactions impacting our income tax balances.

Preliminary Guidance on Differences Between IFRS and Spanish GAAP

We are required to prepare consolidated financial statements in accordance with IFRS from January 1, 2005. The opening IFRS consolidated balance sheet will be prepared for the period beginning January 1, 2004. The Committee of European Securities Regulators has recommended that selected IFRS financial information be disclosed in advance of publication of such IFRS financial statements. In line with this recommendation, we are providing a summary of certain of the expected differences in the preparation of our consolidated financial statements on the basis of IFRS. The following summary is not an exhaustive description of the effects of preparing our Consolidated Financial Statements under International Financial Reporting Standards, or IFRS compared to Spanish GAAP. Additional significant effects on our Consolidated Financial Statements may occur when they are prepared under IFRS due to new pronouncements from the International Accounting Standards Board (IASB) or pronouncements that are not endorsed by the EU prior to the preparation of our December 31, 2005 consolidated financial statements. The actual effects on our Consolidated Financial Statements from the adoption of IFRS may be different from those shown below for these or other reasons.

The information included in this Annual Report regarding the potential effects on our Consolidated Financial Statements from the adoption of IFRS are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and readers are cautioned not to place undue reliance on such information.

Total Shareholders' Equity

At December 31, 2004 our total shareholders' equity was (euro)16,225.1 million under Spanish GAAP. We have performed a preliminary analysis of how the adoption of IFRS will impact our total shareholders' equity. Based on this analysis, we estimate that the principal adjustments to our total shareholders' equity at December 31, 2004 under IFRS would result in a decline in our shareholders' equity of approximately (euro)3,729 million from (euro)16,225.1 million at that date under Spanish GAAP. This decrease would be principally due the adoption of accounting policies under IFRS that would require us to change how we measure the value of certain assets and liabilities and to change the timing of when certain revenues and expenses are recognized.

Principal Adjustments Affecting Our Shareholders' Equity Under IFRS

The principal adjustments that would affect our total shareholders' equity under IFRS as estimated are the following:

Goodwill and fair value adjustments in business combinations

Telefonica will adopt the exemption granted by IFRS 1 "First-Time Adoption of IFRS" to apply IFRS 3 "Business combinations" prospectively from the transition date and thus not to restate business combinations prior to January 1, 2005.

Under Spanish GAAP, goodwill and fair value adjustments are reported at historical exchange rates. Under IFRS these items are translated at the exchange rates prevailing at each balance sheet date.

IFRS permits certain intangible assets to be classified as having an "indefinite useful life," which is not permitted under Spanish GAAP. Under IFRS, goodwill and intangible assets with indefinite useful lives are not amortized, but are instead subject to an impairment test at least once a year. Under Spanish GAAP, goodwill and all intangible assets must be amortized over their useful lives.

Under IFRS, the cost of telecommunications licenses is amortized on a straight-line basis over their economic useful lives. Under Spanish GAAP, Telefonica's policy is to amortize its telecommunications licenses systematically over their useful lives, using patterns based on revenues generated or the average number of clients during such measuring period.

Based on our preliminary analysis, we estimate that these changes to our accounting policies would have reduced our total shareholders' equity at December 31, 2004 by approximately (euro)3,398 million.

Treasury shares and equity instruments

Under Spanish GAAP, treasury shares are classified as assets (except if held exclusively for subsequent cancellation pursuant to resolution approved at a general shareholders' meeting) and are measured at the lower of cost or market value. For IFRS purposes, treasury shares are deducted from total shareholders' equity and any related transactions are also deducted from shareholders' equity, rather than through our consolidated income statement.

For IFRS purposes, certain instruments issued to cover employee stock option plans are classified as shareholders' equity, since the agreements provide for the exchange of a fixed number of treasury shares for a fixed amount of cash. In addition, however, a liability is also recognized in the balance sheet under IFRS because the issuer is obligated to repurchase its own equity instruments.

Based on our preliminary analysis, we estimate that these changes would have reduced our total shareholders' equity at December 31, 2004 by approximately (euro)847 million.

Revenue recognition

Under Spanish GAAP, fees charged when customers connect to our network are recognized upfront, together with the related costs. Also, handset sales are recognized separately upon delivery.

For IFRS purposes, connection revenues are recorded together with the related revenues from handsets or other equipment to the extent that the aggregate of such equipment and connection revenues do not exceed the fair value of the equipment delivered to the customer. Any connection revenues not recognized together with the related equipment revenues are recognized over the period in which services are expected to be provided to the customer. Under IFRS equipment sales are recognized upon delivery to end customers.

Based on our preliminary analysis, we estimate that these changes to our accounting policies would have reduced our total shareholders' equity at December 31, 2004 by approximately (euro)347 million.

Income taxes

The accounting treatment for income taxes under Spanish GAAP requires the use of the income statement liability method, which focuses on timing differences between taxable profit and accounting profit. IFRS require the recognition of deferred taxes using the balance sheet liability method, which focuses on temporary differences between the tax base of an asset or liability and its carrying value on the balance sheet.

Based on our preliminary analysis, we estimate that these changes to our accounting policies would have reduced our total shareholders' equity at December 31, 2004 by approximately (euro)282 million.

Post-employment and termination benefits

Although provisions are required to be recognized for pension obligations under both Spanish GAAP and IFRS, differences in the measurement of the obligation exist between IFRS and Spanish GAAP. Under Spanish GAAP, part of the actuarial losses relating to these plans are deferred, provided certain circumstances are met, whereas under IFRS all actuarial gains and losses are recognized in the consolidated income statement in the year they are identified.

Based on our preliminary analysis, we estimate that these changes to our accounting policies would have reduced our total shareholders' equity at December 31, 2004 by approximately (euro)238 million.

Capitalized costs

Under Spanish GAAP, start-up costs are deferred and amortized over five years. Under IFRS, expenditures that do not meet the criteria for recognition as an asset are expensed as incurred.

Under Spanish GAAP, costs related to the issuance of equity instruments are also capitalized and amortized over five years. Under IFRS, capital increase expenses are charged against the gross proceeds of the new capital.

Under Spanish GAAP, research and development expenses are capitalized and amortized over three years from the date of completion of the internal project. Under IFRS research costs are expensed as incurred.

Based on our preliminary analysis, we estimate that these changes to our accounting policies would have reduced our total shareholders' equity at December 31, 2004 by approximately (euro)220 million.

Minority Interests

Under Spanish GAAP, minority interests are classified as a separate liability on the balance sheet but excluded from total shareholders' equity. Under IFRS, minority interests are considered as part of total shareholders' equity.

Additionally, under IFRS the preference shares issued by Telefonica's subsidiary Telefonica Finance would be reclassified from minority interests to liabilities as explained below.

Based on our preliminary analysis, we estimate that these changes to our accounting policies would have increased our total shareholders' equity at December 31, 2004 by approximately (euro)1,603 million.

Other Adjustments Affecting Our Shareholders' Equity Under IFRS

Financial reporting in hyperinflationary economies

Under Spanish GAAP, the restatement of financial statements for hyperinflation is required when it is required under local GAAP.

Under IFRS, a number of qualitative and quantitative indicators are analyzed to determine whether hyperinflation exists, and therefore whether financial statements should be restated in terms of the measuring unit current at each balance sheet date. Under IFRS, of the countries in which we operate only Venezuela is considered to be a hyperinflationary economy.

Definition of associate: significant influence

For Spanish GAAP purposes, significant influence is presumed to exist when an investor holds 3% or more of the voting rights in a listed company (20% or more in the case of unlisted companies). Under IFRS, provided that an investor holds 20% or more of the voting power of the investee, it is presumed that the investor has significant influence. Under IFRS, certain investments, classified as associated companies under Spanish GAAP, shall be accounted for as available for sale and marked to market at each balance sheet date, with the resulting unrealized gains or losses being recognized directly in shareholders' equity.

Financial instruments

Spanish GAAP requires that financial assets, including derivatives, be measured at the lower of cost or market value, whereas financial liabilities are measured at their redemption amount. Financial assets are derecognized when expired, transferred or sold.

Under IFRS, financial assets and liabilities are classified into categories that determine their measurement at fair value or at amortized cost. Certain gains and losses on financial instruments are required to be recognized directly in shareholders' equity until derecognition, or in the event of an impairment. Also, IFRS sets out very strict requirements for the derecognition of financial assets, based on an assessment of the risks and rewards related to the asset.

In addition to this, IFRS requires compliance with very specific criteria in order to apply hedge accounting. As a consequence, certain hedging relationships that would qualify for hedge accounting under Spanish GAAP would not qualify for hedge accounting under IFRS.

Foreign exchange differences

Spanish GAAP requires unrealized foreign currency exchange gains in excess of recorded foreign currency exchange losses to be capitalized and deferred. Under IFRS, foreign currency exchange gains or losses are recognized or expensed through the income statement.

Under Spanish GAAP, the exchange differences arising in intra-group loans (mainly in U.S. dollars) are eliminated in the consolidation process against cumulative translation differences. Under IFRS, exchange differences arising in intra-group loans are recognized in the income statement unless the loan is considered to be part of the entity's net investment in a foreign operation.

Net Financial Debt and Commitments

At December 31, 2004 our net financial debt and commitments was (euro)24,614 million under Spanish GAAP. We have performed a preliminary analysis of how the adoption of IFRS will impact our net financial debt. Based on our analysis, we estimate that our net financial debt at December 31, 2004 would have been approximately (euro)27,041 million under IFRS. This increase would be principally due to the reclassification of preferred stock issued by one of our subsidiaries. Under IFRS, the preference shares issued by Telefonica's subsidiary Telefonica Finance would be reclassified from non-equity minority interests to liabilities because we are obliged to pay dividends if there is distributable profit and we do not have the unconditional right to avoid delivering cash, which is required under IFRS in order for the preferred shares to avoid treatment as a liability.

Net Income

Our net income was (euro)2,877.3 million for the year ended December 31, 2004 under Spanish GAAP. We have performed a preliminary analysis of how the adoption of IFRS will impact our net income. Based on our analysis, we estimate that our net income for the year ended December 31, 2004 would have been approximately (euro)3,100 million under IFRS. This increase would be principally due to the changes in how goodwill and fair value adjustments in business combinations and financial instruments are measured under IFRS as described above.

Operating Environment

Operating Environment by Country

Spain

Our results of operations are dependent to a large extent on the level of demand for our services in Spain. As of December 31, 2004, revenues from our operations in Spain represented 60% of our consolidated revenues. Demand

for our services in Spain is related to the performance of the Spanish economy. Spain's real gross domestic product (GDP) expanded by approximately 2.7% in 2004, reflecting relatively stronger domestic demand. Inflation was 3.2% in 2004. The current-account deficit was estimated at 4.5% of GDP in 2004. The unemployment rate was 10.4% at December 31, 2004.

Brazil

The Brazilian economy experienced robust growth in 2004. Brazil's GDP rose an estimated 5.3% in 2004, a much faster pace than the 0.5% growth registered in 2003. Consumer prices increased 7.6% in 2004 compared to 9.3% in 2003. In order to curb inflation and achieve target inflation rates, the Central Bank of Brazil began raising interest rates in 2004. As of March 5, 2005, the Brazilian central bank's benchmark lending rate stood at 18.75% compared to 16% in September 2004. Brazil finished 2004 with a trade balance surplus of U.S.$33.7 billion, compared to U.S.$24.8 billion in 2003. Exports went up by 32% to U.S.$96.5 billion, while imports increased by 30% to U.S.$62.8 billion.

Argentina

Argentina's estimated GDP growth in 2004 was 8.8%, which matched the growth rate in 2003 and concluded the second year of growth after 4 years of recession ending with the deep economic and political crisis of 2001-2002. The peso depreciated 1.7% closing at 2.98 peso/U.S.$1. The consumer inflation rate increased by approximately 6.1%, below the target range of 7% to 11% established by Argentina's central bank, while wholesale prices rose by approximately 7.9% in 2004. The unemployment rate decreased to approximately 13.2% in September 2004 from 14.5% in December 2003 due to continued economic growth and the implementation of the "Plan Jefes y Jefas de Hogar," the federal government's main social assistance program.

Chile

Chile's GDP grew approximately 5.9% in 2004 compared to 3.2% growth in 2003. In 2004, inflation stood at approximately 1.1%, compared to an inflation rate of approximately 2.8% in 2003. The Chilean peso, which floats freely, appreciated approximately 13.4% in nominal terms (11.4% in real terms) against the U.S. dollar in 2004. Chile's unemployment rate rose to 8.8% in 2004 compared to 8.5% in 2004. In 2004, Chile had its largest budget surplus in eight years after a surge in copper prices boosted revenue. The surplus, following a 2003 deficit equivalent to 0.4% of GDP, was 2.2% of GDP.

Peru

Peru's GDP grew by 5.1%, the highest rate in seven years. This growth was mainly explained by an exceptional improvement in terms of trade, which increased 8.1% (the highest increase since 1979). In 2004, exports rose 15.2% last year and private investment rose 9.4%. Exports are expected to continue growing, albeit at a more modest rate, while domestic demand is expected to grow in line with GDP. During 2004, Standard & Poor's and Fitch raised the Peruvian government's credit rating to BB (stable), two levels below investment grade. In 2002, Peru's central bank adopted an explicit medium-term annual inflation target at 2.5% within a range that could vary +/- 1%. Inflation for 2004 was 3.5% compared to 2.5% in 2003.

Mexico

Mexico's estimated GDP growth in 2004 was 4.5%, compared to 1.2% in 2003. Monetary policy has been kept tight by the Mexican government in order to limit inflation and to bolster the currency, which appreciated by approximately 0.3% relative to the U.S. dollar during the course of 2004.

Exchange Rate Fluctuations

We publish our Consolidated Financial Statements in euro. Because a substantial portion of our assets, liabilities, sales and earnings are denominated in currencies other than the euro, we are exposed to fluctuations in the values of these currencies against the euro. These currency fluctuations have had and may continue to have a material impact on our financial condition and results of operations.

In 2004, variations in currencies increased our consolidated cash flows by approximately (euro)30.7 million and decreased our consolidated revenues from operations by approximately 2.5%. Currency fluctuations can also have a significant impact on our balance sheet, particularly stockholders' equity, when translating the financial statements of subsidiaries located outside the euro zone into euro. For example, in 2004 stockholders' equity was increased by (euro)244 million due to the translation of the financial statements of our foreign subsidiaries, principally due to the decline of the U.S. dollar and key Latin American currencies relative to the euro.

The table below sets forth the average exchange rates against the euro of the U.S. dollar and the key Latin American currencies that impacted our consolidated results for the periods indicated.

	2003(1) Average	2004(1) Average	% change Average
U.S. Dollar......................	1.13	1.24	10.0%
Argentine Peso....................	3.32	3.65	9.8%
Brazilian Real....................	3.45	3.63	5.2%
Chilean Peso......................	670.17	757.58	12.9%
Mexican Peso......................	12.68	12.02	10.5%
Peruvian Nuevos Soles.............	3.91	4.24	8.5%

Source: Central Treasury Bank of the respective countries

----

(1) These exchange rates are used to convert the income statements of our Latin American subsidiaries from local currency to euro Income statements for subsidiaries that use inflation adjusted accounting criteria (Mexico, Chile, Peru, Colombia and Venezuela), are first converted to US dollars at

the closing exchange rate, and then the conversion into euros is made according to the average exchange rate during the period.

In the comparison below of our results of operations for the year ended December 31, 2004 compared to the year ended December 31, 2003 and for the year ended December 31, 2003 compared to the year ended December 31, 2002, we have provided certain comparisons at constant exchange rates in order to present an analysis of the development of our results of operations from year to year without the effects of currency fluctuation. To make such comparisons, we have converted certain financial items using the prior year's exchange rate.

We describe certain risks relating to exchange rate fluctuations in "Item 3--Key Information--Risk Factors" and describe our policy with respect to limiting our exposure to short-term fluctuations in exchange rates under "Item 11--Quantitative and Qualitative Disclosure about Market Risk".

Regulation

We are subject to regulation in the different markets where we operate, which has a significant effect on our profitability. In Spain, we are regulated by the Telecommunications Market Commission, which applies "price caps" to the fees we can charge our customers for interconnection and subscription. In addition, as a dominant operator, Telefonica de Espana is obligated to grant other operators access to its network. Interconnection prices must remain within the Interconnection Offer Framework as determined by the Telecommunications Market Commission.

Telefonica Moviles is also regulated in Spain by the Telecommunications Market Commission, which has declared Telefonica Moviles to be an operator with "significant market power". Telefonica Moviles is obligated to allow other mobile operators to access its network, and the Telecommunications Market Commission sets the rates that Telefonica Moviles can charge other mobile operators for such access. Telefonica Moviles must pay a yearly fee to reserve the public domain radioelectric spectrum in respect of the allocated frequencies.

We are also subject to regulation in the Latin American markets where we have operations. These regulations include the application of, among other things, "price caps", governmental regulation of rates and fees, and the obligation to allow other operators to access our networks at competitive or regulated rates.

For a more detailed description of how regulation affects us, please see "Item 4--Information on the Company--Business Overview".

Results of Operations

A summary of our results of operations during 2002, 2003 and 2004 are shown below.

	Year ended December 31,		
	2002	2003	2004
	(in millions of euro, except share and per sh data)		

Revenues from operations..........................	28,411.3	28,399.8	30,321.
Operating profit..................................	5,031.8	6,327.9	7,235.
Income (loss) before tax and minority interest....	(14,601.1)	3,362.5	4,397.
Net income (loss).................................	(5,576.8)	2,203.6	2,877.
Net income (loss) per share(1)....................	(1.13)	0.45	0.6
Weighted average number of shares (millions)......	4,948.04	4,960.13	4,955.9

----

(1) The per share computations for all periods presented have been adjusted to reflect the stock split and stock dividends which occurred during the periods presented and after the close of the period but before the issuance of the financial statements.

The table below sets forth certain consolidated revenue and expense items as a percentage of consolidated revenue from operations for the periods indicated.

	Year ended December 31,		
	2002	2003	200
	(in millions of euro)		
Revenues from operations..........................	28,411.3	28,399.8	30,321.
Other operating revenue...........................	1.0%	1.0%	1.
Internal expenditures capitalized.................	1.7%	1.9%	1.
Increase (decrease) in inventories, net...........	(0.1%)	(0.5%)	0.
Goods purchased...................................	(24.5%)	(22.1%)	(24.
External services and local taxes.................	(17.5%)	(17.9%)	(18.
Personnel expenses................................	(16.9%)	(16.3%)	(14.
Provision for depreciation and amortization.......	(23.6%)	(22.1%)	(19.
Trade provisions..................................	(2.3%)	(1.5%)	(1.
Other operating expenses..........................	(0.3%)	(0.2%)	(0.
Total operating costs before financial e xpenses and goodwill amortization..............	(85.0%)	(80.1%)	(79.
Operating profit..................................	17.7%	22.3%	23.
Amortization of goodwill and reversal to negative goodwill..............................	(2.3%)	(1.6%)	(1.
Financial income (expense)........................	(5.6%)	(5.5%)	(4.
Exchange gains (losses), net......................	(2.2%)	1.8%	0.
Income (loss) from associated companies...........	(1.9%)	(0.8%)	(0.
Profit from ordinary activities...................	5.7%	16.2%	18.
Extraordinary revenues............................	1.7%	4.1%	1.
Losses on fixed assets............................	(33.8%)	(0.2%)	(0.
Extraordinary expenses............................	(24.9%)	(8.3%)	(
Income (loss) before tax and minority interest....	(51.4%)	11.8%	14.
Corporate income tax..............................	11.4%	(3.2%)	(3.
Minority interests................................	20.4%	(0.9%)	(1.
Net Income..	(19.6%)	8%	9.

The table below sets forth the percentage of our consolidated net sales by geographic region for the periods indicated.

	Year ended December 31,		
	2002	2003	200
Spain	58%	62%	6
Latin America	35%	33%	3
Rest of World	7%	5%	
Total	100%	100%	1

The table below sets forth the contribution to our results of operations by each of our principal business segments for 2002, 2003 and 2004 after elimination of sales to other members of the Telefonica Group. During 2004, we integrated the former Telefonica Empresas business line's operations into the Spanish and Latin American fixed business lines. See "Item 4-- History and Development of the Company--Overview". In light of the integration of the Telefonica Empresas business line into the Spain and Latin America fixed line businesses, to provide a comparable year-to-year discussion of our results of operations for the two years ended December 31, 2004, we have presented the results of operations for the year ended December 31, 2003 as if the Telefonica Empresas business line had been integrated into the Spain and Latin America fixed line businesses during such period. In the discussion of our results of operations for the two years ended December 31, 2003, however, the discussion of our results of operations does not reflect the integration of the Telefonica Empresas business line into the Spain and Latin America fixed line businesses. In order to provide information regarding our results of operations for all three periods on a comparable basis, we have set forth below the results of operations of our business lines, reflecting the integration of the Telefonica Empresas business line into the Spain and Latin America fixed line businesses, for the three years ended December 31, 2004.

	Year ended December 31,		
	2002	2003	2004
	in millions of euro		
Revenues from Operations			
Telefonica de Espana	9,929.0	10,028.3	10,295.
Telefonica Latinoamerica	7,138.0	6,456.8	6,549.
Telefonica Moviles	7,993.0	8,905.1	10,577.
Telefonica de Contenidos	1,068.1	1,374.5	1,200.
Terra Networks	546.3	414.5	399.
Other companies(1)	1,736.88	1,220.7	1,300.
Operating Expenses			
Telefonica de Espana	6,050.1	6,048.7	6,019.
Telefonica Latinoamerica	3,880.9	3,548.5	3,646.
Telefonica Moviles	5,600.3	5,881.3	7,381.
Telefonica de Contenidos	964.4	1,179.7	1,027.
Terra Networks	741.5	577.79	510.
Other companies(1)	5,574.6	2,139.3	2,331.
Eliminations	(6,038.5)	(3,328.4)	(3,377.
Operating profit before amortization			
Telefonica de Espana	4,695.4	4,762.4	5,054.
Telefonica Latinoamerica	3,295.0	3,101.3	3,141.
Telefonica Moviles	3,830.0	4,581.9	4,755.
Telefonica de Contenidos	114.5	210.3	182.
Terra Networks	(141.7)	(39.5)	20.
Other companies(1)	2.4	72.8	133.

Eliminations	(71.5)	(87.1)	(71.
Amortizations			
Telefonica de Espana............................	(2,765.8)	(2,638.8)	(2,374.
Telefonica Latinoamerica........................	(2,163.4)	(1,805.7)	(1,697.
Telefonica Moviles..............................	(1,391.9)	(1,516.4)	(1,673.
Telefonica de Contenidos........................	(49.6)	(49.9)	(30.
Terra Networks..................................	(142.7)	(78.7)	(79.

	Year ended December 31,		
	2002	2003	2004
	in millions of euro		
Other companies(1)..............................	(254.3)	(227.2)	(188.
Eliminations	75.3	42.1	63.
Operating Profit			
Telefonica de Espana............................	1,929.6	2,123.6	2,680.
Telefonica Latinoamerica........................	1,131.7	1,295.6	1,443.
Telefonica Moviles..............................	2,438.1	3,065.9	3,081.
Telefonica de Contenidos........................	64.9	160.4	152.
Terra Networks..................................	(284.4)	(118.2)	(58.
Other companies(1)..............................	(251.9)	(154.4)	(55.
Eliminations	3.8	(44.9)	(8.

----

(1) TPI, Atento, Telefonica, S.A., Grupo T. Gestiona and other subsidiaries.

We present the results of operations of each consolidated operating subsidiary under the line of business to which it relates, regardless of whether the legal entity has been transferred to the holding company that heads such line of business. The results shown for our different lines of business may therefore differ from those reported by our subsidiaries such as Telefonica Moviles and Terra Lycos, which are reporting companies in the United States. They will also differ from the results of operations reported by those companies because they are not wholly owned by us and because certain transactions they enter into with other members of the Telefonica Group are eliminated in consolidation. We use this presentation because it more accurately reflects the way in which we evaluate the performance of our different lines of business.

Year Ended December 31, 2004 Compared to Year Ended December 31, 2003

The table below sets forth an analysis of consolidated revenues from operations for each of our principal business segments for 2003 and 2004 after elimination of sales to other members of the Telefonica Group. Financial data related to our business segments is also included in Note 25 to our Consolidated Financial Statements.

	Year ended December 31,	
	2003	2004
	(in millions of euro)	
Telefonica de Espana............................	10,028.3	10,295.1

Telefonica Latinoamerica.........................	6,456.8	6,549.2
Telefonia Moviles................................	8,905.1	10,577.3
Telefonica de Contenidos.........................	1,374.5	1,200.2
Terra Networks...................................	414.5	399.9
Other companies(1)...............................	1,220.7	1,300.2
Total Revenues from Operations	28,399.8	30,321.9

----

(1) Includes revenues from operations from TPI, Atento, Telefonica, S.A., Grupo T. Gestiona and other subsidiaries.

The table below shows the contribution to our total revenue from operations of each of our principal lines of business for 2003 and 2004 after adjustments for sales to other members of the Telefonica Group.

	Year ended December 31,	
	2003	2004
Telefonica de Espana.............................	35.3%	34.0%
Telefonica Latinoamerica.........................	22.7%	21.6%
Telefonica Moviles...............................	31.4%	34.9%
Telefonica de Contenidos.........................	4.8%	4.0%
Terra Networks...................................	1.5%	1.3%

	Year ended December 31,	
	2003	2004
Other companies(1)...............................	4.3%	4.3%
Total Revenues from operations...................	100.0%	100.0%

----

(1) Includes revenues from operations from Telefonica, S.A., Grupo T. Gestiona and other subsidiaries.

The table below shows the contribution to our consolidated net income of each of our principal business lines in 2003 and 2004.

	Year ended December 31,	
	2003	2004
	(in millions of euro)	
Telefonica de Espana.............................	280.20	1,112.07
Telefonica Latinoamerica.........................	558.50	806.61
Telefonica Moviles...............................	1,594.30	1,620.41
Telefonica de Contenidos.........................	119.7	(65.46)
Terra Networks...................................	(172.71)	163.97
Other companies and Eliminations(1)...............	(176.4)	(760.31)
Total Net Income.................................	2,203.59	2,877.29

----

(1) Includes net income from TPI, Atento, Telefonica, S.A., Grupo T. Gestiona and other subsidiaries.

Revenues from operations (sales to external clients)

Our revenues from operations, which accounted for 97.3% and 97.2% of our consolidated total revenues for 2004 and 2003, respectively, increased to (euro)30,321.9 million in 2004 compared to (euro)28,399.8 million in 2003. The increase in revenue from Telefonica de Espana, Telefonica Moviles, Telefonica Latinoamerica, Telefonica Publicidad e Informacion, or TPI and Atento was offset by the negative exchange rate impact suffered in 2004. Exchange rate fluctuations had a negative impact of approximately 1.50% on our revenues from operations in 2004.

Whereas we calculate revenues from operations both before and after adjustments for sales to other members of the Telefonica Group, our analysis of revenue from operations is strictly limited to revenues from operations after adjustments for sales to other members of the Telefonica Group. In the aggregate, we believe that sales to other members of the Telefonica Group did not have a significant impact on the percentage fluctuations during the periods discussed.

Telefonica de Espana Group. Since 2004, the results of Telefonica Data Espana and Telefonica Soluciones are included in the results of Telefonica de Espana due to the integration of the former Telefonica Empresas business line's operations into the Spain and Latin America fixed business lines. As discussed above, in order to facilitate comparison we have recalculated the analysis of certain results of our operations in 2003 to account for the reorganization of our structure.

Telefonica de Espana Group's revenues from operations increased to (euro)10,295.1 million in 2004 from (euro)10,028.3 million in 2003. The positive evolution in revenues compared to 2003 was principally due to the increase in revenues from broad band services and services provided to other operators, which offset the decline in outgoing traffic and commercialization of handsets.

- Revenues from connection access fees include all revenues from our clients for rental of and connection to PSTN lines (for basic telephony service), ISDN lines (for integration of voice, data and video services), Corporate Services and TUP (for public telephony service) and additional charges and publicity in telephone booths. Revenues for connection access fees increased by 0.9% to 2,821.3 million in 2004 compared to 2,795.8 million in 2003. The increase in revenue was due to a 4.35% increase in the PSTN monthly rental fee ((euro)0.55) and the increase of the surcharge on calls made from public cabins to free toll numbers partially offset the by the 1.5% decrease in the number of PSTN lines in service. This increase in the monthly rental fee was excluded from the price-cap on tariffs imposed by Spanish regulation.

- Revenues from leased circuits include revenues received from leasing our circuits, both domestic and international, to customers and other telecommunication operators. Revenue from leased circuits decreased by 10.0% to (euro)173.2 million in 2004 compared to (euro)192.4 million in 2003. The decrease in revenue in 2004 was due to a diminution in the number of leased circuits as a result of customer migration to higher speeds, ADSL, and to the carrier capacity of wholesalers.

- Revenues from the commercialization of handsets include all revenues from the sale, leasing, maintenance and installation of handsets. Revenues from the commercialization of handsets decreased by 16.9% to (euro)586.0 million in 2004 from (euro)705.5 million in 2003 as the result of a reduction in maintenance revenues due to price reductions, changes made to comprehensive maintenance service price and generally to a policy to offer increased discounts and bonuses to certain client segments.

- Broadband services revenues, principally composed of revenues generated by TdE IP network, increased by 55.6% to (euro)1,068.2 million in 2004 from (euro)686.7 million in 2003. This increase was principally due to a 50.0% increase in the number total of connections in 2004. Retail ADSL connections increased to (euro)1,611.9 million in 2004 compared to (euro)1,070.3 million in 2003. This situation led to a twofold increase in the revenues obtained from ADSL services in 2004 as compared to 2003. The increase in ADSL connections was primarily due to the increased popularity of broadband in Spain and increased marketing efforts.

- Revenues from operator services include all revenues from operator services, national and international. International operator services include automatic access, transit, leasing capacity and manual international access. National operator services include national interconnection, rented subscriber loop and commercial wholesale services (access, transit, traffic and support). Revenues from operator services increased by 8.8% to (euro)717.3 million in 2004 from (euro)659.6 million in 2003, due to an increase in the use of our rented subscriber loop and increases in commercial wholesale services.

- Revenues from outgoing traffic, which include all revenues from net effective consumption and other consumption (including phone cards, messages, manual traffic and RPV), decreased 3.2% to (euro)3,521.0 million in 2004 from (euro)3,639.1 million in 2003. This decrease was due to a market recession and increased competition leading to a loss of market share and a 2% price reduction in 2004 as a result of a price-cap on tariffs imposed by Spanish regulation. See "Item 4--Information on the Company--Business Overview--Fixed-Line Telecommunications Services in Spain--Telefonica de Espana--Spain--Regulation".

- Revenues from data services, including revenues from retail access, the installation and operation of virtual private networks and the solutions business increased 3.7% to (euro)742 million in 2004 from (euro)715.5 in 2003.

Telefonica Moviles. Telefonica Moviles' revenue from operations increased 18.8% to (euro)10,577.3 million in 2004 from (euro)8,905.1 million in 2003. Exchange rate fluctuations had a negative impact of approximately 3.2% on Telefonica Moviles revenues from operations. Revenues from Telefonica Moviles' Spanish operations increased 11.7% to (euro)7,114.3 million in 2004 from (euro)6,372.2 million in 2003. This resulted primarily from a 12% increase of traffic.

Revenues from Telefonica Moviles' Latin American wireless operations increased 36.9% as measured in euro to (euro)3,461.8 million in 2004 from (euro)2,529.5 million in 2003, due principally to the incorporation of BellSouth's Latin American operations acquired by Telefonica Moviles in 2004. Excluding the impact of exchange rate fluctuations and the incorporation of

Bellsouth operators, revenues from operations would have increased primarily due to the increase in the number of customers in Mexico and Argentina.

Telefonica Latinoamerica. Beginning in 2004, the results of Telefonica Empresas America and Telefonica International Wholesale Services (TIWS) have been included in the Telefonica Latinoamerica business line due to the integration of the former Telefonica Empresas business line's operations into the Spanish and Latin American fixed line businesses as discussed above. In order to facilitate comparison we have recalculated the analysis of certain results of our operations in 2003 to account for the reorganization of our structure.

Telefonica Latinoamerica's operating revenues increased by 1.4% to (euro)6,549.2 million in 2004 from (euro)6,456.8 million in 2003. Exchange rate fluctuations had a negative impact of approximately 5.4%. Excluding the impact of

exchange rate fluctuations, revenues from operations would have increased by 6.8%. In local currency, revenues from Telesp's operations increased principally due to the expansion of broadband, new business, such as long distance originated out of Sao Paulo or Personal Mobile System (SMP), and the increase in the tariffs, in addition to an increase in fixed to mobile traffic. Telefonica de Argentina's revenues from operations increased due to the continuation of the improved economic conditions started in year 2003 in Argentina as reflected by high customer demand, increased network traffic and increases in fixed-line as well as ADSL users. Telefonica del Peru and CTC's operating revenues decreased in 2004 compared to 2003 mainly due to lower average tariffs and the effects of increased mobile competition.

- Revenues from operations generated by Telesp increased 8.8% (excluding exchange rate fluctuations, revenues from operations would have increased 14.4%) to (euro)3,603.0 million in 2004 from (euro)3,311.3 million in 2003 reflecting the growth of lines in service, especially those associated with products targeted to certain population sectors, broadband revenues and an increase in long distance market share. In addition to those effects, Telesp's results from operations also improved because of a tariff increment since July 2004 (6.89% average increase as measured in local currency), as well as an additional increase according to the tariff increase not applied during 2003 as a result of a legal decision.

- Revenues from operations generated by Telefonica de Argentina decreased 0.9% (excluding exchange rate fluctuations, revenues from operations would have increased 8.9%) to (euro)741.2 million in 2004 from (euro)747.8 million in 2003. The increase in revenues from operations, excluding exchange rate fluctuations, was mainly due to a higher demand for fixed lines and ADSL and a 9.9% significant increase in total traffic, mainly as a result of prepaid traffic growth.

- Revenues from operations generated by Compania de Telecomunicaciones de Chile decreased 10.8% (excluding exchange rate fluctuations, revenues from operations would have decreased 7.7%) to (euro)859.6 million in 2004 from (euro)963.5 million in 2003, due to the fall in local and long distance traffic, influenced by customers increasingly substituting fixed line services with mobile telephony services, and the reduction in local fixed to mobile traffic tariffs since January 2004. These effects were partially offset by an increase in broadband revenues as a consequence of a 60.3% increase in broadband lines to 200,700 lines.

- Revenues from operations generated by Telefonica del Peru decreased approximately 8.0% (excluding exchange rate fluctuations, revenues from operations would have decreased 4.1%) to (euro)957.9 million in 2004 from (euro)1,041.6 million in 2003, principally due to the decrease of 10% in local traffic tariffs and the fall in traffic as a result of increased competition from the mobile business and the long distance competitors. These effects were partially offset by the increase in broadband revenues resulting from an increase in broadband lines of 126.5% to 205,400 lines.

- Telefonica Empresas America's revenues from operations increased 2.2% to (euro)319.8 million in 2004 from (euro)312.9 million in 2003. (excluding exchange rate fluctuations, revenues from operations would have increased 7.6%), principally due to an increase in revenues from Internet, data and solution services.

Terra Networks. Terra Networks' revenues from operations decreased 3.5% to (euro)399.9 million in 2004 from (euro)414.5 million in 2003. This decrease is principally due to the Lycos sale in October 2004. The decrease in revenues from operations was partially offset by an increase in number of subscribers for Internet access and communication and portal services due to the success of the OBP (Open, Basic, Premium) model initiated in 2001. Exchange rate fluctuations had a positive impact of approximately 1.1%.

Telefonica de Contenidos Group (formerly Admira). Telefonica de Contenidos Group's revenues from operations decreased 12.7% to (euro)1,200.2 million in 2004 from (euro)1,374.5 million in 2003, mainly due to the sale of Antena 3, which was consolidated using the full integration method during the first six months of 2003. Antena 3 contributed (euro)303.8 million to 2003 revenues from operations. This decrease in revenues was partially offset by increases in revenues from Endemol and ATCO. The Endemol Group generated revenues of (euro)1,033.7 million in 2004, a 13.1% from 2003 due primarily to a strong results from its operations in the United Kingdom and the U.S.. The performance of ATCO is mainly explained by a recovery in the advertising business in Argentina.

Others. Revenues from operations from our other businesses decreased 6.3% to (euro)1,220.6 million in 2004 from (euro)1,297.8 million in 2003. Revenue from operations from Atento increased 24.1% to (euro)611.7 million in 2004 from (euro)493 million in 2003, despite the negative impact of foreign exchange fluctuations of 4.3% primarily due to the strong increase in revenues from its operations in Spain, Brazil and Mexico and minor increases in other countries, with the exception of Morocco. Telefonica Publicidad e Informacion's revenues from operations increased 3.9% to (euro)546.4 million in 2004 from (euro)525.8 million in 2003 due to the growth in revenues of all subsidiaries as measured in local currencies, which more than offset the depreciation of Latin American currencies against the euro.

Total expenses (operating expenses and other operating expenses)

Operating expenses, which consist of inventories (net), goods purchased, external services and local taxes and personnel costs increased 8.7% to (euro)17,539.2 million in 2004 from (euro)16,136.9 million in 2003, principally due to the incorporation of Bellsouth's Latin American operators and to the commercial effort made to add new customers and to maintain existing ones. Other operating expenses and trade provisions decreased 12.0% to (euro)423.4 million in 2004 from (euro)480.9 million in 2003, due to a decrease in trade provisions at Telefonica Latinoamerica, Telefonica de Espana and Telefonica Moviles.

Telefonica de Espana. For the business line headed by Telefonica de Espana, operating expenses decreased 0.5% to (euro)6,019.0 million compared to (euro)6,048.7 million in 2003. This decrease was due to a decrease in personnel expenses recorded during the year as a result of the continuation of the labor reduction program for 2003-2007 at Telefonica de Espana, which began in July 2003.

Goods purchased increased 1.7% to (euro)2,571.3 million in 2004 from (euro)2,528.7 million in 2003. This increase was due to an increase in the expenses at Telyco linked to the handset sale business and to an increase in the expenses for the acquisition of equipment related to the development of ADSL services. The decrease of the interconnection expenses after the reduction of the fixed to mobile interconnection tariffs that came into effect in November 2003 and October 2004 partially offset these increased expenses.

Personnel expenses decreased 9.3% to (euro)2,083.6 million in 2004 from (euro)2,298.3 million in 2003 due to the labor reduction program for years 2003-2007 approved in July 2003, which reduced headcount by 2,417 employees during 2004. At December 31, 2004, Telefonica de Espana Group had 36,425 employees, a 5.2% decrease compared to 2003.

External services increased 13.5% to (euro)1,179.9 million in 2004 from (euro)1,039.2 million in 2003. This increase is mainly due to stronger marketing efforts resulting from growing competitive pressure and to higher operational activity related to the growth of our ADSL services.

Other operating expenses decreased 39.6% primarily due to a decrease in the amount of account receivables paid in 2004 which led to a 37.3% decrease in our provisions for bad debt.

Telefonica Moviles. Operating expenses at Telefonica Moviles increased 25.5% to (euro)7,381.9 million in 2004 from (euro)5,881.3 million in 2003, principally due to a 36.3% increase in the cost of goods purchased to (euro)3,743.9 million in 2004 from (euro)2,747.0 million in 2003, and a 17.4% increase in external services costs and taxes to (euro)3,082.8 million in 2004 from (euro)2,625.7 million in 2003.

Goods purchased (including interconnection costs) at Telefonica Moviles' Spanish operations increased 13.6% to (euro)2,044.0 million in 2004 from (euro)1,799.0 million in 2003, mainly due to the increase in commercial activity and in outgoing traffic to other networks, generating an increase in interconnection expenses. External services at Telefonica Moviles' Spanish operations increased 13.0% to (euro)1,759.0 million in 2004 from (euro)1,557.0 million in 2003, principally due to greater commercial activity. Personnel expenses at Telefonica Moviles' Spanish operations increased 8.2% to (euro)257.6 million in 2004 from (euro)238 million in 2003 due to a 1.3% increase in headcount for the period.

Goods purchased (including interconnection costs) at Telefonica Moviles' Latin American operations increased 84.5% to (euro)1,715.9 million in 2004 from (euro)929.9 million in 2003 due principally to the incorporation of BellSouth's Latin American operators. Excluding the impact of exchange rate fluctuations and the incorporation of Bellsouth's operators, good purchases would have increased primarily as a result of an increase in commercial activity in Brazil, Mexico and Argentina. External services at Telefonica Moviles' Latin American operations increased 18.5% to (euro)1,283.3 million in 2004 from (euro)1,082.7 million in 2003, due principally to the incorporation of BellSouth's Latin American operators. Excluding the impact of exchange rate fluctuations and the incorporation of the Bellsouth operators, external services would have increased due to the same reasons as the increases in goods purchased. Personnel expenses at Telefonica Moviles' Latin American operations increased 34.7% to (euro)293.3 million in 2004 from (euro)217.7 million in 2003 mainly due to the high turnover in Mexico's salesforce during 2004.

Telefonica Latinoamerica. Telefonica Latinoamerica's operating expenses increased 2.8% to (euro)3,646.7 million in 2004 compared to (euro)3,548.50 million in 2003. Excluding the impact of exchange rate fluctuations, operating expenses would have increased approximately 8.0% due to an increase in interconnection expenses in Brazil as a result of an increase in traffic to mobile networks and the introduction of SMP system in August of 2003 for long distance mobile to mobile calls. Likewise, there was an increase in external services costs in Brazil and Argentina because of commercial efforts made during 2004.

Other operating expenses decreased 5.6% to (euro)204.2 million in 2004 from (euro)216.2 million in 2003. Excluding the impact of exchange rate fluctuations, other operating expenses would have decreased 1.3% as a consequence of the reduction in bad debt provisions from amounts billed to customers in Brazil and Argentina.

- Telesp's operating expenses increased 14.7% in 2004 (excluding exchange rate fluctuations, operating expenses would have increased 20.6%) mainly due to more traffic volume directed to mobile networks and the SMP expansion, with higher interconnection expenses associated, and to the price increase of certain contracts indexed to inflation. Other operating expenses decreased 5.4% (excluding exchange rate fluctuations, other operating expenses would have decreased 0.5%), due to a reduction in uncollectible accounts receivable.

- Telefonica de Argentina's operating expenses increased 0.4% in 2004 (excluding exchange rate fluctuations, operating expenses would have increased 10.3%), principally due to an increase in personnel expenses, in part related to an increase in salaries indexed to inflation, goods purchased and an increase in external services reflecting the increase of commercial activity. These cost increases were partially offset by a decrease in other operating expenses, which gave rise to a gain of (euro)11.5 million in 2004 as compared to gain of (euro)3.5 million in 2003. The positive result with respect to other operating expenses was primarily due to the effective management of bad debt, the increased use of prepaid and consumption control products which help maximize debt recovery and ensuring that profitable customers are maintained.

- Compania de Telecomunicaciones de Chile's operating expenses decreased 10.8% to (euro)482.51 in 2004 (excluding exchange rate fluctuations, operating expenses would have decreased 7.75%), mainly due to the reduction in goods purchased as a result of the fall in mobile interconnection rates. This decrease was partially offset by an increase in external services expenses and personnel costs measured in local currency.

- o Telefonica del Peru's operating expenses decreased 9.3% to (euro)605.19 million in 2004 (excluding exchange rate fluctuations, operating expenses would have decreased 5.45%), principally as a result of a reduction in external services expenses. In 2004 Telefonica Latinoamerica renegotiated its management fee contract such that management fees charged to Telefonica del Peru are 1% of its revenues instead of a payment of a 9% of its quarterly operating profits before depreciation and amortization. In addition, until 2003 Telefonica de Peru paid a technology transfer fee to Telefonica Latinoamerica of 1% of its revenues. Promotion and plant maintenance expenses also declined. There was also a reduction in goods purchased as a result of a decline in fixed line to mobile traffic.

- o Telefonica Empresas America's operating expenses increased by 2.1% to (euro)425.89 million in 2004 from (euro)417.02 million in 2003 (excluding exchange rate fluctuations, operating expenses would have increased 7.8%), mainly due to an increase in goods purchased and personnel expenses.

Terra Networks. operating expenses decreased 11.7% to (euro)510.4 million in 2004 from (euro)577.8 million in 2003, principally due to improvements in efficiency, personnel reduction and less sales and marketing expenses.

- o Goods purchased decreased 3.6% to (euro)256.3 million in 2004 from (euro)265.8 million in 2003, principally due to the reductions observed in practically all items and particularly in communications costs. Personnel expenses decreased 19.9% to (euro)95.8 million in 2004 from (euro)119.7 million in 2003, principally due to workforce reductions.

- o External services decreased 18.7% to (euro)148.3 million in 2004 from (euro)182.4 million in 2003 as a result of successful cost control with respect to all expenses, particularly those relating to marketing and professional services.

Telefonica de Contenidos (formerly Admira). Telefonica de Contenidos Group (formerly Admira). Telefonica de Contenidos Group's revenues from operations decreased 12.7% to (euro)1,200.2 million in 2004 from (euro)1,374.5 million in 2003, mainly due to the sale of Antena 3, which was consolidated using the full integration method during the first six months of 2003. Antena 3 contributed (euro)303.8 million to 2003 revenues from operations. This decrease in revenues was partially offset by increases in revenues from Endemol and ATCO. The Endemol Group generated revenues of (euro)1,033.7 million in 2004, a 13.1% from 2003 due primarily to strong results from its operations in the United Kingdom and the U.S. The performance of ATCO is mainly explained by a recovery in the advertising business in Argentina.

Others and eliminations. Operating expenses of our other businesses increased 9.4% to (euro)1,980.5 million in 2004 from (euro)1,795.0 million in 2003. Atento's operating expenses increased 22.2% in 2004 due to the increase of personnel expenses related to an increase of activity. Operating expenses for Telefonica Publicidad e Informacion increased by 1.3% due mainly to the increase of external services, including expenses for a full year of operating the telephone directory service 11888 in Spain.

Operating profit before depreciation and amortization

Our management believes that operating profit before depreciation and amortization is meaningful for investors because it provides an analysis of our operating results profitability of our business lines using the same measure used by our chief decision makers. See "Item 5. Operating and Financial Review and Prospects -- Presentation of Financial Information -- Non-GAAP Financial Information". The following table provides a reconciliation of operating profit before depreciation and amortization to operating profit for the Telefonica Group and each of our business lines for the periods indicated.

	Year ended December 31, 2004					
	Telefonica de Espana	Telefonica Moviles	Telefonica Latinoamerica	Telefonica Contenidos	Terra Network	Telefonic Holding(1
	(in millions of euro)					
Operating profit before depreciation and amortization expenses.........	5,054.5	4,755.0	3,141.0	182.6	20.9	(220.
Depreciation and amortization expenses.........	2,374.0	1,673.4	1,697.8	30.5	79.5	49.
Operating profit....	2,680.5	3,081.6	1,443.2	152.1	(58.7)	(270.

	Year ended December 31, 2003					
	Telefonica de Espana	Telefonica Moviles	Telefonica Latinoamerica	Telefonica Contenidos	Terra Network	Telefonic Holding(1
	(in millions of euro)					
Operating profit before depreciation and amortization expenses.......	4,762.40	4,581.90	3,101.3	210.33	(39.49)	(223.7
Depreciation and amortization expenses.......	2,638.8	1,516.04	1,805.70	49.93	78.74	47.9

107

	Year ended December 31, 2004					
	Telefonica de Espana	Telefonica Moviles	Telefonica Latinoamerica	Telefonica Contenidos	Terra Network	Telefonic Holding(1
	(in millions of euro)					
Operating Profit..	2,123.59	3,065.86	1,295.60	160.40	(118.22)	(271.6

----

(1) Group parent company

Our operating profit before depreciation and amortization increased 4.9% to (euro)13,215.4 million in 2004 from (euro)12,602.1 million in 2003, due to increases in operating profit before depreciation and amortization at Telefonica Moviles, Telefonica de Espana, Telefonica Latinoamerica, Telefonica Publicidad e Informacion and Atento. Operating profit before depreciation and amortization also increased at Terra Networks, which recorded positive operating profit before depreciation and amortization. Exchange rate fluctuations had a negative impact of approximately 1.7%.

Telefonica de Espana. Telefonica de Espana's operating profit before depreciation and amortization increased 6.1% to (euro)5,054.5 million in 2004 from (euro)4,762.4 million in 2003. This increase was mainly due to the positive evolution of broadband revenues and to cost reductions principally due to a 9.3% reduction in personnel expenses.

Telefonica Latinoamerica. Telefonica Latinoamerica's operating profit before depreciation and amortization increased slightly to (euro)3,141.0 million in 2004 from (euro)3,101.3 million in 2003, as a result of depreciation of almost all Latin American currencies against the euro. Excluding the impact of exchange rate fluctuation, Telefonica Latinoamerica's operating profit before depreciation and amortization increased 6.8% mainly due to increases of operating profit before depreciation and amortization in local currencies of Telesp (6.9%) Telefonica de Argentina (12.8%), and Telefonica del Peru (9.7%), which offset decreases of operating profit before depreciation and amortization in local currencies of Compania de Telecomunicaciones de Chile (-3.6%).

- Telesp's operating profit before depreciation and amortization increased 1.7% (excluding exchange rate fluctuations, operating profit before depreciation and amortization would have increased 6.9%) in 2004 to (euro)1,699.9 million from (euro)1,672.1 million in 2003. The increase in local currency was principally due to growth in Telesp's ADSL, traditional lines based in a low income markets and SMP and rhe average increase in tariffs of 16%. This increase offsets an increase in expenses following the increase in commercial activity and higher interconnection costs associated to the SMP development.

- Telefonica de Argentina's operating profit before depreciation and amortization increased 2.7% (excluding exchange rate fluctuations, operating profit before depreciation and amortization would have increased 12.8%) in 2004 to (euro)466.1 million from (euro)453.9 million in 2003. The increase was principally due to the improvement of the main operational indicators (especially lines and traffic), to a reduction of bad debt and to the collection of amounts owed for which provisions had been taken in prior years.

- Compania de Telecomunicaciones de Chile's operating profit before depreciation and amortization decreased 6.9% (excluding exchange rate fluctuations, operating profit before depreciation and amortization would have decreased 3.7%) in 2004 to (euro)417.8 million from (euro)448.7 in 2003. This reduction was principally due to a decrease in revenues, which could not be offset by strict cost controls. Revenues decreased due to a reduction in the long distance market and decreases in network traffic, influenced by customers increasingly substituting fixed line services for mobile telephony services.

- Telefonica del Peru's operating profit before depreciation and amortization increased 5.2% (excluding exchange rate fluctuations, operating profit before depreciation and amortization would have increased 9.7%) in 2004 to (euro)426.4 million from (euro)405.3 million in 2003. The decrease in revenues from operations was primarily due to a decrease in local traffic tariffs and a decrease in traffic as a result of increased competition. These decreases was offset by a reduction in operating expenses.

- Telefonica Empresas America's operating profit before depreciation and amortization increased 71.5% (an increase of 79.0% in local currencies) in 2004 to (euro)54.3 million from (euro)31.7 million in 2003. The increase in revenues from operations is mainly due to significant increases in revenues from internet, data and solution services, which were partially offset by an increase in operating expenses.

Telefonica Moviles. Telefonica Moviles' operating profit before depreciation and amortization increased 3.8% to (euro)4,755.0 million in 2004 from (euro)4,581.9 million in 2003 due principally to a significant increase in operating profit before depreciation and amortization for Telefonica Moviles' Spanish operations due to increased marketing efforts. Exchange rate fluctuations had a negative impact of approximately 0.8%.

Terra Networks. Terra Networks had positive operating profit before depreciation and amortization of (euro)20.9 million in 2004 compared to negative operating profit before depreciation and amortization of (euro)39.5 million in 2003 due to a reduction in personnel costs from a headcount reduction carried out in 2004.

Telefonica de Contenidos (former Admira). Telefonica de Contenidos' operating profit before depreciation and amortization decreased 13.2% to (euro)182.6 million from (euro)210.3 million in 2003. The principal reason for this decrease was a change in accounting relating to the Antena 3 Group. However, the effect of cost-cutting measures implemented by Telefonica de Contenidos partially offset this decrease.

Others. Operating expenses of our other businesses increased 9.4% to (euro)1,980.5 million in 2004 from (euro)1,795.0 million in 2003. Atento's operating expenses increased 22.2% in 2004 due to the increase of personnel expenses related to an increase of activity. Operating expenses for Telefonica Publicidad e Informacion increased by 1.3% due mainly to the increase of external services, including expenses for a full year of operating the telephone directory service 11888 in Spain.

Depreciation and amortization

Consolidated depreciation and amortization decreased 4.7% to 5,980.2 million in 2004 from 6,274.2 million in 2003. This decrease was due in large part to our commitment to a conservative investment policy. This policy seeks to control capital expenditures by eliminating expenditures that are unnecessary or that cannot be recovered in a reasonable amount of time.

Telefonica de Espana Group. Depreciation and amortization of Telefonica de Espana Group decreased 10.0% to (euro)2,374.0 million in 2004 from (euro)2,638.8 million in 2003, due to a more controlled and conservative investment policy

Telefonica Latinoamerica. Depreciation and amortization of Telefonica

Latinoamerica decreased 6.0% to (euro)1,697.8 million in 2004 from (euro)1,805.7 million in 2003. Excluding the impact of exchange rate fluctuations, depreciation and amortization would have decreased 1.4% when compared with the previous year. This decrease was primarily due to a more controlled and conservative investment policy.

Telefonica Moviles Depreciation and amortization of Telefonica Moviles increased 10.4% to (euro)1,673.4 million in 2004 from (euro)1,516.0 million in 2003 (excluding the impact of exchange rate fluctuations, depreciation and amortization would have increased by 4.3%) mainly due to a increase of the amortization in Mexico due to investment in developing the GSM network.

Terra Networks. Depreciation and amortization of Terra Networks increased 1.0% to (euro)79.5 million in 2004 from (euro)78.7 million in 2003.

Telefonica de Contenidos. Depreciation and amortization of Telefonica de Contenidos (formerly Admira) decreased to (euro)30.5 million in 2004 compared to (euro)49.9 million in 2003.

Others. Depreciation and amortization of our other businesses decreased to (euro)138.9 million in 2004 from (euro)179.2 million in 2003. Atento's depreciation and amortization decreased 30.3% to (euro)36.4 million in 2004 from (euro)52.2 million in 2003. Telefonica Publicidad e Informacion's depreciation and amortization decreased 18.3% to (euro)25.1 million in 2004 compared to (euro)30.8 million 2003.

Operating profit

Operating profit increased 14.3% to (euro)7,235.25 million in 2004 from (euro)6,327.9 million in 2003. This increase compared to last year is the result of the increase in revenues and a 4.7% decrease in amortization expense.

Telefonica de Espana. Operating profit of Telefonica de Espana Group increased 26.2% to (euro)2,680.5 million in 2004 from (euro)2,123.6 million in 2003, mainly due to the positive evolution of Internet and broadband services and a 10.0% decrease in amortization compared to 2003.

Telefonica Latinoamerica. Operating profit at Telefonica Latinoamerica increased by 11.4% to (euro)1,443.2 million in 2004 from (euro)1,295.6 million in 2003 as a result of a 1.4% increase in revenue and a 6.0% decrease in amortization. Excluding the impact of exchange rate fluctuations, operating profit would have increased by 18.1%.

Telefonica Moviles. Operating profit of Telefonica Moviles increased 0.5% to (euro)3,081.6 million in 2004 from (euro)3,065.9 million in 2003, mainly due to a 3.8% increase in operating profit before depreciation and amortization, offset in part by a 10.4% increase in depreciation expense.

Terra Networks. Terra Networks' operating loss in 2004 was (euro)58.6 million compared to an operating loss of (euro)118.2 million during 2003. The strong performance in operating profit before depreciation and amortization of Terra Networks was more than offset by (euro)79.5 million of depreciation and amortization expenses.

Telefonica de Contenidos. Operating profit of Telefonica de Contenidos was (euro)152.1 million in 2004 compared to an operating profit of (euro)160.4 million in 2003.

Others. Operating profit of our other businesses increased to (euro)206.5 million in 2004 from (euro)72.3 million in 2003 due to a 34.4% increase in operating profit before depreciation and amortization and to a 45.2% decrease in depreciation and amortization expenses. Atento's operating profits grow 281.5% to (euro)54.4 million in 2004 from (euro)14.3 million in 2003. This improvement was due to the increase in revenues together with a reduction of amortizations in 30.3% due to a decrease in capital expenditures. Telefonica Publicidad e Informacion's operating profit in 2004 was (euro)190.1 million, a 24.0% increase compared to 2003 mainly due to a 16.9% increase in operating profit before depreciation and amortization and a 18.3% decrease in depreciation and amortization.

Profit from ordinary activities

Profit from ordinary activities increased 20.6% to (euro)5,562.8 million in 2004 compared to (euro)4,612.2 million in 2003. This increase was principally due to a 14.3% increase in operating profit and:

- the losses from associated companies decreased in 2004 by 73.6% to (euro)56.1 million from (euro)212.6 million in 2003 as a result of the deconsolidation of Via Digital, the sale of certain subsidiaries (Antena 3 TV and Atlanet in 2003 and Audiovisual Sport in 2004), smaller losses related to IPSE-2000, Medi Telecom and the Lycos Group, and the positive impact of the results of Portugal Telecom due to both its improved results and our increased participation compared to 2003.

- Goodwill amortization totaled (euro)432.6 million euros in 2004, a 2.2% decrease compared to 2003. This performance was principally due to a reduction of goodwill amortization in the cellular business resulting from the reclassification of certain licenses as intangible assets rather than goodwill and as a result of sale of Lycos Inc. in 2004 and Antena 3 in 2003. This decrease was partially offset by an increase in goodwill resulting from the incorporation of goodwill amortization from Bellsouth's Latin American operators for the last two months of 2004 and from Sogecable since July 2003.

- Net financial expenses decreased 19.8% to (euro)1,173.2 million in 2004 (excluding an expense of (euro)10.6 million resulting from the depreciation of the Argentine peso against the euro) compared to (euro)1,462.6 million in 2003 (excluding a (euro)134.4 million profit generated by the appreciation of the Argentine peso and a (euro)267.5 million profit from the cancellation of U.S. dollar-denominated debt). This decrease in net financial expenses was due to a decrease in average net debt as well as a reduction of costs as a result of the decrease in average interest rates in Europe and Brazil in 2004.

Income (loss) before tax and minority interest

Income (loss) before tax and minority interest was (euro)4,397.0 million in 2004 compared to (euro)3,362.5 million in 2003.

Extraordinary revenues decreased to (euro)409.0 million in 2004 from (euro)1,167.2 million in the previous year, due principally to the capital gain for the sale of Antena3 TV for (euro)392.3 million recorded in 2003 and capital gains related to real estate disposals of (euro)39.3 million in 2004 compared to (euro)203.0 million in 2003.

Extraordinary expenses decreased to (euro)1,574.8 million in 2004 from (euro)2,416.8 in 2003. Extraordinary expenses for 2004 primarily related to a (euro)674.7 million provision related to the acceptance of early retirement benefits by employees of Telefonica de Espana under its labor reduction program, a (euro)273.5 million provision from the headcount reduction of Terra Networks and other personnel reorganizations within the Telefonica Group, and the anticipated writedown of (euro)101.5 million of goodwill in Telefonica UK.

Corporate income tax

The tax provision in 2004 was (euro)1,138.7 million compared to (euro)913.4 million 2003. The increase was primarily due to an increase in revenues from operations.

Minority interests

Profit attributable to minority interests was (euro)381.0 million in 2004 compared to (euro)245.5 million in 2003. The 55.2% increase was principally due to net income recorded by Terra Networks, compared with a loss of (euro)2,203.6 in 2003.

Net income

Consolidated net income amounted to (euro)2,887.3 million in 2004 compared to net income of (euro)2,203.6 million in 2003.

Year Ended December 31, 2003 Compared with Year Ended December 31, 2002

The table below sets forth an analysis of consolidated revenue from operations for each of our principal business segments for 2002 and 2003 after elimination of sales to other members of the Telefonica Group. Financial data related to our business segments is included in Note 25 to our Consolidated Financial Statements.

	Year ended December 31, After adjustments for intra-group sales	
	2002	2003
	(in millions of euro)	
Telefonica de Espana	9,337.7	9,319.0
Telefonica Latinoamerica	6,822.8	6,150.3
Telefonia Moviles	7,993.0	8,905.1
Telefonica Empresas	1,445.3	1,425.6
Telefonica de Contenidos	1,068.1	1,374.5
Terra Lycos	546.3	414.5
Telefonica Publicidad e Informacion	503.5	525.8
Atento	216.4	191.7
Other companies(1)	478.1	93.4
Total Revenue from operations	28,411.3	28,399.8

----

(1) Includes revenue from operations from Telefonica, S.A., Grupo T. Gestiona and other subsidiaries.

The table below shows the contribution to our total revenues from operations of each of our principal lines of business for 2002 and 2003 after adjustments for sales to other members of the Telefonica Group.

	Year ended December 31,	
	After adjustments for intra-group sales	
	2002	2003
Telefonica de Espana	32.9%	32.8%
Telefonica Latinoamerica	24.0%	21.7%
Telefonica Moviles	28.1%	31.3%
Telefonica Empresas	5.1%	5.0%
Telefonica de Contenidos	3.8%	4.8%
Terra Lycos	1.9%	1.5%
Telefonica Publicidad e Informacion	1.8%	1.9%
Atento	0.8%	0.7%
Other companies	1.7%	0.3%
Total revenues from operations	100.0%	100.0%

---

(1) Includes revenue from operations from Telefonica, S.A., Grupo T. Gestiona and other subsidiaries.

The table below shows the contribution to our consolidated net income of each of our principal business lines in 2002 and 2003.

	Year ended December 31,	
	2002	2003
	(in millions of euro)	
Telefonica de Espana	807.93	178.08
Telefonica Latinoamerica	(182.54)	677.22
Telefonica Moviles	(3,744.47)	1,594.30
Telefonica Empresas	(728.25)	(74.66)
Telefonica de Contemdos	(669.15)	119.7
Terra Lycos	(2,008.87)	(172.71)
Telefonica Publicidad e Informacion	71.57	88.80
Atento	(99.09)	(16.25)
Other companies(1)	976.07	(190.89)
Total net income (loss)	(5,576.80)	2,203.59

---

(1) Includes net income from Telefonica, S.A. Grupo T. Gestiona and other subsidiaries.

Revenues from operations (sales to external clients)

Our revenue from operations, which accounted for 97.2% and 97.1% of our consolidated total revenues for 2003 and 2002, respectively, remained stable in 2003 at (euro)28,399.8 million compared to (euro)28,411.3 in 2002. The increase in revenue from Telefonica Moviles, Telefonica Latinoamerica, Telefonica Publicidad e Informacion, or TPI, Atento and Telefonica Empresas was offset by the negative exchange rate impact suffered in 2003. Exchange rate fluctuations had a negative impact of approximately 6.5% on our revenues from operations in 2003.

Whereas we calculate revenues from operations both before and after adjustments for sales to other members of the Telefonica Group, our analysis of revenue from operations is strictly limited to revenues from operations after adjustments for sales to other members of the Telefonica Group. In the aggregate, we believe that sales to other members of the Telefonica Group did not have a significant impact on the percentage fluctuations during the periods discussed.

Telefonica de Espana. Telefonica de Espana's revenues from operations decreased 0.2% to (euro)9,319.0 million in 2003 from (euro)9,337.7 in 2002. The stability in revenues compared to 2002 was principally due to the increase in revenues from IP Services and services provided to other operators.

- o Revenues from connection access fees include all revenues from our clients for rental and connection of PSTN lines (for basic telephony service), ISDN lines (for integration of voice, data and video services), Corporate Services and TUP (for public telephony service) and additional charges and publicity in telephone booths. Revenues for connection access fees decreased by 2% to (euro)2,795.2 million in 2003 compared to (euro)2,852.2 million in 2002. The decrease in revenue was due to a 2.0% decrease in the number of PSTN lines in service that was not offset by the 8% increase ((euro)0.94) in the PSTN monthly rental fee. This increase in the monthly rental fee was excluded from the price-cap on tariffs imposed by Spanish regulation.

- o Revenues from leased circuits include revenues received from leasing our circuits, both domestic and international, to customers and other telecommunication operators. Revenue from leased circuits decreased by 23.6% to (euro)195.0 million in 2003 compared to (euro)255.2 million in 2002. The decrease in revenue in 2003 was due to a decrease in the number of leased circuits as a result of customer migration to higher speeds, ADSL, and to the carrier capacity of wholesalers.

- o Revenues from the commercialization of handsets include all revenues from the sale, leasing, maintenance and installation of handsets. Revenues from the commercialization of handsets decreased by 3.1% to (euro)705.5 million in 2003 from (euro)728.3 million in 2002 as the result of a reduction in maintenance revenues due to a decreased number of users requiring maintenance for the period.

- o IP services revenues include all revenue from Telefonica de Espana's IP networks, and are principally composed of revenues from ADSL subscribers. Revenue from IP services increased by 119.2% to (euro)557.2 million in 2003 from (euro)254.2 million in 2002. This increase was principally due to a 76.5% increase in the number of ADSL retail subscriber connections in 2003 as compared to 2002, which led to a twofold increase in the revenues obtained from ADSL services in 2003 as compared to 2002. At the year-end 2003 we had 1,070.3 thousand ADSL retail subscribers compared to 606.4 thousand at the year-end 2002.

- Revenues from operator services include all revenues from operator services, national and international. International operator services include automatic access, transit, leasing capacity and manual international access. National operator services include national interconnection, rented subscriber loop and wholesale ADSL and commercial wholesale services (access, transit, traffic and support). Revenues from operator services increased by 4.7% to (euro)708.7 million from (euro)676.6 million in 2002, due to increases in the use of our rented subscriber loop and increases in wholesale ADSL services.

- Revenues from outgoing traffic, which include all revenues from net effective consumption and other consumption (including RPV, phone cards, messages, manual traffic), decreased 7.5% to (euro)3,639.3 million in 2003 from (euro)3,935.0 million in 2002. This decrease was due to the market recession, increased competition leading to a loss of market share and a 2% price reduction in 2003 as a result of a price-cap on tariffs imposed by Spanish regulation. See "Item 4--Information on the Company--Business Overview--Fixed-Line Telecommunications Services in Spain--Telefonica de Espana--Spain--Regulation".

Telefonica Moviles. Telefonica Moviles' revenue from operations increased 11.4% to (euro)8,905.1 million in 2003 from (euro)7,993.0 million in 2002. Exchange rate fluctuations had a negative impact of approximately 6.8%. Revenues from Telefonica Moviles' Spanish operations increased 15.3% to (euro)6,372.2 million in 2003 from (euro)5,528.7 million in 2002. This resulted primarily from a 6.8% increase in our customer base to 19.7 million at December 31, 2003 from 18.4 million at December 31, 2002, as well as increased customer usage.

Revenues from Telefonica Moviles' Latin American wireless operations increased 5.9% as measured in euro to (euro)2,529.5 million in 2003 from (euro)2,388.9 million in 2002, due principally to the negative impact of exchange rate fluctuations. Excluding the impact of exchange rate fluctuations, revenues from operations increased primarily due to the increase in the number of customers in Brazil and Mexico, full consolidation of twelve months of operations in Pegaso in 2003 compared to three months of operations in 2002, and consolidation of the Brazilian Joint Venture in 2003 compared to our participations in TeleSudeste, Teleleste and CRT in 2002.

Telefonica Latinoamerica. Telefonica Latinoamerica's operating revenues decreased by 9.9% to (euro)6,150.3 million in 2003 from (euro)6,822.8 million in 2002 principally as a result of the decline in value of local currencies, with

the exception of the Chilean peso. Exchange rate fluctuations had a negative impact of approximately 16.6%. Excluding the impact of exchange rate fluctuations, revenues from operations increased by 6.7%. In local currency, revenues from Telesp's operations increased principally due to the increase in the tariffs and the expansion of broadband and long distance services. Telefonica de Argentina's revenues from operations increased due to improved economic conditions in Argentina, increases in network traffic and increases in tariffs due to the application of the CER index (wholesaler inflation indexation) to wholesale contracts. Telefonica del Peru and CTC's operating revenues decreased in 2003 compared to 2002. Operating revenues of Telefonica del Peru decreased due to the launch of new tariff plans with lower average tariffs. Operating revenues of CTC decreased due to decreases in network traffic, influenced by customers increasingly substituting fixed line services by mobile telephony services.

- Revenues from operations generated by Telesp denominated in euro decreased 8.1% (an increase of 15.4% as measured in Brazilian reais) to (euro)3,343.2 million in 2003 from (euro)3,638.0 million in 2002. This was principally due to the depreciation of the Brazilian real against the euro. The value of the Brazilian real declined 20.3% compared to the euro, based on average exchange rates for 2003 and 2002. The increase in revenues from operations, as measured in Brazilian reais, was mainly due to an increase in tariffs (17% average increase in tariffs for local calls (as measured in local currency)) effective from July 2003, as well as an increase in broadband revenues and an increase in the long distance market share.

- Revenues from operations generated by Telefonica de Argentina denominated in euro increased 2.5% (an increase of 14.3% as measured in Argentine pesos) to (euro)747.8 million in 2003 from (euro)729.5 million in 2002. The increase in revenues from operations, as measured in Argentine pesos, was mainly due to the improvement of general economic conditions, the application of the CER Index and a 10.2% increase in total traffic per line per day.

- Revenues from operations generated by Compania de Telecomunicaciones de Chile denominated in euro decreased 14.6% (a decline of 15.2% as measured in Chilean pesos) to (euro)963.5 million in 2003 from (euro)1,128.3 million in 2002. This change was in part influenced by the change in the scope of consolidation following the sale of 25% of Sonda in September 2002. Sonda was previously fully consolidated in our financial statements. Excluding the in our scope of consolidation, the decrease in Chilean pesos would have been 7.0%, due to the fall in the long distance market and decreases in network traffic, influenced by customers increasingly substituting fixed line services by mobile telephony services.

- Revenues from operations generated by Telefonica del Peru denominated in euro decreased approximately 16.6% (a decline of 1.5% as measured in Peruvian nuevos soles) to (euro)1,041.6 million in 2003 from (euro)1,248.7 million in 2002, principally due to the launch of the new tariff plans starting in March, following the Peruvian Government's proposal to eliminate monthly rental fees, and as a result of increased competition from the mobile business.

Telefonica Empresas. Telefonica Empresas' revenue from operations decreased 1.4% to (euro)1,425.6 million in 2003 from (euro)1,445.3 million in 2002, principally due to change in the scope of consolidation after the accounting of Atlanet by the equity method from July 2002. In October 2003, Atlanet was sold to Fiat Gestione Participacione S.p.A.

Terra Lycos. Terra Lycos' revenues from operations decreased 24% to (euro)414.5 million in 2003 from (euro)546.3 million in 2002. This decrease is principally due to the global economic slowdown in advertising, the end of the agreement with Bertelsmann at the end of 2002 and the depreciation of certain currencies against the euro from which Terra Lycos obtains its revenues outside Spain. The decrease in revenues from operations was partially offset by an increase in number of subscribers for Internet access and communication and portal services due to the success of the OBP (Open, Basic, Premium) model initiated in 2001. Exchange rate fluctuations had a negative impact of approximately 11%.

Telefonica de Contenidos Group (formerly Admira). Telefonica de Contenidos

Group's revenues from operations increased 28.7% to (euro)1,374.5 million in 2003 from (euro)1,068.1 million in 2002, principally due to changes in the scope of consolidation as participation in Antena 3 Group was not consolidated through the global method in 2002. During the first semester of 2003 Antena 3 was fully consolidated. Impact of the change in consolidation

methods of Antena 3 Group explains a (euro)303.8 million increase in revenues. The increase was also due to the recuperation of the Argentine peso and advertising in the Argentine market, which have enabled Atco to increase its revenues to (euro)72.0 million in 2003 from (euro)54.6 million in 2002.

Others. Revenues from operations from our other businesses decreased 32.3% to (euro)810.9 million in 2003 from (euro)1,198 million in 2002. Revenue from operations from Atento decreased 11.4% to (euro)191.7 million in 2003 from (euro)216.4 million in 2002 principally due to exchange rate fluctuations, which had a negative impact of approximately 16.6%. Excluding the impact of exchange rate fluctuation, revenues increased 5.1% due mainly to an increase in revenues in most of Atento's markets, which offset decreases in revenue in Morocco and decreases in revenue due to the sale of Atento's operations in Japan. Telefonica Publicidad e Informacion's revenues from operations increased 4.4% to (euro)525.8 million in 2003 from (euro)503.5 million in 2002 due to the growth in revenues of all subsidiaries as measured in local currencies.

Total expenses (operating expenses and other operating expenses)

Operating expenses, which consist of increase in inventories (net), goods purchased, external services and local taxes and personnel costs decreased 3.8% to (euro)16,136.9 million in 2003 from (euro)16,773.3 million in 2002, principally due to decreased operating expenses at Telefonica Latinoamerica, Telefonica de Espana, Telefonica Empresas, Terra Lycos, and Atento, offset in part by an increase in operating expenses at Telefonica Moviles, Telefonica Publicidad e Informacion and Telefonica de Contenidos. Other operating expenses and trade provisions decreased 35% to (euro)480.9 million in 2003 from (euro)739.3 million in 2002, due to a decrease in trade provisions at Telefonica Latinoamerica, Telefonica de Espana and Telefonica Moviles.

Telefonica de Espana. For the business line headed by Telefonica de Espana, operating expenses decreased by 1.2% to (euro)5,795.6 million compared to (euro)5,868.6 million in 2002. This decrease was due to a decrease in goods purchased together with the decrease in personnel expenses recorded during the last quarter as a result of the approval of a labor reduction program in July 2003 (Plan Social de Expediente de Regulacion de Empleo) for 2003-2007 at Telefonica de Espana.

Goods purchased by the business line headed by Telefonica de Espana in Spain decreased 6.5% to (euro)2,490.3 million in 2003 from (euro)2,662.1 million in 2002. This decrease was due to a reduction in fixed-mobile interconnection tariffs with Telefonica de Espana's mobile operators and to a decrease in the expenses for the acquisition of equipment.

Personnel expenses increased 0.9% to (euro)2,174.9 million in 2003 from (euro)2,156.5 million in 2002. The operating company, Telefonica de Espana S.A., accounts for 97.8% of all personnel expenses, a 1% increase compared to last year due to an increase in salaries, partially offset in the last quarter of 2003 by the launch of the Telefonica de Espana labor reduction program. Personnel expenses in 2003 includes the impact related to 5,489 employees leaving under the labor reduction program approved in July 2003. At year-end

2003, Telefonica de Espana had 35,216 employees, a 13.4% decrease when compared to 2002.

External services increased 7.9% to (euro)956.6 million in 2003 from (euro)886.3 million in 2002. This increase is mainly due to commercial efforts carried out to develop ADSL services and to launch the "combinados", which is a consumer plan that combines access and traffic, allowing each client to optimize its consumption according to volume of use, destination and calling time profile.

Other operating expenses decreased by 55.4% primarily due to an increase in the amount of account receivables paid in 2003 which led to a 42.7% decrease in our provisions for bad debt.

Telefonica Moviles. Operating expenses at Telefonica Moviles increased 5% to (euro)5,881.3 million in 2003 from (euro)5,600.3 million in 2002, principally due to a 6.9% increase in the cost of goods purchased to (euro)2,747.0 million in 2003 from (euro)2,571.1 million in 2002, and a 6.6% increase in external services costs and taxes to (euro)2,625.7 million in 2003 from (euro)2,462.5 million in 2002.

Goods purchased (including interconnection costs) at Telefonica Moviles' Spanish operations increased 9.7% to (euro)1,799.0 million in 2003 from (euro)1,640.0 million in 2002, mainly due to the increase in the commercial activity and in

outgoing traffic to other networks, generating an increase in the interconnection expenses. External services at Telefonica Moviles' Spanish operations increased 6.3% to (euro)1,557.0 million in 2003 from (euro)1,465.0 million in 2002, principally due to the greater commercial activity. Personnel expenses at Telefonica Moviles' Spanish operations increased 4.8% to (euro)238 million in 2003 from (euro)227 million in 2002 due to a 1.6% increase in headcount for the period.

Goods purchased (including interconnection costs) at Telefonica Moviles' Latin American operations increased 12.3% to (euro)929.9 million in 2003 from (euro)828.1 million in 2002 primarily as a result of the increase in commercial activity in Brazil, Mexico and Argentina, and of changes in the scope of consolidation of the operations in Brazil and Mexico mentioned above. External services at Telefonica Moviles' Latin American operations increased 29.2% to (euro)1082.7 million in 2003 from (euro)838.0 million in 2002, principally due to the same reasons as the increases in goods purchased. Personnel expenses at Telefonica Moviles' Latin American operations increased 2.5% to (euro)217.7 million in 2003 from (euro)212.5 million in 2002. The increase in personnel expenses is low despite the changes in the consolidation of Brazil and Mexico operations in 2003 compared to 2002.

Telefonica Latinoamerica. Telefonica Latinoamerica's operating expenses decreased 5.7% to (euro)3,215.0 million in 2003 compared with (euro)3,407.5 million in 2002, principally as a result of the depreciation of Latin American currencies during 2003. Excluding the impact of exchange rate fluctuation, operating expenses increased approximately 11.3%, due to an increase in the long distance and ADSL activity in Brazil and to the new tariff plans and ADSL in Peru that offset the strict cost reduction policy in Argentina and the decrease in activity and cost reduction policy in Chile.

Other operating expenses decreased 23.9% to (euro)234.3 million in 2003 from (euro)307.9 million in 2002.

- o Telesp's operating expenses increased 0.9% in 2003 (an increase of 26.6% as measured in Brazilian reais, mainly due to the expansion of the new long distance business, to the acceleration of the broadband deploy and to the price increase of the contracts indexed to inflation). Other operating expenses, which in euro decreased 7.1%, increased 16.6% in local currency, due principally to provisions for bad debt linked to an increase in the amounts billed to customers.

- o Telefonica de Argentina's operating expenses decreased 3.3% in 2003 (an increase of 7.8% as measured in Argentine pesos, principally due to the increase in the personnel expenses, in part related to an increase in salaries indexed to inflation, goods purchased as a result of increased commercial activity, and a small increase in external services). Other operating expenses were (euro)3.4 million in 2003 as compared to negative (euro)55.0 million in 2002. The positive result with respect to other operating expenses was primarily due to the effective management of bad debt, as a result of the launch of specific products in the market to maximize debt recovery and ensuring that profitable customers are maintained.

- o Compania de Telecomunicaciones de Chile's operating expenses decreased 15.8% to (euro)541.2 in 2003 (a decrease of 16.4% as measured in Chilean pesos), mainly due to the change in the scope of consolidation following the sale of 25% of Sonda in September 2002. Personnel expenses decreased as the result of reductions in headcount and the reduction of interconnection costs due to the decrease in traffic.

- o Telefonica del Peru's operating expenses decreased 9.4% to (euro)667.5 million in 2003 (an increase of 7% as measured in Peruvian nuevos soles), principally as a result of the expenses related to the new commercial plans and to the expansion of the broadband business.

Telefonica Empresas. Telefonica Empresas' operating expenses decreased by 8.6% to (euro)1,486.9 million in 2003 from (euro)1,626.4 million in 2002, mainly due to the change to equity method accounting of Atlanet from July 2002 and to the cost control measures.

Terra Lycos. Terra Lycos' operating expenses decreased 22% to (euro)577.8 million in 2003 from (euro)741.5 million in 2002, principally due to effective management, improvements in efficiency, personnel reduction and less sales and marketing expenses.

- o Goods purchased decreased 9.5% to (euro)265.8 million in 2003 from (euro)293.6 million in 2002, principally due to the reductions observed in practically all items and particularly in communication costs. Personnel expenses decreased 28% to (euro)119.7 million in 2003 from (euro)165.4 million in 2002, principally due to workforce reductions. Personnel expenses from Lycos accounted for 35% of Terra Lycos' total personnel expenses.

- o External services decreased 33% to (euro)182.4 million in 2003 from (euro)273.7 million in 2002 as a result of successful cost control with respect to all expenses, particularly those relating to marketing and professional services.

Telefonica de Contenidos (formerly Admira). Telefonica de Contenidos' operating expenses increased approximately 22.3% to (euro)1,179.7 million in 2003 from (euro)964.4 million in 2002, due principally to changes in the scope of consolidation as our participation in the Antena 3 Group was not consolidated through the global method in 2002. During the first semester of 2003 Antena 3 was fully consolidated.

Others. Operating expenses of our other businesses decreased 70.7% to (euro)1,256.1 million in 2003 from (euro)4,280.3 million in 2002. Atento's operating expenses decreased 16.5% in 2003 due to the negative impact of exchange rate fluctuations of the Latin American currencies, and to the cost control, both operating and structural. Operating expenses for Telefonica Publicidad e Informacion increased by 4.0% due mainly to the increase of external services, including the expenses for telephone platform 11888.

Operating profit before depreciation and amortization

Our management believes that operating profit before depreciation and amortization is meaningful for investors because it provides an analysis of our operating results and our segment profitability using the same measure used by our chief operating decision makers. See "Item 5. Operating and Financial Review and Prospects -- Presentation of Financial Information -- Non-GAAP Financial Information". The following table provides a reconciliation of operating profit before depreciation and amortization to operating profit for the Telefonica Group for the periods indicated on a segment basis.

	Year ended December 31, 2003						
	Telefonica de Espana	Telefonica Moviles	Telefonica Latinoamerica	Telefonica Contenidos	Terra Lycos	Telefonica Empresas	Telefon Holdi
	(in millions of euro)						
Operating profit before depreciation and amortization expenses.......	4,534.16 8	4,581.90	3,065.28	210.33	(39.49)	304.38	(223
Depreciation and amortization expenses.......	2,567.98	1,516.04	1,718.79	49.93	78.74	245.65	47
Operating profit..	1,966.18	3,065.87	1,346.48	160.40	(118.23)	58.73	(271

	Year ended December 31, 2002						
	Telefonica de Espana	Telefonica Moviles	Telefonica Latinoamerica	Telefonica Contenidos	Terra Lycos	Telefonica Empresas	Telefon Holdi
	(in millions of euro)						
Operating profit before depreciation and amortization expenses.......	4,517.24	3,830.00	3,346.74	114.50	(141.69)	128.58	(231.
Depreciation and	2,701.82	1,391.88	1,999.41	49.58	142.72	292.10	57.

amortization expenses.......							
Operating Profit..	1,815.42	2,438.12	1,347.34	64.92	(284.41)	(163.52)	(288.

Our operating profit before depreciation and amortization increased 7.5% to (euro)12,602.1 million in 2003 from (euro)11,724.2 million in 2002, due to the increases of operating profit before depreciation and amortization at

Telefonica Moviles, Telefonica de Espana, Telefonica de Empresas, Telefonica Publicidad e Informacion, Telefonica de Contenidos and Atento. Operating profit before depreciation and amortization also increased at Terra Lycos, which recorded negative operating profit before depreciation and amortization. This offsets the decrease in Telefonica Latinoamerica due to the exchange rate fluctuations in Latin America. Exchange rate fluctuations had a negative impact of approximately 6%.

Telefonica de Espana. Telefonica de Espana Group's operating profit before depreciation and amortization increased 0.4% to (euro)4,534.2 million in 2003 from (euro)4,517.2 million in 2002. This increase was mainly due to cost reduction savings principally due to a 42.7% decrease in bad debt provisions.

Telefonica Latinoamerica. Telefonica Latinoamerica's operating profit before depreciation and amortization decreased 8.4% to (euro)3,065.3 million in 2003 from (euro)3,346.7 million in 2002, as a result of the decrease in euro demonstrated by all companies, except Argentina. Excluding the impact of exchange rate fluctuation, Telefonica Latinoamerica's operating profit before depreciation and amortization increased 8.6% mainly due to increases of operating profit before depreciation and amortization in local currencies of Telesp (10.3%) and, Telefonica de Argentina (39.9%), which offset decreases of operating profit before depreciation and amortization in local currencies of Compania de Telecommunicaciones de Chile (5.8%) and Telefonica del Peru (8.1%).

- Telesp's operating profit before depreciation and amortization decreased 12.2% (an increase of 10.3% as measured in Brazilian reais) in 2003 to (euro)1,672.1 million from (euro)1,903.7 million in 2002. The increase in local currency was principally due to a 17% average increase in tariffs for local calls (as measured in local currency) effected in July 2003, and the good performance of Telesp's ADSL and long distance business. This increase offset an increase in expenses following the increase in commercial activity and in the provisions for bad debt.

- Telefonica de Argentina's operating profit before depreciation and amortization increased 25.5% (an increase of 39.9% as measured in Argentine pesos) in 2003 to (euro)453.9 million from (euro)361.7 million in 2002. The increase was principally due to the improvement of the main operational indicators (especially plant and traffic), and to the reduction of bad debt due to the timely customer payment during the year and to the collection of payments provisioned over the last years.

- Compania de Telecomunicaciones de Chile's operating profit before depreciation and amortization decreased 5.2% (a decrease of 5.8% as measured in Chilean pesos) in 2003 to (euro)448.7 million from (euro)473.1 in 2002. This reduction was principally due to the change in the scope of consolidation following the sale of 25% of Sonda in

September 2002 and a decrease in revenues, which could not be offset by cost containment measures. Revenues decreased due to the reduction in the long distance market and decreases in network traffic, influenced by customers increasingly substituting fixed line services by mobile telephony services.

- o Telefonica del Peru's operating profit before depreciation and amortization decreased 22.2% (a decrease of 8.1% in Peruvian nuevos soles) in 2003 to (euro)405.3 million from (euro)521.0 million in 2002. The small increase on revenues from operations (due to the launching of new tariff plans and influenced by the decrease revenues from public telephony and the increasing competition in long distance) could not offset the increase in expenses relating to the new commercial plans, the ADSL expansion and the increase in fixed-to-mobile traffic.

Telefonica Moviles. Telefonica Moviles' operating profit before depreciation and amortization increased 19.6% to (euro)4,581.9 million in 2003 from (euro)3,830.0 million in 2002 due principally to a significant increase in operating profit before depreciation and amortization for Telefonica Moviles' Spanish operations. Exchange rate fluctuations had a negative impact of approximately 3.4%.

Telefonica Empresas. Telefonica Empresas' operating profit before depreciation and amortization increased 136.7% to (euro)304.4 million in 2003 from (euro)128.6 million in 2002, due principally to significant cost containment efforts in a macroeconomic environment unfavorable to the generation of new revenues.

Terra Lycos. Terra Lycos had negative operating profit before depreciation and amortization of (euro)39.5 million in 2003 compared to negative operating profit before depreciation and amortization of (euro)141.7 million in 2002 due to successful cost containment measures.

Telefonica de Contenidos (former Admira). Telefonica de Contenidos' operating profit before depreciation and amortization increased 83.3% to (euro)210.3 million from (euro)114.5 million in 2002. The principal reasons for this increase was the change in accounting relating to the Antena 3 Group. Also affecting the increase was the increasing margins in Endemol and the effect of the cost cutting measures in the holding Telefonica de Contenidos.

Others. Operating profit before depreciation and amortization of our other businesses increased 15.6% to (euro)268.0 million in 2003 from (euro)231.8 million in 2002. Atento's operating profit before depreciation and amortization increased 22.4% to (euro)66.5 million in 2003 from (euro)54.3 million in 2002. Exchange rate fluctuations had a negative impact of approximately 23.3%. Growth for Atento was due principally to the increase of the profit margins in Brazil, Venezuela, Colombia, Mexico and Central America, and the control exercised over operating and fixed costs during the year. Telefonica Publicidad e Informacion's operating profit before depreciation and amortization increased 22.0% due mainly to the growth in Spain and to the improvement of the negative operating profit before depreciation and amortization in Brazil due to the operating cost containment measures.

Depreciation and amortization

Consolidated depreciation and amortization decreased 6.2% to 6,274.2

million in 2003 from 6,692.4 million in 2002. This increase was due in large part to a controlled and conservative investment policy implemented over the last years. Exchange rate fluctuations had a positive impact of approximately 7.5%.

Telefonica de Espana. Depreciation and amortization of Telefonica de Espana Group decreased 5.0% to (euro)2,568.0 million in 2003 from (euro)2,701.8 million in 2002, due to a more controlled and conservative investment policy implemented over the last years and the increase of totally amortized elements.

Telefonica Latinoamerica. Depreciation and amortization of Telefonica Latinoamerica decreased 14.0% to (euro)1,718.8 million in 2003 from (euro)1,999.4 million in 2002. Excluding the impact of exchange rate fluctuations, depreciation and amortization remained stable when compared with the previous year, due to a more controlled and conservative investment policy implemented in 2003.

Telefonica Moviles. Depreciation and amortization of Telefonica Moviles increased 8.9% to (euro)1,516.0 million in 2003 from (euro)1,391.9 million in 2002. Excluding the impact of exchange rate fluctuations, depreciation and amortization increase by 21.26%. This increase was principally due to the increase of the amortization expense due to the changes in the scope of consolidation of the Telefonica Moviles' operations in Brazil and Mexico mentioned above.

Telefonica Empresas. Depreciation and amortization of Telefonica Empresas decreased 15.9% to (euro)245.7 million in 2003 from (euro)292.1 million in 2002.

Terra Lycos. Depreciation and amortization of Terra Lycos decreased 44.8% to (euro)78.7 million in 2003 from (euro)142.7 million in 2002 due to the write-off of start-up and intangible assets recorded in 2002.

Telefonica de Contenidos. Depreciation and amortization of Telefonica de Contenidos (formerly Admira) remained stable when compared with the previous year amounting to (euro)49.9 million in 2003.

Others. Depreciation and amortization of our other businesses decreased to (euro)108.2 million in 2003 from (euro)133.11 million in 2002. Atento's depreciation and amortization decreased 30.7% to (euro)52.2 million in 2003 from (euro)75.4 million in 2002. Telefonica Publicidad e Informacion's depreciation and amortization in 2003 amounted to (euro)30.8 million, a 1.3% decrease when compared to 2002.

Operating profit

Operating profit increased 25.8% to (euro)6,327.9 million in 2003 from (euro)5,031.7 million in 2002. This increase compared to last year is the result of the increase in operating profit before depreciation and amortization and of the 6.2% decrease in amortization.

Telefonica de Espana. Operating profit of Telefonica de Espana Group increased 8.3% to (euro)1,966.2 million in 2003 from (euro)1,815.4 million in 2002, mainly due to a 5.0% decrease in the amortization of fixed assets during the period, compared to 2002.

Telefonica Latinoamerica. Operating profit at Telefonica Latinoamerica decreased by 0.1% to (euro)1,346.5 million in 2003 from (euro)1,347.3 million in 2002, mainly due to a 8.4% decrease in operating profit before depreciation and amortization which was offset in part by a 14% decrease in amortization. Excluding the impact of exchange rate fluctuations, operating profit increased by 21.6%.

Telefonica Moviles. Operating profit of Telefonica Moviles increased 25.8% to (euro)3,065.9 million in 2003 from (euro)2,438.1 million in 2002, mainly due to a 19.6% increase in operating profit before depreciation and amortization, offset in part by a 8.9% increase in depreciation expense.

Telefonica Empresas. Operating profit of Telefonica Empresas in 2003 was approximately (euro)58.7 million compared to an operating loss of (euro)163.5 million during 2002, mainly due to the fact that operating profit before depreciation and amortization increased by 136.7% and amortization expense decreased by 15.9%.

Terra Lycos. Terra Lycos' operating loss in 2003 was (euro)118.2 million compared to an operating loss of (euro)284.4 million during 2002, mainly due to the decrease in negative operating profit before depreciation and to a 44% decrease in the depreciation and amortization expense during 2003.

Telefonica de Contenidos. Operating profit of Telefonica de Contenidos' (formerly Admira) was (euro)160.4 million in 2003 compared to (euro)64.9 million in 2002.

Others. Operating profit of our other businesses increased to (euro)159.8 million in 2003 from (euro)98.7 million in 2002 due to a 15.6% increase in operating profit before depreciation and amortization and to a 18.7% decrease in depreciation and amortization. Atento's operating profits were (euro)14.3 million in 2003 compared to an operating loss of (euro)21.1 million in 2002. This improvement is due to the increase in operating profit before depreciation and amortization together with a 30.8% decrease of amortization. Telefonica Publicidad e Informacion's operating profit in 2003 was (euro)153.3 million, a 28.1% increase when compared to 2002 mainly due to a 22.0% increase in operating profit before depreciation and amortization, offset in part by a 1.3% increase in depreciation and amortization.

Profit from ordinary activities

Profit from ordinary activities, which consists of operating profit, amortization of goodwill, financial income (expense), exchange gains (losses) and income (loss) from associated companies, increased 185.3%, to (euro)4,612.2 million in 2003 from (euro)1,616.8 million in 2002. In addition to the 25.8% increase in the operating profit, the growth rate is mainly due to:

o the negative results for associates were reduced over 2003 by 59.7% to (euro)212.6 million from (euro)527.9 million in 2002 as a result of both the sale of certain subsidiaries (ETI Austria, Data Uruguay, Azul TV in 2002, and Antena3 TV and Atlanet in 2003) and the smaller losses related to IPSE-2000, Medi Telecom, Pearson and Via Digital (Sogecable was included in the consolidated accounts in July 2003).

o the improvement in the goodwill amortization which decreased 33.5% compared to 2002 to (euro)442.5 million, following write-offs at Terra Lycos, Telefonica Deutschland, lobox and Pearson carried out in 2003. Goodwill of our mobile businesses increased by 14.6% as compared to last year, principally due to the acquisitions of Pegaso in September 2002 and TCO in May 2003; and

o a 52.3% decrease in net financial expense to (euro)1,060.7 million in 2003 from (euro)2,221.6 in 2002, including a positive impact from the appreciation of the Argentinean peso of (euro)134.4 million. Excluding the impact of exchange rate fluctuations, the financial result rose to (euro)1,195.1 million, which meant a drop of 29.4% compared to the comparable financial results for 2002 ((euro)1,692.8 million). Out of that percentage, 15.8

percentage points were due to the positive result of (euro)267.5 million coming from the cancellation of US dollars denominated debt. Excluding also this positive result, 2003 financial results would have totaled (euro)1,462.6 million, falling 13.6% versus the above-mentioned comparable figure of 2002. Net financial debt of Telefonica Group reached (euro)19,235.3 million as of December 2003, decreasing (euro)3,297.8 million from 2002.

Income (loss) before tax and minority interest

Income (loss) before tax and minority interest consists of profit (loss) from ordinary activities, extraordinary income, losses on sales of fixed assets and extraordinary expenses. Income before tax and minority interest was (euro)3,362.5 million in 2003 compared to a loss of (euro)14,601.1 million in 2002.

This principal cause for the increase was due to extraordinary losses in 2002 ((euro)16,217.9 million) related to the assets and restructuring costs of UMTS and those of Terra Lycos, Telefonica Deutschland and Pearson that were accounted for last year.

Extraordinary revenues increased to (euro)1,167.2 million in 2003 from (euro)474.6 million in the previous year, due principally to the capital gain for the sale of Antena3 TV for (euro)392.3 million and the net capital gain related to real estate disposals amounting to (euro)180.9 million.

Extraordinary expenses decreased to (euro)2,416.8 million in 2003 from (euro)16,692.5 in 2002. Extraordinary expenses for 2003 primarily related to the provision relating to the 5,489 employees that participated in the "Streamlining Social Plan" 2003-2007 ((euro)1,372.3 million) and the costs associated to the different contingencies and compensation for workforce reduction at Telesp and Telefonica del Peru.

Corporate income tax

The provision for corporate income tax expense at the consolidated level was (euro)913.4 million compared to the fiscal credit that arose in 2002 due to the depreciation in value (provision for investment valuation allowances, deductible) of European subsidiaries that were awarded UMTS licenses.

Minority interests

Profit attributable to minority interests was (euro)245.5 million in 2003 compared to a loss attributable of (euro)5,795.6 million in 2002, primarily due to (euro)4,600 million losses by the Telefonica Moviles group relating to the write-off of UMTS assets in Europe and (euro)900 million of extraordinary expenses incurred by Terra Lycos in 2002. The improved performance in 2003 was mainly due to the smaller losses in Terra Lycos and higher net income in the companies operated by Telefonica Latinoamerica.

Net income

Consolidated net income amounted to (euro)2,203.6 million in 2003 compared to a loss of (euro)5,576.8 million in 2002.

Material Differences Between U.S. GAAP and Spanish GAAP

The principal differences between U.S. GAAP and Spanish GAAP relevant to us are discussed below. See also note 25 to the Consolidated Financial Statements included elsewhere herein.

- We have performed in 2003 and prior years some business combinations accounted for under Spanish GAAP using the pooling of interest method. Under U.S. GAAP, these acquisitions were recorded using the purchase accounting method. In the case where a capital increase in a subsidiary is carried out to effect a business combination that is part of a broader corporate reorganization and which is accounted for using the purchase accounting method, under U.S. GAAP Telefonica recognizes the increase in its investment as a result of the capital increase by crediting shareholders' equity.

- Prior to 1988, Spanish GAAP permitted the revaluation of fixed assets. As a result of such revaluation, in years prior to 1988, we stated our property, plant and equipment at the then current replacement cost less

accumulated depreciation, and credited the revaluations to the surplus account shown on the balance sheet under "other reserves". Depreciation was calculated each year based on the then current gross replacement cost using estimated remaining useful lives. Between 1988 and 1995, Spanish GAAP did not permit such revaluations, and we used historical cost basis accounting. In 1996, new legislation permitted us to write up the value of certain of our assets. This write-up was reversed in the reconciliation to U.S. GAAP of shareholders' equity.

- In accordance with Spanish GAAP, interest incurred during periods exceeding 12 months in which assets are under construction may be capitalized. However, interest incurred during periods in which qualifying assets are under construction are capitalized and amortized over such qualifying asset's expected life under U.S. GAAP.

- Start-up costs are capitalized under Spanish GAAP, but expensed under U.S. GAAP.

- Spanish GAAP requires that research and development expenses and capital increase expenses be capitalized and amortized over a period not exceeding five years. Such expenses are expensed in current periods and reduced from capital proceeds, respectively, under U.S. GAAP.

- Under Spanish GAAP, provisions are recorded for early retirement expenses in the period during which management announces the early retirement programs. Under U.S. GAAP, early retirement provisions are recorded in the period during which an agreement is reached with the employee.

- Under Spanish GAAP exchange gains may be deferred. Under U.S. GAAP, exchange gains are included in income on a current basis.

- Under Spanish GAAP, revenues and expenses are recognized on accrual basis, i.e., when the goods and services are actually provided, regardless of when the resulting monetary or financial flow occurs. Under U.S. GAAP, according to SAB 104, some revenues must be deferred.

- SFAS No. 115 requires certain investments in financial assets to be classified on the basis of the purpose for which they were acquired (held-to-maturity securities, trading securities or available-for-sale securities). The treatment of the unrealized gains and losses differs depending on the classification:

- unrealized gains and losses (other than permanent diminutions in value) on securities that we consider held-to-maturity are not recorded.

- unrealized gains and losses on securities considered available-for-sale are not recorded in the income statement but included as a separate equity caption.

- unrealized gains or losses on trading securities are recorded in the income statement.

These criteria differ from Spanish GAAP.

- Under Spanish GAAP, derivatives not assigned as hedge are accounted for at the lower of their cost or market value and those assigned as hedge generally are considered a change in hedge item characteristics. Under U.S. GAAP all derivatives are accounted at fair value through earnings and all derivatives assigned as hedge instruments may have a different accounting or require its hedge item also to be accounted at fair value. Additionally, measuring hedge ineffectiveness differs between Spanish and U.S. GAAP.

- Under Spanish GAAP, goodwill is amortized on a straight-line basis over the expected life of asset. Under U.S. GAAP, in accordance with SFAS No. 142, goodwill and intangible assets deemed to have indefinite lives should no longer be amortized but instead are subject to periodic impairment testing under a fair value approach. SFAS No. 142 requires the testing of all goodwill and intangibles deemed to have indefinite lives for impairment as of January 1, 2002.

- Under Spanish GAAP, companies in which significant influence is maintained over the management are carried by the equity method and investments in companies in which a company owns less than 50% but

has the majority of the common voting stock or are controlled by a company must be consolidated. In addition, a holder of at least 20% or 3%, for listed investments, presumes a significant influence. In general, under U.S. GAAP, only companies in which a holding of between 20% and 50% is owned are carried by the equity method, unless there is evidence that significant influence is exercised over their management. Investee companies in which a participation above 50% and control rights exist are consolidated.

Under U.S. GAAP, shareholders' equity was (euro)16,314.6 million at December 31, 2004, compared with (euro)16,225.1 million under Spanish GAAP.

Under U.S. GAAP, shareholders' equity was (euro)17,291.4 million at December 31, 2003, compared with (euro)16,756.6 million under Spanish GAAP. Under U.S. GAAP, shareholders' equity was (euro)16,989.3 million at December 31, 2002, compared with (euro)16,996.0 million under Spanish GAAP.

Under U.S. GAAP, net income was (euro)2,578.0 million for the year ended December 31, 2004 compared to (euro)2,877.3 million under Spanish GAAP. Under U.S. GAAP, net income was (euro)2,686.1 million for the year ended December 31, 2003 compared with (euro)2,203.6 million under Spanish GAAP. Under U.S. GAAP, net income was negative (euro)5,214.5 million for the year ended December 31, 2002 compared with negative (euro)5,576.8 million under Spanish GAAP.

For additional information concerning significant differences between U.S. GAAP and Spanish GAAP, as well as a reconciliation of net income and shareholders' equity to U.S. GAAP, please see note 25 to the Consolidated Financial Statements included elsewhere herein.

New U.S. Accounting Pronouncements

Statements of Financial Accounting Standards No. 123 (Revised 2004): Share-Based Payment

In December 2004, the FASB issued SFAS No. 123 (revised 2004), Shared Based Payments (SFAS 123R). This statement eliminates the option to apply the intrinsic value measurement provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" to stock compensation awards issued to employees. Rather, SFAS 123R requires companies to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide services in exchange for the award--the requisite service period (usually the vesting period). SFAS 123R applies to all awards granted after the required effective date, December 15, 2005, and to awards modified, repurchased, or cancelled after that date. SFAS 123R will be effective for our fiscal year ending December 31, 2005. The Company does not anticipate that adoption of this Standard will have a material effect on its financial position, results of operations, or cash flows.

Statements of Financial Accounting Standards No. 151: Inventory Costs - An Amendment of ARB No. 43, Chapter 4

On November 24, 2004, the FASB issued SFAS No. 151, "Inventory Cost, a revision of ARB No. 43, Chapter 4". The amendments to SFAS No. 151 aim to improve financial information, stating that the expenses of inactive facilities, transportation costs, manipulation costs and scrap material costs should be recorded in the statement of operation as expenses of the period. The application of fixed cost to inventories should be based on the normal capacity of the production facilities.

SFAS No. 151 will be applicable to valuation of Inventories by the end of the first reporting period ending after June 15, 2005. The Company does not anticipate that the adoption of SFAS No. 151 will have a material impact on its financial position, cash flows or results of operations.

Statements of Financial Accounting Standards No. 153: Exchanges of Non-monetary Assets - An Amendment of APB Opinion No. 29

On December 16, 2004, the FASB issued SFAS N0.153, "Exchanges of Non-monetary Assets - an amendment of APB Opinion No. 29", which amends Accounting Principles Board Opinion No. 29 "Accounting for Nonmonetary Transactions". This amendment is based on the idea that exchange transactions should be valued in accordance with the value of the exchanged assets. The exception made for similar non-monetary productive assets is eliminated and substituted by a more extensive exception related to non-monetary assets with a non-commercial consideration. APB No. 29 stated that the exchange transaction of a productive asset for a similar one should be recorded at the book value of the exchanged asset.

SAS No. 153 will be applicable for non-monetary asset exchange transactions occurring in fiscal periods beginning after June 15, 2005. The Company does not anticipate that the adoption of SFAS No. 153 will have a material impact on its financial position, cash flows or results of operations.

SAB No. 107: Shared Based Payment

On March 29, 2005, the SEC released a Staff Accounting Bulletin (SAB) relating to the FASB accounting standard for stock options and other share-based payments. The interpretations in SAB No. 107, "Share-Based Payment," (SAB 107) express views of the SEC Staff regarding the application of SFAS No. 123 (revised 2004), "Share-Based Payment "(Statement 123R). Among other things, SAB 107 provides interpretive guidance related to the interaction between Statement 123R and certain SEC rules and regulations, as well as provides the Staff's views regarding the valuation of share-based payment arrangements for public companies. The Company does not anticipate that adoption of SAB 107 will have any effect on its financial position, results of operations or cash flows.

FIN No. 46 - Consolidation of Variable Interest Entities - an interpretation of ARB No. 51

In January 2003, the Financial Accounting Standards Board ("FASB") released Interpretation No. 46 Consolidation of Variable Interest Entities ("FIN 46") which requires that all primary beneficiaries of Variable Interest Entities (VIE) consolidate that entity. FIN 46 is effective immediately for VIEs created after January 31, 2003 and to VIEs in which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after June 15, 2003 to VIEs in which an enterprise holds a variable interest it acquired before February 1, 2003. In December 2003, the FASB published a revision to FIN 46 ("FIN 46R") to clarify some of the provisions of the interpretation and to defer the effective date of implementation for certain entities. Under the guidance of FIN 46R, entities that do not have interests in structures that are commonly referred to as special purpose entities are required to apply the provisions of the interpretation in financials statements for periods ending after March 14, 2004. As indicated in note 25.20.4 the only impact on the application of FIN 46 R was the desconsolidation of Telefonica Finance our trust preferred shares vehicle.

SAB No. 104 - Revenue Recognition and EITF 00-21

In December 2003, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 104, Revenue Recognition. SAB 104 updates portions of the interpretive guidance included in Topic 13 of the codification of Staff Accounting Bulletins in order to make this interpretive guidance consistent with current authoritative accounting and auditing guidance and SEC rules and regulations. The company believes it is currently following the guidance of SAB 104. SAB 104 also revises or rescinds certain interpretive guidance regarding SAB 101 that was in conflict with the provisions of EITF 00-21.

In 2004, The Company adopted EITF 00-21, 'Revenue Recognition' (SAB 104), which revises or rescinds certain interpretive guidance regarding SAB 101 that was in conflict with the provisions of EITF 00-21. The effects of this implementation are explained in Note 25.4.

EITF 04-1: Accounting for Preexisting Relationships between the Parties to a Business Combination

This Issue addresses the accounting for preexisting relationships between the parties to a business combination. The consensuses in this Issue should be applied to business combinations consummated and goodwill impairment tests performed in reporting periods beginning after October 13, 2004. The application of this new accounting literature by Telefonica had no impact on its financial position, cash flows or results of operations.

EITF Issue No. 01-08 - Determining Whether an Arrangement Contains a Lease

In May 2003, the EITF reached consensus in EITF Issue No. 01-08 to clarify the requirements of identifying whether an arrangement should be accounted for as a lease at its inception. The guidance in the consensus is designed to mandate reporting revenue as rental or leasing income that otherwise would be reported as part of product sales or service revenue. EITF Issue No. 01-08 requires both parties to an arrangement to determine whether a service contract or similar arrangement is, or includes, a lease within the scope of SFAS No. 13, "Accounting for Leases." The application of this EITF has not had any effect on The Company's financial position, cash flows or results of operations.

EITF Issue No. 03-11 - Reporting Realized Gains and Losses on Derivative Instruments That Are Subject to FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, and Not Held for Trading Purposes

In July 2003, the EITF reached consensus in EITF Issue No. 03-11 that determined whether realized gains and losses on derivative contracts not held for trading purposes should be reported on a net or gross basis is a matter of judgment that depends on the relevant facts and circumstances and the economic substance of the transaction. In analyzing the facts and circumstances, EITF Issue No. 99-19, and Opinion No. 29, "Accounting for Nonmonetary Transactions," should be considered. EITF Issue No. 03-11 is effective for transactions or arrangements entered into after September 30, 2003. The application of this EITF has not had any effect on The Company's financial position, cash flows or results of operations.

B. LIQUIDITY AND CAPITAL RESOURCES

Cash Flow Analysis

The table below sets forth our consolidated cash flows for the periods indicated. Positive figures refer to cash inflows and negative figures or those in brackets refer to cash outflows.

	Year ended December 31,		
	2002	2003	2004
	(in millions of euro)		
Net cash provided by operating activities........	8,814.6	9,191.1	10,186.8
Net cash used in investing activities...........	(5,780.2)	(5,171.7)	(8,978.7)

Net cash used in financing activities...........	(2,101.1)	(4,178.9)	(1,961.2)

A more detailed consolidated cash flow table is included in note 25 to the Consolidated Financial Statements for the year ended December 31, 2004.

Net Cash Provided by Operating Activities

Net cash provided by operating activities amounted to (euro)10,186.8 million in 2004, (euro)9,191.1 million in 2003 and (euro)8,814.6 million in 2002. Net cash provided by operating activities increased 10.8% in 2004 compared to 2003. This growth in 2004 was mainly due to the strong performance of cash received from customers. Net cash inflow from operating activities (which is a subtotal of cash received from customers minus cash paid to suppliers and employees and minus income taxes paid) increased 6.1% in 2004 to (euro)11,338.98 million from (euro)10,687.91 million in 2003. This variation was primarily due to cash received from customers, which totaled (euro)36,339.08 million at the end of 2004, an increase of 8.8% compared to 2003. This significant growth was provided by almost all business lines through commercial efforts and the increase in our client base and, in case of Telefonica Moviles, the integration of the new operators acquired from Bellsouth in Latin America in 2004. Net cash inflow from operating activities increased 2.9% in 2003 to (euro)10,687.91 million from (euro)10,384.3 million in 2002, due principally to to increases in cash provided by Telefonica Moviles.

In 2004, cash paid to suppliers and employees totaled (euro)24,674.10 million, 10.0% more than in 2003. These higher outflows were also mainly explained by larger payments of commercial and advertising expenses and handset purchases from the commercial efforts made by the Telefonica group during 2004 and, in the case of Telefonica Moviles Group, the incorporation of Bellsouth's Latin American operations in 2004. Payments to employees, however, decreased compared to 2003, mainly supported by the savings obtained through the 2003-2007 headcount reduction program at Telefonica de Espana.

Net cash outflow for interest paid less dividends and interest charged (which is a subtotal of dividends from associated companies plus net interest paid) decreased 23.0% to (euro)1,152.2 million in 2004 from (euro)1,496.9 million in

124

2003. This decrease was principally due to a decrease in net interest paid, which is the principal compenent of net cash outflow to (euro)1,223.4 million in 2004 from (euro)1,559.5 million in 2003. The principal reasons for the decrease in net interest paid were continued low interest rates combined with a average net financial debt reduction of approximately 7.1% at a consolidated level in 2004. Net cash outflow for interest paid less dividends and interest charged decreased 4.6% in 2003 to (euro)1,496.85 million from (euro)1,569.7 million in 2002, principally due to the decrease in net interest paid to (euro)1,559.5 million in 2003 from (euro)1,610.9 million in 2002.

Net Cash Used in Investing Activities

Net cash used in investing activities increased to (euro)8,978.7 million in 2004 from (euro)5,171.7 million in 2003, which was a decline from (euro)5,780.2 million in 2002. The principal components of net cash used in investing activities are:

- net cash outflow for capital expenditures (which is a subtotal of net payments for tangible and intangible assets and deferred charges and proceeds from sale of property, plant and equipment);

- and net cash outflow for investments in affiliates (which is a subtotal of proceeds from investments in affiliates, proceeds from capital grants, and purchase of new investments, net of cash acquired).

Net cash outflow for capital expenditures increased slightly to (euro)3,488.2 million in 2004 from (euro)3,483.8 million in 2003 compared to (euro)4,311.8 million in 2002. Our principal capital expenditures in 2004 amounted to (euro)1,305.8 million from Telefonica de Espana, (euro)1,385.7 million from our Telefonica Moviles and (euro)771.9 million from our Telefonica Latinoamerica. Other payments amounted to (euro)24.7 million, which relates to payments from our other business lines. The stability of net cash outflow for capital expenditures was due principally to a more controlled and conservative investment policy implemented in 2002 and 2003. During 2004 Telefonica de Espana continued to implement a policy of shifting its focus toward broadband by stepping up the deployment of ADSL technology and devoting greater resources to the growing Internet and multimedia businesses without neglecting the needs of its traditional business. Despite increasing its investment in broadband, the reduction of unit costs and the rationalization of investments (re-use of vacant infrastructure, process redesign, etc.) enabled Telefonica de Espana to significantly reduce its capital expenditures compared to 2003. The principal capital expenditures made by our mobile business in 2004 were investments in wireless telephony networks and technology. For example, our mobile business in Brazil invested to develop an enhanced version of its CDMA network and to increase its capacity and coverage. Our mobile business in Spain invested in its UMTS network and our mobile businesses in Argentina and Mexico invested to deploy the GSM network. Capital expenditures by our Latin American fixed line business rose in 2004, principally from increased investments in broadband technology made by our fixed line businesses in Argentina and Peru.

Net cash outflow for investments in affiliates increased 120.0% to (euro)6,380.9 million in 2004 from (euro)2,112.2 million in 2003. Our main investments in affiliates in 2004 were (euro)208.7 million related to tender offers to increase our interests in the Brasilcel subsidiaries, (euro)3,179.4 million for the acquisition of the Bellsouth's operators in Latin America and (euro)483.7 million for the acquisition of additional Portugal Telecom shares. Our main investments in affiliates in 2003 were (euro)1,030 million for the take-over bid of Terra Networks and (euro)461 million for the acquisition of Via Digital shares and its subsequent integration with Sogecable. Net cash outflow for investments in affiliates increased 35.7% to (euro)2,112.2 million in 2003 from (euro)1,556.5 million in 2002.

Net Cash Used by Financing Activities

Net cash used by financing activities decreased to (euro)1,961.2 million in 2004 from (euro)4,178.9 million in 2003. This was due principally to the proceeds, net of repayments, from other loans, credit facilities and notes payable, which amounted to (euro)2,113.4 million in 2004 compared to a negative figure of (euro)3,927.5 in 2003. Debentures and bonds redeemed, net of proceeds, amounted to (euro)1,217.6 million in 2004 compared to a negative figure of (euro)1,223.1 in 2003). Finally, dividends paid, net of proceeds from the issuance of stock, amounted to (euro)2,857.0 million in 2004 compared to (euro)1,474.5 million in 2003. In 2003, the principal component of net cash used by financing activities was the repayments of other loans, credit facilities, notes payable and short term loans, net of proceeds, which amounted to (euro)3,927.5 million. Net cash used by financing activities doubled approximately in 2003 to (euro)4,178.9 million from (euro)2,101.1 million in 2002.

Anticipated Uses of Funds

Our principal liquidity and capital resource requirements consist of the following:

- capital expenditures for existing and new operations;
- acquisitions of new licenses, or other operators or companies engaged in complementary or related businesses such as Telefonica Moviles'acquisition of BellSouth's wireless operations in Latin America and Telefonica Movil Chile, the acquisition of Cesky Telecom and other potential acquisitions;
- debt service requirements relating to our existing and future debt;
- costs and expenses relating to the operation of our business; and
- dividend and early retirement payments.

We expect to spend approximately 48% of our capital expenditures budget for 2005 on our fixed line telephony and Telefonica Empresas' businesses (including broadband services, which are expected to account for approximately 50% of our fixed line telephony and Telefonica Empresas business expenditures in 2005 compared to approximately 39% in 2004), approximately 40% on our wireless services business and approximately 12% on our other lines of business. Our principal capital expenditures are described in "Item 4--Information on the Company". Our anticipated amounts of capital expenditures and investments in affiliates and the underlying assumptions are subject to risks and uncertainties, and actual capital expenditures and investments in affiliates may be less than or exceed these amounts. See "Cautionary Statement Regarding Forward-Looking Statements".

Anticipated Sources of Liquidity

Cash flows from operations are our primary source of cash funding for existing operations, capital expenditures, debt interest and principal payments. We also rely on external borrowings, including a variety of short- and medium-term financial instruments, principally bonds and debentures, and borrowings from financial institutions. Cash and equivalents are mainly held in euro and euro-denominated instruments. Our gross financial debt was (euro)24,183.2 at December 31, 2004, which includes cash ((euro)855 million) and short and long-term financial investments ((euro)2,724.1), but excludes other payables ((euro)373.55 million) and uncalled capital payments payable ((euro)4.50 million). These items are taken into consideration to calculate our net financial debt, which was (euro)20,982.2 million at December 31, 2004. As described below, approximately 3.5% of our consolidated gross financial debt at December 31, 2004 represented zero-coupon obligations.We believe that, in addition to internal generation of funds, our medium-term note program, our euro commercial paper program, our corporate domestic promissory note program and available lines of credit will provide us with substantial flexibility for our future capital requirements as existing debt is retired. As of the date of this Annual Report, our management believes that our working capital is sufficient to meet our present requirements.

The following table describes our consolidated gross financial debt, as stated in euro using the December 31, 2004 exchange rate. We may have exchange rate financial derivatives instruments assigned to the underlying debt instruments. In 2004, the average interest rate on our consolidated gross financial debt was 6.7%. The debt profile below shows the notional amount at the date at which we entered into the related derivatives.

audited amounts (in millions of euros)	Amortization schedule 2005	2006	2007	2008
Non convertible euro and foreign currency debentures, bonds and other marketable debt securities...	3,350.95	1,570.63	675.99	1,015.05
Promissory notes and commercial paper.	1,892.65	6.56	6.37	11.51
Corporate promissory notes...........	4.70	--	--	--
Loans and credits....................	2,629.13	756.49	245.51	134.90
Foreign currency loans...............	1,535.97	474.30	315.13	749.42

126

audited amounts (in millions of euros)	2005	2006	2007	2008	
TOTAL...............................	9,413.40	2,807.98	1,243.00	1,910.88	2,

At December 31, 2004, we had unused committed credit lines in an amount of (euro) 5,271 million, and all of them bear interest at a floating rate based on market indices, principally the Euro Interbank Offered Rate (EURIBOR) and the London Interbank Offered Rate (LIBOR). At the same date, additionally we had (euro)1,942 million available of the (euro)3 billion syndicated revolving credit facility we entered into on July 6, 2004. See "Item 7 - Major Shareholders and Related Party Transactions--Related Party Transactions".

Our borrowing requirements are not significantly affected by seasonal trends.

The table below sets forth the ratings of our short and long term debt as of the date of this Annual Report. A credit rating is not a recommendation to buy, sell or hold securities, may be subject to revision at any time and should be evaluated independently of any other rating.

Rating Agency	Issuer (1)	Long-Term Debt	Short-Term Debt	Outlook	La
Standard & Poor's	Telefonica, S.A.	A	A-1	CreditWatch-Negative	Mar
Moody's	Telefonica, S.A.	A3	P-2	Stable	Dece
Fitch	Telefonica, S.A.	A	F-1	Rating Watch-Negative	Apr

On March 31 and April, 2005, Standard and Poor's and Fitch placed our corporate credit ratings on "CreditWatch" and "Rating Watch", respectively, with negative implications. These placements followed the announcement by the Czech

Republic's privatization commission that our (euro)2.7 billion bid to acquire a 51.1% state in Cesky Telecom a.s. is the preferred bid in the auction process.

Our ability to use external sources of financing will depend in large part on our credit ratings. We believe that we are well-positioned to raise capital in the public debt markets. However, a downgrade of any of the ratings of our debt by any of Moody's, Standard & Poor's and/or Fitch may increase the cost of our future borrowing or may make it more difficult to access the public debt markets. In connection with the credit rating agencies' review of our debt ratings, the rating agencies may give considerable weight to the general macroeconomic and political conditions in Latin America given our high degree of exposure in such region, the performance of our businesses in the Spanish market, our ability to turn around our non-profitable businesses, our financial and dividend policy and our acquisition policy.

Intragroup Loans

We lend funds to our operating subsidiaries, directly or through holding companies that head our different lines of business. These funds are derived from retained cash flows, loans, bonds and other sources (such as asset disposals). Some of the subsidiaries receiving funds are located in Latin American countries.

C. RESEARCH AND DEVELOPMENT

We continue to be firmly committed to technological innovation as a key tool to achieve a sustainable competitive edge, such as preempting market trends and differentiating our products, through the introduction of new technologies, with the development of both new products and business processes with a view to becoming a more effective, efficient and customer oriented Group.

In 2004, Telefonica has established a new model in technological innovation management to align, even more, our technological innovation with the strategy of the Telefonica Group. Also it promotes the collaboration with other agents, who will become "technological partners" (clients, Public Administrations, suppliers, content providers, other enterprises, etc.).

As regards the means of obtaining innovative solutions, Telefonica also considers that achieving the differentiation of its products with respect to its competitors and a better market positioning cannot be based solely

on acquired technology. It is necessary to foster research and development activities to guarantee this differentiation and to drive forward other innovation activities. Our research and development (R&D) policy is aimed at:

- developing new products and services in order to gain market share;
- fostering customer loyalty;
- increasing revenues;
- improving management;
- improving business practices;
- increasing the quality of our infrastructure and services to improve

customer service and reducing costs.

In 2004 the Telefonica Group undertook technological innovation projects focusing on profitable innovation, process efficiency, the creation of new sources of revenues, customer satisfaction, the consolidation of the new markets and technological leadership. The technological innovation activities have been especially integrated in Telefonica's strategy to create value through broadband and IP network communications and services.

Also, projects to promote the Information Society were performed, new services that will use o3G mobile technologies capacities and new wireless handsets were prepared, and work was performed with a view to identifying as soon as possible the emerging technologies that might have a relevant impact on the businesses, testing them with trials relating to new services, applications and platform prototypes.

In 2004 new systems were developed and the existing systems were substantially improved, the detail being as follows:

- Commercial and operating management systems, aimed at providing innovative solutions for business processes, in order to provide intelligence thereto and to increase the profitability and effectiveness of the procurement, customer service, billings and infrastructure management processes.

- Network and service management systems, aimed at strengthening infrastructures and their quality, using innovative solutions.

Most of the R&D activities are undertaken by Telefonica Investigacion y Desarrollo S.A.U. (Telefonica I&D). a wholly-owned investee of Telefonica, which works principally for the Group's lines of business. In performing its functions, it receives the assistance of other companies and universities, Telefonica I&D's mission focuses on improving the Telefonica Group's competitiveness through technological innovation and product development. Telefonica I&D conducts experimental and applied research and product development to increase the range of our services and reduce operating costs. It also provides technical assistance to our Latin American operations. Telefonica I&D's activities include the following:

- the development of new products and fixed telephone services, particularly the development of such value added services as broadband, wireless communications and Internet services for the public, corporate, wireless and multimedia sectors, and the automation of customer services while integrating new opportunities of the GPRS and UMTS systems;

- the development of interactive services, focusing on the development of information services and new infrastructure to provide such services, primarily in the Internet Protocol environment;

- the development of management systems designed to strengthen infrastructure and its quality and to develop innovative solutions for the management of our networks and services;

- the development of business support systems intended to provide innovative solutions for business processes; and

- innovation in business services intended to reinforce technological skills in the areas of networks, software and information technologies.

In 2004 Telefonica I&D opened a new R&D center in Mexico DF (Telefonica I&D Mexico). This subsidiary was created, as Telefonica Pesquisa e Desenvolvimento, located in Sao Paulo, to address the Latin American market.

In 2004, approximately 55% of Telefonica I&D's research and development was for the benefit of Telefonica de Espana, 24% for the benefit of Telefonica Moviles, 11% for Telefonica Latinoamerica, 4% for Telefonica Empresas and 6% for our other subsidiaries, such as Atento, Terra and Telefonica Contenidos.

At December 31, 2004, Telefonica I&D had 1271 employees, who also collaborate with Telefonica R&D qualified professionals from more than 32 companies and 14 universities. In 2004, 1660 projects were undertaken and incorporated into our strategy for value creation via broadband communications and services, and IP networks. New projects were started to develop profitable innovations providing an increase in efficiency to the different telecommunications processes, while maintaining our technological leadership.

Our total research and development expenses were (euro)513 million, (euro)444 million and (euro)461 million in 2002, 2003 and 2004.. These expenses represented 1.8%, 1.6% and 1.5% of our consolidated revenues in each of those years, respectively. These figures have been calculated using the guidelines set out in the OECD Manual. These guidelines include expenses for research and development that, because of timing of projects or accounting classifications, we do not include in their entirety in our consolidated balance sheet.

As a result, the methodology used in calculating our total research expenses for 2004 is not the same as the methodology used for the research and development expenses reported in 2002 and 2003 ((euro)94.4 million and (euro) 73,3 million, respectively) in our Annual Report on Form 20-F for those years.

Lastly, it should be noted in connection with technological innovation, and in particular with R&D, that in 2003 the Telefonica Group, through Telefonica I+D, implemented measures aimed more at the medium and long term in order to detect, understand, develop and apply, using strategic studies, technological monitoring and experimental development methods, issues, singular matters, opportunities and particularly technologies that will have an effect on the performance of the Group's various lines of business. This includes participation in projects financed mainly by Spanish Administration or Regional Administrations where Telefonica I&D centers are located (Aragon, Castilla y Leon, Cataluna y Madrid). Also this includes extensive participation in European projects promoted and financed mainly by the EU.

D. TRENDS AND OUTLOOK

Our strategy going forward will enable us to continue enhancing cash returns through growth and transformation. We have a clear strategy to grow cash flows and improve our return on capital. The customer is our strategy's starting point, and the focus of our future development.

Management for revenue growth will focus on managing and developing the broadband market opportunities, while maximizing growth in the wireless sector and accomplishing continuous growth in the Latin American fixed-line market.

- In broadband we will continue to develop the opportunities offered by the market, innovating to make broadband truly "mass-market".

- In the wireless sector, we stand to capture further growth, both in Spain and in Latin America, given the important potential for market growth.

In Spain:

- In the short-term, our aim will be to further grow our voice business (increased penetration, tariff and service innovation, prepaid-to-contract migrations and loyalty schemes)

- In the medium term, the aim will be to further grow data services (offer customized data services oriented to all customers by segment, enhance customer experience with new content and applications, and guarantee access to affordable and enhanced handsets)

- UMTS deployment will simultaneously support voice growth and guarantee the future contribution of data services.

In Latin America:

- Our main goal is to keep growing our costumer base in Telefonica Moviles' current Latin American markets. Our growth strategy is based on strengthened local branding, leveraged scale in handset policies, improved channel reach and productivity and transferred best practices from Telefonica Moviles Espana across our Latin American operations (channels, branding, loyalty programs).

- Latin American fixed-line business will keep growing organically. The aim will be to retain and grow our customer base while stimulating usage and annual revenue per user while achieving continuous organic revenue growth.

- Retain and grow customer base maximizing penetration by income level, accelerating internet mass penetration, retaining customers through bundling and further segmentation and anticipating and minimizing churn from high-value, high risk customers.

- Stimulating usage and annual revenue per user, with traffic bundling and flat rates, increasing weight of fixed fees, introducing new value added services and developing new businesses (telemergency, handsets, etc.) leveraging customer base.

At the same time, the Telefonica Group is transforming itself in order to grow its cash flow and improve return on capital. This transformation is centered around its customers and focused on two key aspects aiming to reach an integrated telecom group serving all customers' needs in each segment:

- Becoming a commercially oriented company, developing commercial excellence across our business lines in order to stimulate growth. To do this, the aim is to shift the Telefonica Group's operations towards commercial activities.

More efficient business model: We are quickly evolving the Telefonica Group's economic model towards a more agile model. We are optimizing capital expenditures while redirecting our capital expenditures towards broadband and new services and becoming a much less capital intensive business.

This section contains forward-looking statements that are based upon certain assumptions. Such forward-looking statements are not guarantees of future performance and involve numerous risks and uncertainties, and actual results may differ materially from those anticipated. For a discussion of the important factors that could cause such differences please see "Item 3--Key risk factors", "Item 4--Information on the Company", "Item 5--Operating and Financial Review and prospects" and "Item 11--Quantitative and Qualitative Disclosures about Market Risk".

E. OFF-BALANCE SHEET ARRANGEMENTS

We have commitments that could require us to make material payments in the future. These commitments are not included in our consolidated balance sheet at December 31, 2004. Our principal commitments as of the date of this Annual Report are detailed in the Consolidated Financial Statements as is described below. These commitments are primarily contingent obligations in the form of guarantees for our subsidiaries and put and call rights with respect to some of our joint ventures. These arrangements allow us to provide the necessary credit support for some our subsidiaries to develop their operations and allow us to enter into joint ventures on market terms. As of the date of this Annual Report, we are not aware of any events that would result in the material reduction to us of any of these off-balance sheet arrangements. For a discussion of our off-balance sheet commitments please refer to note 22(b) of our Consolidated Financial Statements.

130

F. TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

The following table describes our contractual obligations and commitments with definitive payment terms which may require significant cash outlays in the future. The amounts payable are as of December 31, 2004.

	Payments Due by Period			
	Total	Less than 1 year	1-3 years	4-5 years
	(millions of euro)			
Contractual Obligations				
Long-Term Debt Obligations(1)................	24,183.24	9,413.40	4,050.98	4,081.1
Operating Lease Obligations(2)...............	1,524.28	279.18	542.71	265.8
Purchase Obligations(3)......................	1,201.50	804.85	273.78	108.0
Other long term obligations(4)...............	6,019.64	864.57	2,242.31	1,095.3
Total..	32,928.66	11,362.00	7,109.78	5,550.3

----

(1) Pursuant to Spanish GAAP, Capital (Finance) Lease Obligations are not calculated separately and are instead included as part of our Debt Obligations.

(2) Our operating lease obligations have in most cases extension options conditioned on the applicable law of each country. Accordingly, we have included only those amounts that represent the initial contract period.

(3) Material Purchase Obligations include network equipment and audiovisual content obligations, and payment obligations under existing licenses.

(4) Other Long Term Obligations include long term debt obligations that require us to make cash payments, excluding financial debt obligations included in the table above.

For details of the composition of, and changes in, our debt, see notes 14, 15 and 16 to our Consolidated Financial Statements.

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. DIRECTORS AND SENIOR MANAGEMENT

We are managed by our Board of Directors, which consists of a minimum of five and a maximum of 20 members. All members of the Board of Directors are elected to five-year terms by our shareholders during a general meeting of shareholders. The Board of Directors, which meets monthly, elects from among its own members the chairman and the vice chairmen. Our Board of Directors is the supervisory and controlling body and determines our strategy and coordination with the other members of the Telefonica Group. Our Board of Directors has expressly delegated all of its authority and power to the Standing Committee except as prohibited by Spanish corporate law or under our Articles of Association. Our Board of Directors is informed at each of its meetings of all resolutions adopted by our Standing Committee and a summary of the minutes of the sessions of our Standing Committee is distributed to all members of our Board of Directors, who then vote whether or not to ratify the aforementioned resolutions. The Standing Committee meets bi weekly and is composed of seven members and the secretary of the Standing Committee. Our Board of Directors has also instituted an audit and control committee, a nominating, compensation and corporate governance committee, a human resources and corporate reputation committee, a regulation committee, a service quality and customer service committee, and an international affairs committee, each of which is composed of between a minimum of three directors and a maximum of five directors, most of whom are directors who do not hold executive functions.

Board of Directors

During 2004, the Board of Directors met 11 times. At April 15, 2005, the Board of Directors had met four times during 2005. At April 15, 2005, the directors of Telefonica, S.A., their respective positions on the Board of Directors and the year they were appointed to such positions were as follows:

Name	Age	First Appointed	Current Term Ends
Cesar Alierta Izuel(1)	60	1997	2007
Isidro Faine Casas(1)(2)	62	1994	2006
Jose Antonio Fernandez Rivero(3)(4)(8)	54	2002	2007
Jesus Maria Cadenato Matia(1)(3)	49	2003	2008
Maximino Carpio Garcia(1)(4)(5)	59	1997	2007
Carlos Colomer Casellas(1)(7)	61	2001	2006
Alfonso Ferrari Herrero(6)(5)(9)	63	2001	2006
Jose Fernando de Almansa Moreno-Barreda(6)	55	2003	2008
Gonzalo Hinojosa Fernandez de Angulo(4)(7)	59	2002	2007
Miguel Horta e Costa	56	1998	2008
Pablo Isla Alvarez de Tejera(5)(9)	41	2002	2007

Luis Lada Diaz(6)(7)	55	2000	2006
Jose Fonollosa Garcia(3)	55	2003	2008
Antonio Massanell Lavilla(2)(4)(7)(9)	50	1995	2006
Enrique Used Aznar(6)(8)(9)	63	2002	2007
Mario Eduardo Vazquez	69	2000	2006
Antonio Viana-Baptista(1)	47	2000	2005
Gregorio Villalabeitia Galarraga(1)(3)(5)(6)(8)	54	2002	2007
Antonio Jesus Alonso Ureba(1)(8)	47	2001	2006
Ramiro Sanchez de Lerin Garcia-Ovies(10)	50	2003	--

----

(1) Member of the Standing Committee of the Board of Directors.

(2) Nominated by Caja de Ahorros y Pensiones de Barcelona.

(3) Nominated by Banco Bilbao Vizcaya Argentaria, S.A.

(4) Member of the Audit and Control Committee of the Board of Directors.

(5) Member of the Nominating, Compensation and Corporate Governance Committee of the Board of Directors.

(6) Member of the International Affairs Committee.

(7) Member of the Service Quality and Customer Service Committee.

(8) Member of the Regulation Committee.

(9) Member of the Human Resources and Corporate Reputation Committee.

(10) Mr. Sanchez de Lerin was appointed vice-secretary of the Board of Directors on October 29, 2003 and is not a director.

A significant majority (14) of our current directors are non-executive directors. In accordance with the regulations of our Board of Directors, minorities of these directors (6) are appointed by our significant shareholders.

Our Board of Directors has expressly delegated all of its authority and power to the Standing Committee except as prohibited by Spanish corporate law or under our Articles of Association. This committee is made up of fewer Directors and meets more frequently than our Board. The members of the Standing Committee are Mr. Cesar Alierta Izuel, Mr. Isidro Faine Casas, Mr. Maximino Carpio Garcia, Mr. Carlos Colomer Casellas, Mr. Jesus Maria Cadenato Matia, Mr. Antonio Viana-Baptista, Gregorio Villalabeitia Galarraga and Mr. Alonso Ureba, who is the secretary of the standing committee.

The Audit and Control Committee functions are regulated by our bylaws and the Board of Directors regulations. The Audit and Control Committee has the primary objective of providing support to our Board of Directors in its supervisory oversight functions, specifically having the following responsibilities:

- To report, through its Chairman, to our General Meeting of Shareholders on matters raised at the General Meeting by the shareholders relating to the functions and matters of competence of the Committee;

- To propose to our Board of Directors, to submit to our General Meeting of Shareholders, the appointment of our Auditors referred to in Article 204 of the Stock Company Act, as well as, when appropriate, the terms of their engagement, scope of professional assignment and revocation or renewal of their appointment;

- To supervise the internal audit services;

- To examine the financial information process and the internal control systems; and

- To maintain the necessary relations with the Auditors to receive information on all matters that may put its independence at risk, and any others related to the process of auditing our accounts, as well as to receive information and maintain the communication with the Auditor as required by law relating to the audit process and with respect to the technical regulations on auditing.

The Audit and Control Committee meets at least once per quarter and as many times as considered necessary. During 2004 the Audit and Control Committee met 11 times and, as of the date of this Annual Report, had met five times in 2005. The members of the Audit and Control Committee are Mr. Antonio Massanell Lavilla (chairman), Mr. Maximino Carpio Garcia, Mr. Jose Antonio Fernandez Rivero and Mr. Gonzalo Hinojosa Fernandez de Angulo.

The Nominating, Compensation and Corporate Governance Committee is responsible for reporting to the Board of Directors of the proposals for the appointment of directors, members of the Standing Committee, and the other committees of our Board of Directors, and top members of our management and our subsidiaries. In addition, the Nominating, Compensation and Corporate Governance Committee is responsible for the compensation packages for our Chairman and our Chief Executive Officer, determining Directors' compensation and reviewing the adequacy of the compensation packages and informing the Board of Directors and top members of management's compensation. The Nominating, Compensation and Corporate Governance Committee is responsible for preparing our Corporate Governance Annual Report. The members of the Nominating, Compensation and Corporate Governance Committee are Mr. Alfonso Ferrari Herrero (chairman), Mr. Maximino Carpio Garcia, Mr. Pablo Isla Alvarez de Tejera and Mr. Gregorio Villalabeitia Galarraga. During 2004 the Nominating, Compensation and Corporate Governance Committee met ten times, and as of the date of this Annual Report, had met three times.

The Human Resources and Corporate Reputation Committee is responsible for reviewing our personnel policy and making proposals to our Board of Directors regarding our personnel policy, and corporate reputation and promoting our values within the Group. The Human Resources and Corporate Regulation Committee met six times during 2004 and as of the date of this Annual Report had met two times. The members of the Human Resources and Corporate Reputation Committee are Mr. Pablo Isla Alvarez de Tejera (chairman), Mr. Alfonso Ferrari Herrero, Mr. Antonio Massanell Lavilla and Mr. Enrique Used Aznar.

The Regulation Committee's main objective is to monitor the main regulatory matters which affect the Telefonica Group. Another responsibility of the Committee is to act as a communication and information channel between our management team and our Board of Directors concerning regulatory matters. The members of the Regulation Committee are Mr. Enrique Used Aznar (chairman), Mr. Gregorio Villalabeitia Galarraga, Mr. Antonio Jesus Alonso Ureba and Mr. Jose Antonio Fernandez Rivero. During 2004, the Regulation Committee met ten times, and as of the date of this Annual Report, had met six times.

The Service Quality and Customer Service Committee is responsible for monitoring and reviewing the standards of quality of the main services provided by the Telefonica Group. The Service Quality and Customer Service Committee acts as an information channel between our senior management team and our Board of Directors. The members of the Service Quality and Customer Service Committee are Mr. Gonzalo Hinojosa Fernandez de Angulo (president), Mr. Carlos Colomer Casellas and Mr. Antonio Massanell Lavilla and Mr. Luis Lada Diaz. During 2004 the Service Quality and Customer Service Committee met four times, and as of the date of this Annual Report, had met once.

The International Affairs Committee is responsible for analyzing the international events and matters that affect the Telefonica Group and reporting these events and possible consequences to our Board of Directors. The

committee pays close attention to events taking place in countries where the Telefonica Group has operations and which may affect our competitive position, corporate image and financial results. The committee also oversees our non-profit foundations in such countries. The members of the International Affairs Committee are Mr. Jose Fernando de Almansa Moreno-Barreda (chairman), Mr. Alfonso Ferrari Herrero, Mr. Enrique Used Aznar, Mr. Gregorio Villalabeitia Galarraga and Mr. Luis Lada Diaz. The International Affairs Committee is responsible for informing the Board of Directors of the international events affecting the Telefonica Group's performance. During 2004, the International Affairs Committee met on six occasions and as of the date of this Annual Report had met once.

Biographies of Directors

Mr. Cesar Alierta Izuel serves as our Executive Chairman and Chairman of our Board of Directors. Mr. Alierta began his career in 1970 as general manager of the Capital Markets division at Banco Urquijo in Madrid until 1985. From June 1996 until his appointment as our Chairman, he was the Chairman of Tabacalera, S.A. which after the merger with the French tobacco company, Seita, became Altadis. Previously, he was the Chairman and founder of Beta Capital, which he combined with his post as Chairman of the Spanish Financial Analysts' Association as from 1991. He has also been a member of the Board of Directors and Standing Committee of the Madrid Stock Exchange. In January 1997, Mr. Alierta was appointed to our Board of Directors, and has also been appointed as director of Telefonica Internacional (TISA), Plus Ultra, Terra and Iberia. During his years as Chairman of Tabacalera, Mr. Alierta was also the Chairman of the Board of Directors of Logista, a subsidiary of the Altadis group. Mr. Alierta is currently a member of the Altadis Board of Directors and Standing Committee. On 26 July 2000, Mr. Alierta was appointed as our Chairman and Chief Executive Officer. Mr. Alierta holds a law degree from the University of Zaragoza and an MBA from Columbia University (New York).

Mr. Isidro Faine Casas serves as our Vice-Chairman of the Board of Directors. Mr. Faine is currently the General Manager of La Caja de Ahorros y Pensiones de Barcelona ("la Caixa"). Mr. Faine has developed his professional career working for several companies in different sectors of the economy, as well as financial institutions, for over 20 years. Mr. Faine holds a doctorate degree in Economics, a Diploma in Alta Direccion from IESE and a ISMP in Business Administration from Harvard University. He is a financial analyst and an academic at the "Real Academia de Ciencias Economicas y Financieras".

Mr. Jose Antonio Fernandez Rivero serves as Vice-Chairman of our Board of Directors. Mr. Fernandez Rivero is currently also a member of the Board of

Directors of Banco Bilbao Vizcaya Argentaria, S.A. (BBVA), Iberdrola, S.A., and Chairman of Adquira, S.A. Mr. Fernandez began his career in Arthur Andersen (Systems) in Madrid in 1976. In 1977, he joined the International Division of Banco de Vizcaya, S.A., were he served as the Manager of Administration and Control from 1982 to 1985. In 1986, he was appointed Chairman of the Standing Committee of Banque de Gestion Financiere, S.A. (Belgium), a subsidiary of Banco de Vizcaya, S.A. Later in 1988 he worked for Banco Bilbao Vizcaya as Deputy General Manager (Control and Planning Department of Retail Banking), and in 1989 he worked as Regional Manager of such Division. In 1990, he joined Banco Exterior de Espana, S.A. as General Controller. In 1991, he was appointed as General Controller for Corporacion Bancaria de Espana, S.A. (Argentaria). In 1994, he was named General Manager and in 1997, he was appointed General Manager of Organization, Systems, Operations, Human Resources, Purchases and Real Estate for Argentaria. Since 1999 until his early retirement in January 2003 as General Manager, Mr. Fernandez Rivero was responsible for the Systems and Operations Division for the BBVA Group. He holds a degree in economics and a master's degree from The College of Europe, Bruges (Belgium).

Mr. Jesus Maria Cadenato Matia serves as a director. Mr. Cadenato began his career as a professor at the Basque Country University from 1977 to 1984 and joined Banco Bilbao in 1977, where he held several key management positions in the head office and within the retail branch network. He currently represents BBVA on the boards of directors of Iberia Cards and Uno-e Bank. Mr. Cadenato has a bachelor's degree in business administration from the Basque Country University, specializing in business finance, and a master's degree from IESE Business School (Executive Management Business Administration).

Mr. Maximino Carpio Garcia serves as a director. Since 1984, he has been Professor of Applied Economics of the Universidad Autonoma de Madrid. From 1983 to 1984, he was Chief of the Studies Services of the Confederacion Espanola de Organizaciones Empresariales. From 1984 to 1992, he worked as head of the

Department of Economic and Public Finance of the Universidad Autonoma. From 1992 to 1995, he was dean of the Economics and Business Faculty of the Universidad Autonoma. From 1995 to 1998, he served as head of the department of Public Economy of the Universidad Autonoma. He also serves as a member of the Economic and Social Council, a Spanish government advisory entity, and the Advisory Committee of Abengoa. Mr. Carpio is a member of the Board of Directors of Telefonica Moviles, S.A. Mr. Carpio also received his doctorate degree from the Universidad Autonoma de Madrid.

Mr. Carlos Colomer Casellas serves as a director. Mr. Colomer is Chairman of the Colomer Group and a director of Altadis, S.A. Mr. Colomer began his career in 1970 as Marketing Vice-Chairman of Henry Colomer, S.A. In 1980, he was appointed as Chairman and General Manager of Henry Colomer, S.A and Haugron Cientifical, S.A. In 1986, he was also appointed President of Revlon for Europe. In 1989, he became the President of Revlon International and in 1990, he was appointed Executive Vice-President and Chief Operating Officer of Revlon Inc. In 2000, he was appointed Chairman and Chief Executive Officer of the Colomer Group. Currently Mr. Colomer is also the Chief Operating Officer of INDO an import-export company, Director of Cataluna for Banco Santander Central Hispano, Director of Hospital General de Cataluna and member of the Advisory Committee of CVC Capital Partners. Mr. Colomer has an economics degree from the University of Barcelona and a degree in business administration from the IESE (Barcelona).

Mr. Alfonso Ferrari Herrero serves as a director. He also serves as a director of CTC Chile S.A. and Telefonica del Peru. From 1995 to 2000, he was

Executive Chairman of Beta Capital, S.A. and prior to that he served on several Boards of Directors representing the Banco Urquijo where he was a partner from 1985. He has a doctorate in Industrial Engineering from the Industrial Engineers Technical School of the Polytechnic University of Madrid and he holds a master's degree in business administration from Harvard University.

Mr. Jose Fernando de Almansa y Moreno-Barreda is Member of the Board and President of the International Affairs Committee of this Board at Telefonica S.A. He is also Member of the Board at Telefonica Moviles S.A., Telefonica de Argentina S.A., Telefonica del Peru S.A, Telecomunicacoes de Sao Paulo S.A., and BBVA Bancomer Mexico. He holds a degree in law from the University of Deusto (Bilbao, Spain). He joined the Spanish Diplomatic Corps, and served from 1976 to 1992, as Secretary of the Spanish Embassy in Brussels, Cultural Counsellor of the Spanish Representation to Mexico, Chief Director for Eastern European Affairs and Atlantic Affairs Director in the Spanish Foreign Affairs Ministry, Counsellor to the Spanish Permanent Representation to NATO, in Brussels, Minister-Counsellor of the Spanish Embassy in the Soviet Union, General Director of the National Commission for the 5th Centennial of the Discovery of the Americas, and Deputy General Director for Eastern Europe Affairs in the Spanish Foreign Affairs Ministry. From 1993 to 2002, Fernando de Almansa was appointed Chief of the Royal Household by His Majesty King Juan Carlos I, and is currently Personal Adviser to His Majesty the King.

Mr. Gonzalo Hinojosa Fernandez de Angulo serves as a director. Mr. Hinojosa currently serves as Chairman and Chief Executive Officer of Cortefiel, S.A. He began his professional career with Cortefiel in 1976, and has served in various management positions since then. From 1991 through 2002, he served as a director of Banco Central Hispano Americano and a director of Portland Valderribas. He currently serves as a director of Altadis. Mr. Hinojosa has a degree in industrial engineering.

Mr. Miguel Horta e Costa serves as a director. Mr. Costa is Chairman of Portugal Telecom, SGPS, S.A. He is also President of PT Comunicacoes, S.A., PT Multimedia-Servicos de Telecomunicacoes e Multimedia, SGPS, S.A., PT Moveis-Servicos de Telecomunicacoes, SGPS, S.A., TMN-Telecomunicacoes Moveis Nacionais, S.A., PT Ventures, SGPS, S.A., PT Sistemas de Informacao, S.A., PT Compras-Servicos de Consultoria e Negociacao, S.A., PT Corporate-Solucoes Empresariais de Telecomunicacoes e Sistemas, S.A., Portugal Telecom Brasil, S.A. and of the Fundacao Portugal Telecom. In 1987, he was appointed State Secretary of Foreign Commerce. He currently serves as a director of Portugalia Airlines. Mr. Costa holds a graduate degree in economics from the Universidad Tecnica de Lisboa.

Mr. Pablo Isla Alvarez de Tejera serves as a director. Mr. Isla is Chairman of the Board of Directors of Altadis, S.A. and Logista, S.A. Mr. Isla began his career in 1988 as Attorney General with the Spanish Ministry of Transports, Tourism and Communications and in 1991 served as the official delegate in Spain for the United Nations Commission in the Spanish General Direction of Legal Services. From 1992 through 1996, Mr. Isla served

as General Manager of the Legal Services Department of Banco Popular. In 1996, he was appointed General Manager of the National Heritage department of the Treasury Ministry. He served as General Secretary of Banco Popular Espanol from 1998 through 2000. In July 2000, Mr. Isla was appointed Chairman of the Board of Grupo Altadis and Co-Chairman of the company. Mr. Isla also serves as director of Iberia Lineas Aereas de Espana, S.A and Mutua Madrilena. Mr. Isla has a law degree from the University Complutense of Madrid.

Mr. Luis Lada Diaz serves as a director. He is currently a board member and our General Manager for Development, Planning and Regulatory Affairs. In 1989, Mr. Lada was Deputy General Manager for Technology, Planning and International Services when he left the Telefonica Group to join Amper Group, a telecommunications systems and equipment manufacturer, as General Manager for Planning and Control. Mr. Lada returned to the Telefonica Group in 1993 as Controller of the Subsidiaries and Participated Companies. In 1994, he was appointed as Chief Executive Officer of Telefonica Moviles de Espana S.A., and was promoted to Chairman and President of Telefonica Moviles, S.A. in August 2000. He served as President until July 2002, after which he accepted his present position. He also serves on the boards of directors of Telefonica Moviles, S.A., Telefonica Internacional S.A. and Sogecable S.A. He holds a degree in telecommunications engineering and joined the Telefonica Group in 1973 in the Research and Development Department, rising through the ranks to hold various managerial and executive positions and currently is a member of A.P.D. Supervisory Board and a member of the Advisory Board of the UOC University.

Mr. Jose Fonollosa Garcia serves as a director. Mr. Fonollosa currently represents BBVA on the Board of Directors of BBVA BHIF (Chile), Provida (Chile), BBVA Banco Provincial (Venezuela) and Bradesco (Brasil). In his long career at BBVA he has served as C.I.O, C.F.O, head of the Latin American retail banking division among other responsibilities. He holds a graduate degree in economics.

Mr. Antonio Massanell Lavilla serves as a director. Mr. Massanell is Senior Executive Vice President of Caja de Ahorros y Pensiones de Barcelona and a member of the Boards of Directors of Port Aventura, S.A. and Baqueira Beret, S.A. He is also President of Servihabitat, e-laCaixa, S.A. and Internet Global Congress (IGC). As a representative of Caja de Ahorros y Pensiones de Barcelona, he has worked with the Telefonica Group in the deployment of Caja de Ahorros y Pensiones de Barcelona's corporate telecoms network. Mr. Massanell received his degree in economics from the University of Barcelona.

Mr. Enrique Used Aznar serves as a director. Mr. Used is the Chairman of AMPER, S.A. and AmperProgramas and the Deputy Chairman of Medidata (Brazil). Previously, he held the position of Chairman of Telefonica Latinoamerica, S.A., Telefonica Moviles, S.A., Estratel and Telefonica Investigacion y Desarrollo, S.A. He has also served as Deputy Chairman and Chief Executive Officer of Telefonica Publicidad e Informacion and Compania Telecomunicaciones de Chile. He has also served as a member of the Board of Directors of Telefonica de Argentina, ATT Network System International and Ericsson (Spain).

Mr. Mario Eduardo Vazquez serves as a director. Mr. Vazquez is the President of Telefonica de Argentina, Telefonica Moviles Argentina, S.A., Telefonica Comunicaciones Personales, S.A., Atento Argentina, S.A. Adquira Argentina, S.A. and serves as Chairman of the Board of Directors of Rio Compania de Seguros, S.A. He also serves as a director of Banco Rio de la Plata, S.A., Riobank International, Corporacion Metropolitana de Finanzas, S.A., Heller Financial Argentina, S.A., Heller-Sud Servicios Financieros, S.A., Motorcare Argentina, S.A., Acsa Loss Control, S.A. and Central Puerto, S.A, Indra SI S.A.

Mr. Antonio Viana-Baptista serves as a director. Mr. Viana-Baptista has served as Chairman and Chief Executive Officer of Telefonica Moviles S.A., since August 2002. He also serves on the Board of Directors of Telefonica Internacional, S.A., Telefonica de Argentina, S.A, Brasilcel, N.V, Tele Sudeste Celular Participacoes, S.A., Telesp Celular Participacoes, S.A., and Portugal Telecom SGPS, S.A. He was a principal partner of McKinsey & Co. at the McKinsey offices in Madrid and Lisbon from 1985 to 1991 and served as Executive Advisor of the Banco Portugues de Investimento (BPI) from 1991 to 1996. From 1996 through July 2002, Mr. Viana-Baptista was President of Telefonica Internacional and Executive President of Telefonica Latinoamerica. Mr. Viana-Baptista holds a bachelor's degree from the Catholic University of Lisbon, a graduate degree in European Economics from the Portuguese Catholic University and a master's degree in business administration from INSEAD.

Mr. Gregorio Villalabeitia Galarraga serves as a director. Mr. Villalabeitia is currently a member of the Board of Directors of Gas Natural, S.A., Iberia Lineas Aereas de Espana, S.A. and Repsol YPF, S.A. He has been General Manager of Caja de Ahorros Vizcaina and Chief Executive of Banco Cooperativo Espanol. He was appointed Chief Operating Officer of Banco de Credito Local and was Chief Executive Officer of Caja Postal in January 1995. Following the merger of the various entities of Argentaria, he was named Wholesale Banking General Manager in 1998. In October 1999, following the merger of Argentaria and Banco Bilbao Vizcaya (BBV), he was named General Manager of Global Investment Banking of Banco Bilbao Vizcaya Argentaria (BBVA), and after the restructuring in December 2001 he was appointed General Manager of the Real Estate and Industrial Group of the Bank. Mr. Villalabeitia has a degree in law and economics from the University of Deusto.

Mr. Antonio J. Alonso Ureba serves as our General Secretary and Secretary to our Board of Directors and serves as a director. Mr. Alonso Ureba has worked on the technical staff of the Madrid Town Council central administration, in the Public Defender's Office and as director of Legal Services and Secretary to the Board of the Spanish Stock Exchange Commission (Comision Nacional del Mercado de Valores). During his professional career, Mr. Alonso has authored a number of publications and has been a speaker at a number of conferences. Mr. Alonso Ureba holds a law degree from the Complutense University of Madrid and a master's degree in financial management and investment analysis.

Mr. Ramiro Sanchez de Lerin Garcia-Ovies serves as our General Vice Secretary and Vice Secretary to our Board of Directors in October 29, 2003. He began his career in Arthur Andersen, first working for its audit department and later for its tax department. In 1982, he became an "Abogado del Estado" and started working for the Treasury Internal Revenue in Madrid (Delegacion de Hacienda de Madrid). Afterwards he was assigned to the State Secretariat for the European Communities and later to the Foreign Affairs Ministry. He has been General Secretary and Secretary of the Board of Elosua, S.A., Tabacalera, S.A., Altadis, S.A. and Xfera Moviles, S.A. He has also been teaching in ICADE, Instituto de Empresa and Escuela de Hacienda Publica, Executive Officers/Management Team.

Executive Officers/Management Team

At April 15, 2005, the members of our executive management team at an executive level was composed of our chief executive officer and seven general managers and the years of their appointments to their respective positions were as follows:

Name	Position	Appointed	Age
Cesar Alierta Izuel	Chairman of the Board of Directors and Chief Executive Officer	2000	60
Luis Lada Diaz	General Manager of Development, Planning and Regulation, Member of the Board	2000	55
Antonio J. Alonso Ureba	General Secretary and Secretary to the Board. Member of the Board	2001	47

Santiago Fernandez Valbuena	Chief Financial Officer of Telefonica, S.A.	2002	46
Luis Abril Perez	General Manager of Corporate Communication	2002	57
Calixto Rios Perez	General Manager of Auditing and Management Resources	2000	60
Guillermo Fernandez Vidal	General Manager of Commercial Development and Subsidiaries	1998	58
Javier Nadal Arino	General Manager of Institutional Relations and the Telefonica Foundation	2005	55

The chief executive officers of our principal business units are:

Name	Position	Appointed	Age
Julio Linares Lopez	Telefonica de Espana	2000	59
Jose Maria Alvarez-Pallete Lopez	Telefonica Latinoamerica	2002	41
Antonio Viana-Baptista	Telefonica Moviles	2002	47

Biographies of the Executive Officers and Senior Management

Mr. Santiago Fernandez Valbuena serves as General Manager of Finance and Shared Resources since December 2003. He has served as our Chief Financial Officer since July 2002. He joined Telefonica in 1997 as Chief Executive Officer of Fonditel, Telefonica's Pension Assets Manager. Previously, he was Managing Director of Societe Generale Equities and Head of Equities & Research at Beta Capital in Madrid. He holds an M.S. and a PhD degree in Economics and Finance from Northeastern University. Mr. Fernandez Valbuena served as President of the Research Commission at the Spanish Institute of Financial Analysts. He has held senior teaching positions at Manchester Business School and Instituto de Empresa's MBA programs.

Mr. Luis Abril Perez serves as our General Manager for Corporate Communication. Mr. Abril started his professional career as a Microeconomics Professor in the Universidad Comercial de Deusto, where he then went on to head the Finance Department. In 1978, he moved to the Banco de Vizcaya as Treasury Director and then worked as head of the President's Technical Department, under Pedro Toledo. During his work with the BBV Group (1988-1991) he acted as General Director for the Asset Management division. During the 1994-99 period Mr. Abril acted as General Director for Banesto and as General Director for Communications for BSCH (1999-2001). Mr. Abril holds a degree in Economics and a degree in Law from the Universidad Comercial de Deusto (1971), and a graduate degree in Business Administration from the North European Management Institute, Oslo, Norway (1973).

Mr. Calixto Rios Perez serves as our General Manager of Auditing and Management Resources. In 1973, Mr. Rios joined Banco Exterior de Espaffa as the General Manager of Extebank in New York City. Subsequently he was appointed Chief Executive Officer and Chief Operating Officer of Extebandes, in Venezuela. Later, Mr. Rios returned to Madrid as the General Manager of Filiales Bancarias Internacionales of Banco Exterior de Espafla. In 1990, he was appointed Chief Operating Officer responsible for overseeing the construction, management and marketing of the Olympic Village for the Olympic games and a year later was named Chief Financial Officer of Tabacalera, S.A. After the merger of Tabacalera and Seita, he was appointed Advisor to the Chairmen and Head of Strategy and Planning. After joining Telefonica as Corporate General Manager for Institutional Relations, in July 2002 he was appointed General Manager for Internal Auditing and Communications. He holds a degree in Economics from the Complutense University of Madrid.

Mr. Guillermo Fernandez-Vidal serves as our Subsidiaries General Manager since December 2003, and he has served as our Corporate General Manager and Assistant to our Chief Executive Officer. He began his career in 1970 as a systems technician at NCR's Computer Testing Center. From 1972 to 1987, he worked for ENTEL, S.A., where he escalated to General Manager. In 1987, he joined Telefonica as Deputy General Manager for large clients. Subsequently he was appointed Assistant Head of Business Communications, Head of Business Communications and General Manager of Businesses and General Public and Chief Operating Officer of Telefonica Data, S.A. Mr. Fernandez-Vidal holds an industrial engineer degree in Computer Science.

Javier Nadal Arino Javier Nadal Arino serves as our General Manager of Institutional Relations and as the CEO of the Telefonica Foundation since December 2004. He joined the Telefonica Group in 1985. From 2003 to 2004, Mr. Nadal served as the Chairman of Telefonica de Peru and from 1995 to 1997,as the Chairman of Telefonica de Argentina. He served for ten years as General Manager of Communications in the Spanish government while also serving as Telefonica de Espana's representative to the government. From 1989 to 1994, he was the President of Retevision. He holds an engineering degree from the Universidad Politecnica de Madrid.

Biographies of the Chief Executive Officers of our Principal Business Units

Mr. Julio Linares Lopez serves as Chief Executive Officer of Telefonica de Espana. He joined Telefonica in May of 1970 in the research and development center, where he held several positions until he was appointed Head of Telefonica's Technology and Technical Regulations Department. In April 1990, he was appointed General

Manager of Telefonica Investigacion y Desarrollo (Telefonica I&D). In December 1994, he became Deputy General Manager of Marketing and Development of Telefonica Services in the commercial area and subsequently Assistant Managing Director of Business Marketing. In July 1997, he was appointed Chief Operating Officer of Telefonica Multimedia and Chairman of Telefonica Cable and Producciones Multitematicas. From May 1998 to January 2000, he served as General Manager of Strategy and Technology at the Telefonica, S.A. Corporate Centre, and as a director of Telefonica Sistemas, Telefonica Investigacion y Desarrollo and Via Digital. In January 2000, he was appointed Chairman of Telefonica de Espana. Mr. Linares holds a degree as a Telecommunications Engineer.

Mr. Jose Maria Alvarez-Pallete Lopez serves as Chief Executive Officer of Telefonica Latinoamerica. He began his career at Arthur Young Auditors in 1987. In 1988, he joined Benito & Monjardin/Kidder, Peabody & Co., where he held various positions in the research and corporate finance departments. In 1995, he joined Valenciana de Cementos Portland (Cemex) as head of the Investor Relations and Studies department. In 1996, he was promoted to Controller for the company in Spain, and in 1998 to General Manager of Administration and Financial Affairs for Cemex Group's interests in Indonesia, headquartered in Jakarta. Mr. Alvarez-Pallete holds a graduate degree in Economics from the Complutense University of Madrid. He also studied Economics at the Universite Libre de Belgique.

B. COMPENSATION

The total amount of payments made to our directors during 2004 was (euro)10.6 million ((euro)3.7 million as a fixed allowance, including compensation made to our directors for serving as directors of our subsidiaries; (euro)167 thousand for expenses of attending our Board's sub-committees meetings; (euro)6.6 million for salaries and variable compensation to our directors with executive functions; (euro)129 thousand for in kind compensation to our executive directors, including life insurance premiums; and (euro)44.5 thousand for our contributions to directors' pensions schemes).

The following table shows the individual breakdown of the fixed payments paid to directors (in their capacity as directors) in 2004:

Position	2004
	(in euro)
Chairman	127,614
Deputy Chairmen	162,690
Directors(1):	
Executive directors	97,614
Nominee directors	97,614
Independent directors	97,614

----

(1) One of the members of our Board of Directors, who is not resident in Spain, receives an additional annual assignment of (euro)52,639.14, due to the special interest we have in him being part of our Board of Directors due to his experience and dedication in relation to Latin America.

The following table shows the individual breakdown of the fixed payments made to our directors (in their capacity as members of our Standing Committee) during 2004:

Position	2004
	(in euro)
Chairman	65,076
Deputy Chairman	65,076
Directors	65,076

The compensation of our directors consists of a monthly fixed allowance and of certain per diems for attending Board of Directors' sub-committees meetings. Our meeting of shareholders held on April 11, 2003 set the annual maximum gross compensation for any director at (euro)6 million for fixed allowances and for expenses of attending our Board's sub-committee meetings. In addition, directors with executive functions receive additional payments for carrying out their executive functions. Directors do not receive any compensation for expenses for attending our Board of Directors' or Standing Committee meetings.

The following table shows the total amount of compensation paid during 2004 to our executive officers Mr. Cesar Alierta, Mr. Luis Lada, Mr. Mario Eduardo Vazquez, Mr. Antonio Viana-Baptista and Mr. Antonio Jesus Alonso Ureba, each of whom are also members of our Board of Directors.

Items	2004
	(in euro)
Salaries	3,337,527
Variable Compensation	3,220,739
Compensation in kind	129,412
Contribution to pension plans	44,500
Total	6,732,178

Additionally, the following table shows the compensation paid to our executive officers (excluding those who are also members of our Board of Directors) in 2004:

Items	2004
	(in euro)
Salaries	3,859,367
Variable Compensation	2,745,943
Fees and allowances	98,374
Compensation in kind	117,520
Total	6,821,205

Employment contracts for executive officers belonging to the Standing Committee have an indemnity clause, which provides for an indemnity in the event we decide to terminate the employment agreement. The indemnification to be paid in such event is equal to three years of salary plus an additional one-year salary depending on the length of service provided to us. The concept of annual salary includes the last fixed remuneration plus the arithmetic average of the sum of the last two variable annual salaries received in accordance with the employment contract.

We provide pension, retirement or similar benefits to our directors with executive functions and to our executive officers. During 2004 we set aside or accrued approximately (euro)44,500 for our directors with executive functions and (euro)91,327 for our other executive officers. Non-executive directors do not receive any compensation in the form of pension plans or life insurance policies and do not participate in any stock option plan linked to our market share price.

We did not provide any advances or loans to our directors or members of our management team and do not provide our directors or senior management team with any benefits upon termination of their terms of employment.

Incentive Plans

Our TIES Program, which was tied which tied to the market value of our shares, ended on February 15, 2005. At the commencement of the TIES plan, eligible employees were able to subscribe for shares at the discounted price of (euro)5 per share. The number of shares an eligible employee was able to subscribe for in the initial allocation was based on such employee's wage level. As part of the initial allocation, we offered 1,197,880 shares, of which 1,123,072 were subscribed. These shares became freely transferrable when the TIES plan expired on February 15, 2005.

Our subsidiaries, Telefonica Moviles, S.A. and Terra Networks, S.A. have also established their own compensation plans tied to the market price of their shares.

EN-SOP

In order to satisfy certain obligations in connection with our acquisition in 2000 of Endemol Entertainment Holdings, N.V., in April 2001 our Board of Directors approved the establishment of a new stock option plan, which we refer to as the "EN-SOP program", that is open to all permanent employees of Endemol Entertainment N.V. and

its affiliated companies at January 1, 2001 who do not participate in a similar compensation plan. As part of the EN-SOP program, we will deliver to each eligible employee who is employed on January 1 of 2001, 2002, 2003 and 2004 a variable number of options to purchase shares of Telefonica, S.A. based on such employee's level and salary.

The options expire four years from their respective date of grant and may be exercised in equal amounts beginning in the third and fourth years from such date of grant. The total number of options granted each year pursuant to the plan will be determined by dividing (euro)27.5 million by the exercise price, which price shall be equal to the weighted average of the price per ordinary share of Telefonica, S.A. on the automated quotation system of the Spanish stock exchanges during the five trading days prior to the meeting of the Board of Directors which convenes the annual shareholders' meeting.

The EN-SOP program is subject to anti-dilution and other provisions customary for stock option plans of this type and to the condition that the participant not terminates his or her employment voluntarily and unilaterally prior to the exercise date.

On December 22, 2004, our Board of Directors decided that the EN-SOP plan would be covered with Telefonica shares acquired in the open market. In accordance with the conditions of the EN-SOP plan, 2,246,732 options to purchase shares of Telefonica, S.A. were granted to Endemol Group employees in 2004 with an exercise price of (euro)12.24 per share. The total number of participants under the EN-SOP plan as of December 31, 2004 was 947.

C. BOARD PRACTICES

Please see "--Directors and Senior Management" above.

D. EMPLOYEES

Employees and Labor Relations

The table below sets forth the number of employees at the dates indicated for the parent company of the Telefonica Group, each of the consolidated companies of the groups which comprise our different lines of business and other consolidated subsidiaries. Temporary employees represented 13% of our total employees at December 31, 2004, compared to 10.8% in 2003 due to an increase in the number of temporary employees of Atento. On average during 2004 we had approximately 20,755 temporary employees in 2004 compared to 15,950 in 2003.

	Year Ended December 31,		
Line of Business	2002	2003	2004
Telefonica, S.A.	799	767	622
Telefonica de Espana(1)	43,952	38,464	36,425

Telefonica Moviles............................	13,694	13,093	19,797
Telefonica Latinoamerica........................	28,019	25,762	25,905
Telefonica Contenidos...........................	5,574	4,638	5,860
Terra Networks..................................	2,455	2,229	1,584
Atento..	49,432	54,394	74,829
Telefonica Publicidad e Informacion.............	2,752	2,787	2,876
Other...	6,168	6,154	5,656
Total Employees.................................	152,845	148,288	173,554

----

(1) In 2003, Katalyx and Emergia became part of Telefonica Empresas Group, and in 2004, Telefonica Empresas became part of Telefonica de Espana and Telefonica Latinoamerica. As a consequence of this reorganization and in order to have comparable figures for prior years , we have re-classified certain employees to Telefonica de Espana with (1,779 in 2002, 1,878 in 2003, and 2,091 in 2004) and to Telefonica Latinoamerica (2,346 in 2002, 2,621 in 2003 and 2,571 employees in 2004).

Management believes that labor relations are generally good. On July 23, 2003, Telefonica de Espana entered into a collective bargaining agreement that provided for increases in wage levels in accordance with anticipated

increases in the Indices de Precios de Consumo (IPC), the Spanish consumer price index, and an additional productivity bonus per employee. In accordance with this agreement in 2004 wage levels increased 3.2% and employees received an additional productivity bonus of approximately (euro)387.54 per active employee.

On July 13, 2004, Telefonica Data Espana entered into a collective bargaining agreement. Telefonica Moviles Espana published its collective bargaining agreement on September 30, 2004, which provided for increases in wage levels in accordance with anticipated increases in the Spanish consumer price index and established an additional productivity bonus for each employee.

Our retired employees are provided with certain pension benefits. While Telefonica de Espana contributes the required amounts to fund these benefits over time, there remains an unfunded past service liability, which is estimated to be approximately (euro)320.3 million. We have agreed to fund this obligation over a period ending in 2007.

In order to adapt to the new competitive environment, we have, among other things, implemented voluntary pre-retirement and early retirement plans in recent years.

On July 29, 2003, Telefonica de Espana's labor reduction program (Plan Social de Expediente de Regulacion de Empleo) was approved by the Spanish Labor Ministry. The program called for voluntary redundancies of up to a maximum 15,000 employees of the company over the next four years. This plan allows Telefonica de Espana to reduce its workforce while maintaining its competitiveness. The plan is non-discriminatory, voluntary and applies to all of our employees. The aggregate number of employees that have requested to be included in the labor reduction program at December 31, 2004 was 7,906 employees.

In connection with our voluntary retirement programs, we recorded provisions of (euro)1,363.7 million in 2003 and (euro)698.2 million in 2004, which were charged to results of operations in each respective year. The provision for pre-retirements and early retirements recorded at December 31, 2004 covers all the obligations assumed at that date in connection with our voluntary pre-retirement and early retirement plans.

On June 22, 2004 Terra Networks' labor reduction program was approved by the Spanish Labor Ministry. This program allows Terra Networks to reduce its workforce up to 130 employees by voluntary redundancies and redeployment. The Labor Ministry has also approved Terra Networks Latin America program to reduce its workforce by 29 employees through similar mechanisms.

E. SHARE OWNERSHIP

At April 15, 2005, the following members of our Board of Directors beneficially owned an aggregate of 898,378 shares, representing approximately 0.018% of our capital stock.

Name	No. of Shares Beneficially Owned
Cesar Alierta Izuel..............................	632,012
Isidro Faine Casas...............................	7,164
Jesus Maria Cadenato Matia.......................	9,906
Antonio Jesus Alonso Ureba.......................	8,438
Maximino Carpio Garcia...........................	5,836
Carlos Colomer Casellas..........................	543
Jose Antonio Fernandez Rivero....................	115
Alfonso Ferrari Herrero..........................	101,311
Jose Fernando de Almansa Moreno-Barreda..........	2,112
Gonzalo Hinojosa Fernandez de Angulo.............	37,958
Miguel Horta e Costa.............................	354
Pablo Isla Alvarez de Tejera.....................	386
Luiz Lada Diaz...................................	30,000
Antonio Massanell Lavilla........................	2,748
Enrique Used Aznar...............................	37,438
Mario Eduardo Vazquez............................	10

Name	No. of Shares Beneficially Owned
Antonio Viana-Baptista...........................	21,994
Gregorio Villalabeitia Galarraga.................	53

At April 15, 2005, members of our executive management team (excluding members of our Board of Directors listed above) beneficially owned an aggregate of 272,789 shares, representing approximately 0.0055% of our capital stock.

None of our Directors or executive officers beneficially owned shares representing one percent or more of our share capital at that date.

None of our Directors and executive officers held options in respect of shares representing one percent or more of our share capital at that date.

ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. MAJOR SHAREHOLDERS

General

At April 15, 2005, we had 4,955,891,361 shares outstanding, each having a nominal value of (euro)1 per share. All outstanding shares have the same rights.

At April 15, 2005, according to information publicly available to Telefonica, S.A., beneficial owners of 5% or more of our voting stock were as follows:

Name of Beneficial Owner	Number of Shares	Percent
Banco Bilbao Vizcaya Argentaria, S.A.(1)...........	284,024,849	5.73%
Caja de Ahorros y Pensiones de Barcelona, "La Caixa"(2)..................................	266,476,222	5.38%
Chase Nominees LTD.(3)............................	491,120,327	9.91%
State Street Bank & Trust Co (4).	377,436,725	7.61%

----

(1) According to information provided to us by the BBVA for our 2004 Corporate Governance Report filed with the CNMV on March 30, 2005.

(2) According to information provided to us by la Caixa for our 2004 Corporate Governance Report filed with the CNMV on March 30, 2005.

(3) Held by Chase Nominees LTD. on behalf of beneficial owners. Based on information obtained from a communication made to the CNMV on May 13, 2004.

(4) Held State Street Bank & Trust Co. on behalf of beneficial owners. Based on information obtained from a communication made to the CNMV on February 2, 2005.

We do not keep a shareholder registry and our ownership structure cannot be known precisely. Based on the information available to us there is no individual or corporation that directly or indirectly through one or more intermediaries may exercise any type of control over us. Nevertheless we have certain shareholders whose holdings are considered material.

Preliminary administrative authorization of certain transactions (Golden Share)

On May 13, 2003, the European Court of Justice ("ECJ") ruled (in the case C-463/00, European Communities Commission vs. The Kingdom of Spain), that the preliminary authorization rules (golden share) set forth in Law 5/1995, enacted on March 23, 1995 governing the necessary legal requirements regime for the transfer of the Spanish government holdings' in certain public companies requiring prior governmental approval with respect to a limited number of fundamental corporate and control transactions affecting us, were no longer valid. In order to adapt Law 5/1995 to the ECJ's May 13, 2003 ruling, Law 5/1995 was modified by virtue of the twenty-fifth

additional provision of Law 62/2003, dated December 31, 2003, governing certain tax, administrative and social matters. This regulation establishes a new post-closing notification model, which, for the purposes of the Telefonica Group, is applicable until February 2007.

The post-closing notification requirements described in Law 5/1995 apply to us, Telefonica Moviles S.A., Telefonica de Espana S.A.U., and Telefonica Moviles Espana S.A.U., and must be observed in the following transactions:

- Transfer or encumbrance of strategic assets located in Spain by Telefonica de Espana and Telefonica Moviles Espana. Transactions affecting these assets carried out between Telefonica Group companies are exempt and need only be reported through a written communication to the competent regulatory body;

- Transfer or encumbrance of shares or any other securities of Telefonica de Espana by Telefonica S.A., Telefonica Moviles S.A. by Telefonica S.A. and Telefonica Moviles Espana by Telefonica Moviles S.A., when such transactions results in a change of control, or the sale of holdings representing 50% or more;

- Substitution of Telefonica Moviles Espana SAU.'s business purpose;

- Direct or indirect acquisition of our or Telefonica Moviles S.A.'s shares representing 10% or more of each company's share capital. Financial transactions, which do not result in a change of control or in a change of management, are exempt from the requirements of Law 5/1995.

- Voluntary winding-up, spin-off or merger need only be reported through a simple written communication, except where these operations affect strategic assets specified in Law 5/1995, which will require the post-closing notification. Transactions between members of the Telefonica Group affecting strategic assets are exempt from the post-closing notification.

Ownership Limitations

The new General Telecommunications Law ("GTL") enacted on November 3, 2003, eliminated the existing ownership limitations, which prohibited non-European national from owning directly or indirectly more than 25% of our assets or share capital, except under certain circumstances. Article 6 of the new GTL provides for the application of the reciprocity principle under existing international treaties or agreements, signed and ratified by Spain. The Spanish government, upon request, may authorize exceptions to the reciprocity principle contained in the new GTL.

B. RELATED PARTY TRANSACTIONS

During 2004 and as of the date of this Annual Report in 2005, none of our Directors and no member of our management team has been involved in any related party transactions with us.

Our Articles of Association grant our Board the exclusive power to authorize any transactions with major shareholders or our directors and any proposed transaction affecting a company where one of our Board members is an executive or a shareholder. Previous to authorizing any such transaction our Board will receive an opinion from the Nominating, Compensation and Corporate Governance Committee addressing the fairness of the transaction to our shareholders and us. Any of our Directors that may have an interest in the proposed transaction must abstain from voting on the proposed transaction.

Two of our major shareholders are financial institutions. We have entered into related party transactions with both companies within our ordinary course of business, and always on arm's length terms. During 2004, the executed transactions were usually loans or capital markets transactions provided to us by these financial institutions and agreements for us to provide telecommunications and broadband services to such institutions.

Related Party Transactions with Significant Shareholders

During 2004 and during the first quarter of 2005, the Board of Directors or its Standing Committee have authorized the following transaction with significant shareholders:

Credit Agreement with BBVA and La Caixa as underwriters, joint bookrunners and mandated lead arrangers.

On July 6, 2004, with the favorable opinion from the Nominating, Compensation and Corporate Governance Committee, we entered into a syndicated multicurrency revolving facility amounting to (euro)3 billion with a group of Spanish and international financial institutions. This facility will mature on July 6, 2009, and carries an interest rate equal to Euribor/Libor plus a margin grade dependent on our credit rating. La Caixa and BBVA acted together with four other banks as underwriters, bookrunners and mandated lead arrangers for the facility.

Agreements with Subsidiaries

On February 23, 2005, the Board of Directors of Telefonica and Terra Networks each agreed to merge their respective companies with the termination through dissolution without liquidation of Terra Networks and the transmission of all of its assets to Telefonica, which through universal succession will acquire the rights and obligations of Terra Networks. The exchange ratio, which was determined on the basis of the real value of the corporate assets and liabilities of both companies, will be two ordinary shares of Telefonica for every nine ordinary Terra Networks shares. The Board of Directors of Terra Networks also proposed the distribution to Terra Networks' shareholders a cash dividend of (euro)0.60 per ordinary Terra Netoworks share. The merger is subject to the approval of the shareholders of both Telefonica and Terra Networks at their respective general shareholders meetings.

Intra-Group Loans

We are the parent company of the Telefonica Group and develop our business purpose through our subsidiaries and affiliated companies. We coordinate group policies, including financial policy and, in some cases actual financial management is conducted by us. Most of the operations we perform with other members of the Telefonica Group correspond to financing transactions, which are necessary to cover their needs for funds and which provide interest rate coverage and exchange rate risks.

During 2004, as recorded in our non-consolidated company accounts, we loaned a total of (euro)26,716 million to companies in the Telefonica Group while companies of the Telefonica Group and their associates loaned us a total of (euro)27,249 million. (euro)11,269.7 million was loaned to us by Telefonica Europe, our company devoted to fundraising in the capital markets and (euro)7,332.80 was loaned to us by Telefonica Finanzas, our company in charge of financial support for Telefonica Group companies.

As to the balances with associated companies, the headings "Other credits" long term and "Credits to associated companies" short term on the Consolidated Balance Sheet at December 31, 2004, include an amount of (euro)230.48 and (euro)24.46 million, respectively, in connection with the financing provided to Sogecable, S.A. according to the commitments acquired in the agreements signed in relation to integration of its satellite platforms. Moreover, there is a long term balance of (euro)66.64 million with Medi Telecom and a long term balance of (euro)314.27 million with Ipse 2000.

Likewise, the "Debtor associated companies" and "Debts to associated companies" amounts to (euro)52.07 million and (euro)15.89 million, respectively, for the companies in the Brasilcel group. In relation to Medi Telecom, these sums amounted to (euro)10.55 and (euro)0.44 million in each heading. The Debts to associated companies also includes (euro)11.71 million balance with Amper.

On the other hand, the amount of sales and services rendered that are recorded in the Profit and Loss Account for the financial year ended on December 31, 2004 are for sales to companies in the Group, mainly the management contract with Telefonica de Argentina renegotiated in 2004 and in force until 2008, which regulates the advisory services provided by Telefonica and the price of such services. The revenue received for that item during financial year 2004 amounted to (euro)20.85 million.

C. INTERESTS OF EXPERTS AND COUNSEL

Not applicable.

ITEM 8. FINANCIAL INFORMATION

Consolidated Financial Statements

Please see Item 18.

Legal Proceedings

We and members of the Telefonica Group are party to several lawsuits which are currently in progress in the law courts and the arbitration courts of the different countries in which the Telefonica Group has operations.

Based on the reports of counsel engaged to act in the lawsuits we are party to, it is reasonable to consider that the adverse outcome of any of these, as yet, unresolved lawsuits will not materially affect the Telefonica Group's economic and financial position or solvency. The following lawsuits are those which we consider most significant because of their subject matter or because of the amounts disputed:

A proceeding contesting the resolutions adopted by our special stockholders' meeting held on February 4, 2000.

The stockholder Javier Sotos Garcia, then owner of 300 shares of our shares, filed a complaint contesting the resolutions adopted by the Special Stockholders' Meeting held on February 4, 2000, based, among other reasons, on the purported contravention of the rules regulating the holding of the mentioned meeting and on the purported contravention of the rules for exclusion of preemptive subscription rights in stock capital increases.

On May 8, 2003, the Court of First Instance no. 33 of Madrid handed down a judgment wholly dismissing the complaint filed by the plaintiff stockholder, holding that there were no basis to declare the voidness or voidability of the resolutions adopted by our Special Stockholders' Meeting held on February 4, 2000, and awarding the costs of the proceeding against the plaintiff. On July 26, 2003, an appeal was filed by the latter before the Provincial Court of

Madrid.. On December 11, 2003, we filed a reply brief contesting the appeal. The hearing related to the appeal was held before the Provincial Court of Madrid on January 18, 2005.

On February 9, 2005, Telefonica was notified about the resolution of the Provincial Court of Madrid in which the Court dismissed the appeal. Javier Sotos Garcia announced his decision to file an appeal in the High Court against this resolution. On March 3, 2005, the Provincial Court decide to dismiss this announcement to file appeal in the High Court. Javier Sotos has filed an appeal against the resolution in which the Provincial Court dismissed his announcement to file an appeal in the High Court and Telefonica has filed its answer contesting this appeal.

It should be noted that the complaint filed against the aforementioned resolutions adopted by our stockholders' meeting held on February 4, 2000, did not in any way affect the implementation of those resolutions.

A proceeding contesting certain resolutions adopted by our annual Stockholders' Meeting held on June 15, 2001.

The aforementioned stockholder, Javier Sotos Garcia, also filed a complaint contesting some of the resolutions adopted by our annual Stockholders' Meeting held on June 15, 2001.

The aforementioned complaint is based, among other allegations, on the purported infringement of the contesting stockholder's right to information and on the purported contravention of the legal rules for disapplication of preemptive rights of subscription in capital increases.

On January 23, 2004, we were notified that the proceeding had been stayed until such time as either any of the parties apply for its resumption or the instance lapses.

It should be noted that the complaint filed against the aforementioned resolutions adopted by our stockholders' meeting held on June 15, 2001, did not in any way affect the implementation of those resolutions.

Complaint filed by IDT against us, Terra Networks, S.A. and Lycos, Inc.

International Discount Telecommunications Corporation (IDT) filed a complaint in the U.S. District Court for the District of New Jersey against us, Terra Networks, S.A., Terra Networks U.S.A., Inc., and Lycos, Inc.

This complaint is based on the alleged breach of the joint venture agreement entered into between IDT and Terra Networks, S.A. in October 1999, on the alleged nonperformance of the obligations under the agreement to terminate the joint venture agreement and on the provision prohibiting fraud in connection with the purchase or sale of securities under the U.S. Securities Exchange Act. IDT has also asserted state law claims alleging fraudulent misrepresentation and concealment in addition to its claim under the Securities Exchange Act.

The lawsuit is currently for an unspecified amount, without prejudice to the possibility of the claim being specified and quantified in the course of the proceeding by the plaintiff for damages.

In May 2002, the U.S. District Court decided to dismiss the part of the complaint relating to certain alleged breaches of the joint venture agreement, which also resulted in the exclusion of Terra Networks, U.S.A., Inc. from the proceeding.

Subsequently, IDT added a new claim to the complaint alleging that we were liable, as a control person, for the fraud alleged against Terra Networks in its negotiations with IDT that led to the termination agreement. We filed objections against this claim.

The defendants have filed an answer and, in turn, Terra Networks S.A. has filed a counterclaim.

On July 2, 2003, in light of the evidence presented, Terra Networks, S.A., Lycos, Inc. and us, filed pleadings seeking summary dismissal of the claims . In turn, IDT has requested to have the counterclaim filed by Terra Networks, S.A. dismissed.

On September 1, 2004, the District Court upheld the Magistrate's September 2002 ruling granting IDT permission to assert the Section 20(a) claim against Telefonica in a Third Amended Complaint. Terra Networks and Telefonica then filed answers denying the allegations of the Third Amended Complaint. In its answer, Terra Networks also has reasserted its counterclaims against IDT.

On September 27, 2004, Telefonica filed a motion asking that the Third Amended Complaint be dismissed based on lack of personal jurisdiction. The District Court has not yet ruled on that motion.

On September 30, 2004, the Court issued decisions resolving two of the summary judgment motions filed by the defendants in July 2003. Specifically, the Court granted Lycos's motion and dismissed Lycos from the action. The Court denied Terra Networks' motion for summary judgment, which argued that IDT waived any claim for fraud. The Court did not rule that there was no waiver; rather, it held that it was up to the jury to decide if there has been a waiver.

Plaintiff's Third Amended Complaint does not specify the damages allegedly suffered by IDT, but IDT will attempt to prove its damages at trial through the introduction of expert testimony.

On March 3, 2005 we were notified that the District Court granted our motion to dismiss Telefonica for lack of specific jurisdiction. On March 11, 2005 we were notified that the District Court denied Terra Networks' summary judgment motion and granted IDT's motion to dismiss Terra Networks' counterclaims.

Sistemas e Instalaciones de Telecomunicacion, S.A.U. (Sintel)

As a result of the voluntary bankruptcy proceeding being conducted at Madrid Court of First Instance no. 42, case number 417/2001, which is the continuation of the petition for Chapter 11-type insolvency filed by the director of Sintel on June 8, 2000, two criminal proceedings have commenced which affect us.

Under the bankruptcy order, inter alia, the effects of the bankruptcy were backdated to June 8, 1998. As a result of the backdated effects of the bankruptcy pursuant to the order we receive a payment demand for (euro)22.9 million,

147

which represents the total amount paid for Sintel from January 1999 to April

2000. The relevant parties, consider null and void as a matter of law the participation of Sintel in the contract dated December 30, 1998, in which a debt of (euro)21.4 million was recognized due to the sale of the shares of Sintel by us to Mastec Internacional, S.A. as well as the amounts paid by Sintel, which acted as a joint and several guarantor to the payments owed by Mastec International to us.

We filed an ancillary complaint in which we solicit that the effects of the bankruptcy be backdated to a date closer to that of the bankruptcy order, so that the contract dated December 30, 1998, is not affected. The representatives of the employees filed another complaint to the contrary, proposing that the effects of the bankruptcy be backdated to the date of the sale of the shares of Sintel (April 1996).

The arrangement proposed by the bankrupt company and approved by the court was the subject of an appeal to a superior court.

On June 14, 2004 the Madrid Provincial Appellate Court denied all complaints regarding to the request of the effects of the bankruptcy be backdated to a date closer to December 30, 1998, in consequence, the arrangement proposed by the bankrupt company and the date in which the effects of the bankruptcy will be effective are firm.

Nevertheless this resolution could not be appealed, the ex-employees of Sintel prepared an appeal in the High Court which was denied by a resolution of July 7, 2004. This resolution was appeal in different instances by the ex-employees and was finally resolved by an order of the High Court confirming the dismissal of the appeal notify to the parties on February 4, 2005.

The two criminal proceedings are as follows:

"Abbreviated" proceeding no. 273/2001, in relation to which, on September 24, 2002, we and Telefonica de Espana, S.A. appeared before Central Examining Court no. 1 filing a criminal suit against the directors of Sintel and of Mastec Internacional, S.A., as parties suffering damages. Leave was given for them to appear as parties to the proceeding.

Preliminary proceeding no. 362/2002, which was commenced on October 23, 2002, by Central Examining Court no. 1 for a possible extortion offense. This proceeding arises from the previous one, concerns the possible commission of an extortion offense in the assumption by Sintel of joint and several liability with Mastec for the obligation to pay the related sale price.

This preliminary proceeding has been joined to proceeding no. 273/200. On April 22, 2004, we were notified of a decision denying the filing of proceedings we requested on June 6, 2003 and allowing the judicial proceedings to continue.

On June 29, 2004, we were notified of an enlargement of this criminal suit by an alleged crime of bankruptcy punishable filed by the ex-employees of Sintel. On July 4, 2004 and August 5, 2004, Telefonica requested its rejection. At present the Judge has not resolved about the enlargement of this criminal suit.

Collective lawsuits filed by stockholders of Terra in the U.S., in connection with the tender offer by us for Terra Networks, S.A.

On May 29, 2003, two class actions were filed with the Supreme Court of New York State by stockholders of Terra Networks, S.A. against us, Terra Networks, S.A. and certain former and current directors of Terra Networks, S.A.

These actions are based on the claim that the price offered by us to the stockholders of Terra Networks, S.A. was not in keeping with the intrinsic value of the shares of that company, and seek to have the tender offer revoked or, in the alternative, to have damages awarded to them.

It should be noted that since the filing of the complaints, the related proceedings have remained inactive.

Lawsuit filed by ADICAE.

On June 21, 2003, a consumer association (ADICAE) filed a lawsuit against Terra Networks, S.A., Telefonica, S.A. and against certain of our directors and directors of Terra Networks, S.A. On April 13, 2004, the Central Instruction Court superseded this lawsuit and directed the complainants to provide a (euro)100,000 deposit (bond) as a prerequisite to file an appeal. On April 16, 2004, ADICAE opposed the decision that provided for such deposit and on April 28, 2004, Terra Networks, S.A. filed a counterclaim requesting the confirmation of such decision. On May 20, 2004, the Central Instruction Court rejected the opposition filed by ADICAE. This resolution was appealed by ADICAE and we opposed to the appeal. The court has not yet ruled on the appeal.

Appeal for judicial review no. 6461/03 filed at the National Appellate Court by the World Association of Stockholders of Terra Networks, S.A. (ACCTER) against the administrative decision made by the Spanish National Securities Market Commission to authorize the tender offer by us for Terra Networks, S.A. shares.

ACCTER filed an appeal for judicial review against the decision of the Spanish National Securities Market Commission to authorize the tender offer made to Terra Networks stockholders on June 19, 2003.

We have filed an application, admitted for consideration, to appear in the proceeding as an intervening nonparty to defend the lawfulness of the decision by the Spanish National Securities Market Commission.

In turn, the National Appellate Court has rejected the appellant's request for an ex parte or inter parties injunctive stay of the aforementioned decision.

A brief was filed on December 19, 2003 by the Government Legal Service. We also replied on February 12, 2004 to the application filed by ACCTER for judicial review.

At present the process is pending to set a date to pass judgement on this claim.

Class action lawsuit filed by a stockholder of Terra Networks in the U.S. in connection with the merger between Telefonica, S.A. Terra Networks, S.A.

On February 22, 2005, a class action was filed with the Supreme Court of the State of New York County of Westchester by an owner of ADSs of Terra Networks, S.A. against Telefonica, S.A., Terra Networks, S.A. and certain former and current directors of Terra Networks, S.A.

This action is based, among other things, on the claim that the price offered by us to the stockholders of Terra Networks, S.A. did not reflect the intrinsic value of the shares of Terra Networks.

Regulatory Sanctions

In 2001 and 2002, the Telecommunications Market Commission and the Spanish Competition Court initiated sanctioning proceedings against Telefonica de Espana for its actions as dominant operator.

The following resolutions have been imposed by the Telecommunications Market Commission and the Spanish Competition Court, which have been appealed before the competent authorities:

Spanish Competition Court's resolution dated March 8, 2000

On March 8, 2000, the Spanish Competition Court imposed on Telefonica de Espana a fine amounting to (euro)8,414,169.46 for violating Article 6 of the Spanish competition Law 16/89 (Ley 16/89 de Defensa de la Competencia) and of Article 82 of the EC Treaty, finding to have been practices in abuse of dominant position by Telefonica de Espana in the launching of the advertising campaign "Planes Claros".

On September 22, 2003, Telefonica de Espana filed a contentious-administrative appeal before the Spanish Court "Audiencia Nacional" against such resolution. This appeal was partially admitted on the grounds that the Spanish Competition Court's resolution was contrary to the law regarding the proportionality of the sanction imposed, and reduced it to (euro) 901,518.16.

Telefonica de Espana, the State lawyer, and the co-plaintiff, Retevision, filed a final appeal before the Spanish Supreme Court ("Recurso de Casacion") against this judgment. Retevision later withdrew its appeal.

Telecommunications Market Commission's resolution dated July 23, 2002

On July 23, 2002, the Telecommunication Market Commission imposed on a fine amounting to (euro)18 million Telefonica de Espana for infringement of the "Closed User Group" regulation as interpreted by the Telecommunications Market Commission.

On July 31, 2002, Telefonica de Espana filed a contentious-administrative appeal to the Spanish Court "Audiencia Nacional" against this sanction.

On July 8, 2004, the Appeals Court notified Telefonica de Espana that it had dismissed its appeal. On October 18, 2004 Telefonica de Espana filed a final appeal (Recurso de Casacion) against the Court's decision before the Spanish Supreme Court.

Telecommunications Market Commission's resolution dated October 24, 2002

On October 24, 2002, the Telecommunication Market Commission imposed a fine amounting to (euro)13.5 million on Telefonica de Espana for breach of its obligations relating to voice capacity and data interconnection.

On February 10, 2003, Telefonica de Espana filed a contentious-administrative appeal to the Spanish Court "Audiencia Nacional" against this sanction. The administrative appeal is pending a court resolution.

Telecommunications Market Commission's resolution dated July 10, 2003

On July 10, 2003 the Telecommunication Market Commission imposed a fine amounting to (euro)8 million on Telefonica de Espana for infringement of Telecommunications Market Commission's resolution relating to the prices applied by Telefonica de Espana to Vic Telehome, S.A.

On September 10, 2003, Telefonica de Espana lodged a contentious-administrative appeal to the Spanish Court "Audiencia Nacional" against this sanction.

Spanish Competition Court's resolution dated April 1, 2004

On April 1, 2004, the Spanish Competition Court imposed a fine amounting to (euro)57 million on Telefonica de Espana for infringement of Article 6 of the Spanish competition Law 16/89 (Ley 16/89 de Defensa de la Competencia) and of Article 82 of the EC Treaty, finding that we had abused our dominant position by making conditional the provision of certain supplementary services to customers to the inexistence of carrier pre-selection and by launching unfair advertising campaigns that misled customers and denigrated competitors.

On April 16, 2004, Telefonica de Espana filed a contentious-administrative appeal to the Spanish Court "Audiencia Nacional" against this sanction.

The Appeals Court has resolved to partially accept the suspension of the decision rendered by the Spanish Competition Court on April 1, 2004, the Appeals Court has specifically resolved to suspend our payment of the fine imposed on us by the Spanish Competition Court, amounting to (euro)57 million until a final judgment is rendered.

Proceedings and Convictions

During the last five years, neither we nor, to the best of our knowledge, any person listed in Item 6 above:

- has been convicted in a criminal proceeding, excluding traffic violations or similar misdemeanors; or

- has been a party to a civil proceeding of a judicial or administrative body of competent jurisdiction and as a result of such proceeding was or is subject to a judgment, decree or final order enjoining future violations of, or prohibiting or mandating activities subject to, United States federal or state laws or finding any violation with respect to such laws.

Dividend Information

At the extraordinary general meeting of shareholders held in June 1998, we announced our previous dividend policy of capital increases charged to freely disposable reserves that would be distributed to our shareholders free of charge. The ratio for each of the share dividends was one new share for every 50 then outstanding. This policy allowed our shareholders to obtain liquidity by trading their shares.

The table below sets forth these capital increases carried out during those years:

Date of Shareholders' Meeting Approving Capital Increase	Number of Shares Issued	Date Capital Increase was Carried Out

June 24, 1998................................	61,492,674	January 1999
June 24, 1998................................	62,722,527	April-May 1999
March 26, 1999...............................	63,976,992	November 1999
April 7, 2000................................	86,814,214	January 2001
April 7, 2000................................	89,203,045	March 2001
June 15, 2001................................	93,438,317	January-February 2002
June 15, 2001................................	95,307,084	March-April 2002
April 12, 2002...............................	97,213,225	January-February 2003
April 12, 2002...............................	99,157,490	March 2003

Following increased cash flow generation, we considered cash dividend payments to be appropriate. Accordingly, at the Annual General Shareholders' Meeting held on April 11, 2003, the shareholders approved the distribution of a dividend of (euro) 0.25 per share payable in cash, marking the end of the alternative dividend policy. The first payment was made effective on July 3, 2003, consisting of (euro)0.13 per share and the second payment of (euro)0.12 per share was made effective on October 15, 2003. In both cases, the dividends were charged against the item "Additional paid-in capital".

At the Annual General Meeting of shareholders held on April 30, 2004, the shareholders approved the distribution of a dividend of (euro)0.20 per share payable in cash and a distribution of a share premium of (euro)0.20 per share payable in cash. The first payment of (euro)0.20 per share payable from 2003 net income was made on May 14, 2004 and the second payment of (euro)0.20 per share from additional paid in capital reserve will be made on November 12, 2004.

For fiscal year 2004, and according to the current shareholder remuneration policy approved by the Board of Directors of the Company at its meeting held on July 23, 2003, Telefonica's Board of Directors has approved the following:

- the distribution of an interim dividend of (euro)0.23 per share payable in cash from 2004 net income. This payment will be made on May 13, 2005;

- to propose to the next annual general meeting of shareholders the distribution of a share premium of (euro) 0.27 per share from additional paid in capital reserves. Subject to shareholder approval, this payment will be made on November 11, 2005;

- to submit to next annual general meeting of shareholders a proposal to distribute Telefonica treasury stock among its shareholders in the proportion on one share (1) for every twenty five shares (25). The distribution, subject to shareholder approval, will be charged against paid in capital reserves.

The table below sets forth the annual cash dividends per share paid by us from net income for each of the periods listed during the past five years.

Fiscal Year ended December 31,	Cash Dividends per Share
	(euro)
2004..	0.23
2003..	0.20
2002..	--

Fiscal Year ended December 31, Cash Dividends per Share

	(euro)
2001.....................................	--
2000....................................	--

Distribution of Antena 3 shares to shareholders

At our annual General Shareholders' Meeting of shareholders held on April 11, 2003, our shareholders approved the distribution of 50,000,400 shares of Antena 3 representing 30% of the outstanding share capital of the company. The number of shares to be distributed to each of our shareholders would be the result of dividing the number of Antena 3 shares to be distributed by the number of our shares who had a right to such distribution. Subsequent to the resolution adopted at the General Shareholders' Meeting of Antena 3, S.A. on August 29, 2003, the nominal value of its shares was modified from one euro to three euro. The distribution represented 30% of the share capital of Antena 3, totaling 16,666,800 shares. The exchange ratio was set at one share of Antena 3 for every 295.60802997576 of our shares and our shareholders who were entitled to a fraction of an Antena 3 share as a result of applying the above described exchange ratio received a cash payment for such fractions. For this purpose, the Antena 3 shares were assigned a value of (euro)25.20. This distribution was subject to us commencing an initial public offering of the Antena 3 shares in the Madrid, Barcelona, Bilbao and Valencia stock exchanges, before November 20, 2003.

Antena 3 prepared a full prospectus relating to the listing of all of its shares on the Madrid, Barcelona, Valencia and Bilbao stock exchanges, and their inclusion in the Spanish Automated Quotation System ("sistema de interconexion bursatil"), according to the requirements laid down in Spanish securities exchange laws. The prospectus was verified and was registered by the Spanish Securities Markets Commission on October 17, 2003 thereby fulfilling the condition precedent for the resolution adopted by our shareholders on our annual general meeting held on April 11, 2003, regarding the extraordinary in-kind distribution to our shareholders of part of the Additional Paid-in Capital Reserve by means of allocation of shares representing 30% of the share capital of Antena 3.

The Antena 3 shares received by Citibank N.A. as ADR depositary were sold in the Spanish market and the proceeds, $0.3227182 per ADR, distributed to ADR holders as of the ADR record date on November 6, 2003.

ITEM 9. THE OFFERING AND LISTING

A. OFFER AND LISTING DETAILS

General

Our ordinary shares, nominal value one euro each, are currently listed on each of the Madrid, Barcelona, Bilbao and Valencia stock exchanges under the symbol "TEF". They are also listed on various foreign exchanges such as the London, Frankfurt, Paris, Buenos Aires and Tokyo stock exchanges and are quoted through the Automated Quotation System of the Spanish stock exchanges and through the SEAQ International System of the London Stock Exchange. Our shares are eligible for deposit in the Euroclear system. Our BDSs are listed on the Sao Paulo Stock Exchange. Our ADSs are listed on the New York Stock Exchange and the Lima Stock Exchange.

The table below sets forth, for the periods indicated, the reported high and low quoted closing prices, as adjusted for all stock splits, for the shares on the Madrid Stock Exchange, which is the principal Spanish market for our shares.

	Per Share	
	High	Low
	(euro)	
Year ended December 29, 2000	32.60	17.50
Year ended December 28, 2001	21.10	10.11
Year ended December 30, 2002	15.75	7.45
Year ended December 30, 2003	11.78	7.82

	Per Share	
	High	Low
	(euro)	
Year ended December 30, 2004	13.96	11.20
Quarter ended March 31, 2003	10.18	7.82
Quarter ended June 30, 2003	10.40	8.70
Quarter ended September 30, 2003	11.11	9.83
Quarter ended December 30, 2003	11.78	10.23
Quarter ended March 31, 2004	13.44	11.98
Quarter ended June 30, 2004	13.06	11.33
Quarter ended September 30, 2004	12.25	11.20
Quarter ended December 30, 2004	13.96	12.59
Quarter ended March 31, 2005	14.56	13.44
Quarter ended June 30, 2005 (through April 14)	13.49	13.25
Month ended December 30, 2004	13.96	13.49
Month ended January 30, 2005	14.03	13.44
Month ended February 28, 2005	14.56	13.90
Month ended March 31, 2005	14.12	13.44
Month ended April 30, 2005 (through April 14)	13.49	13.25

Source: Madrid Stock Exchange Information.

On April 14, 2005, the closing price of our shares on the Automated Quotation System of the Spanish stock exchanges was (euro)13.47 per share, equal to $17.27 at the Noon Buying Rate for cable transfers in euro as certified for customs purposes by the Federal Reserve Bank of New York on that date.

Our ADSs are listed on the New York Stock Exchange under the symbol "TEF" and are quoted through SEAQ International. Citibank, N.A. is the Depositary issuing ADRs evidencing the ADSs pursuant to the Deposit Agreement dated as of November 13, 1996, as amended as of December 3, 1999 and as of June 23, 2000, among Telefonica, the Depositary and the holders from time to time of ADRs. Each ADS represents the right to receive three shares.

The table below sets forth, for the periods indicated, the reported high and low quoted closing prices sales prices, as adjusted for all stock splits, of our ADSs on the New York Stock Exchange:

	Per ADS	
	High	Low
	(dollars)	

Year ended December 29, 2000......................	83.19	41.46
Year ended December 31, 2001......................	54.46	27.35
Year ended December 31, 2002......................	39.43	21.47
Year ended December 31, 2003......................	44.38	26.08
Year ended December 31, 2004......................	56.70	40.59
Quarter ended March 31, 2003......................	31.39	26.08
Quarter ended June 30, 2003.......................	36.61	28.54
Quarter ended September 30, 2003..................	37.26	33.32
Quarter ended December 31, 2003...................	44.38	35.84
Quarter ended March 31, 2004......................	51.67	43.70
Quarter ended June 30, 2004.......................	46.95	40.59
Quarter ended September 30, 2004..................	45.25	41.13
Quarter ended December 31, 2004...................	56.70	46.12
Quarter ended March 31, 2005......................	56.89	51.86
Quarter ended June 30, 2005 (through April 14)......	52.32	51.30
Month ended December 31, 2004.....................	56.70	54.20
Month ended January 30, 2005......................	56.22	52.26
Month ended February 27, 2005.....................	56.63	54.27
Month ended March 31, 2005........................	56.01	51.97
Month ended April 30, 2005 (through April 14).......	52.32	51.30

Source: Bloomberg.

At December 31, 2004, approximately 220,898,472 of our shares were held in the form of ADSs by 1,035 holders of record, including Cede & Co., the nominee of The Depository Trust Company. The number of ADSs outstanding was 87,854,712 at December 31, 2004.

Spanish Securities Market Legislation

The Spanish Securities Act which became effective in 1989, restructured the organization and supervision of the Spanish securities markets. This legislation and the regulations implementing it:

- established an independent regulatory authority, the CNMV, to supervise the securities markets;
- established a framework to regulate trading practices, public offerings, tender offers and insider trading;
- required stock exchange members to be corporate entities;
- required companies listed on a Spanish stock exchange to file annual audited financial statements and to make public quarterly financial information;
- established the legal framework for the Automated Quotation System;
- exempted the sale of securities from transfer and value added taxes;
- deregulated brokerage commissions; and
- provided for transfer of shares by book-entry or by delivery of evidence of title.

Effective in November 1998, Law 24/1988 was amended by Law 37/1998, of

November 16, 1998. The amendment introduced the following changes:

- The concept of the "investment services company" was created. Brokers, dealers and portfolio managing companies are considered to be investment services companies. These companies are entitled to render investment services and complementary activities. Banks are not considered to be investment services companies, although they may render investment services upon becoming members of the Spanish stock exchanges.

- An investment services company must be authorized by the Ministry of Treasury in order to render investment services and complementary activities. Once authorization is obtained, the founders of the investment services company must incorporate the company as a sociedad anonima or a sociedad de responsabilidad limitada, both limited liability corporations and, once incorporated, the company must be registered with the Commercial Registry (Registro Mercantil) and the CNMV. This registration must be published in the State Official Gazette.

- The European principle of "single passport" or "single license" was introduced within the Spanish legal system. Under this principle, an investment services company may render investment services and complementary activities within European Union member countries, either through a branch or directly. Any necessary authorizations and licenses must be obtained from the authorities of the country of domicile (the "home country principle"), but the applicable market conduct rules are those set forth in the legislation of the country in which the investment services company renders its services (the "host country principle").

- Spanish investment services companies wishing to render their services overseas must be authorized to do so. However, in the event that they wish to provide services within the European Union, they need only give prior notice to the CNMV.

- An investment guarantee fund was created to protect investors from the insolvency of any investment services company. This fund has the same purpose as the deposit guarantee fund, which is currently in charge of refunding deposits made in insolvent Spanish financial entities. Spanish investment services companies are obligated to maintain a stake in the investment guarantee fund through participation in the share capital of the managing company of the fund.

On July 8, 2003, in order to increase the transparency of the Spanish financial markets, the Spanish parliament passed the so-called "Transparency Act" ("Ley de Transparencia"), also known as "Ley Aldama". The Act regulates the corporate governance structure of listed companies, setting out new reporting obligations and defining the duties of directors and their legal liabilities. The Transparency Act amends the Securities Market Act of 1988 (24/1988) and the Public Companies Act approved by Legislative Royal Decree 1564/1989.

Securities Trading in Spain

The Spanish securities market for equity securities consists of four stock exchanges located in Madrid, Bilbao, Barcelona and Valencia and the Automated Quotation System, or Mercado Continuo. During 2004, the Automated Quotation

System accounted for the majority of the total trading volume of equity securities on the Spanish stock exchanges.

Automated Quotation System

The Automated Quotation System links the four Spanish stock exchanges, providing those securities listed on it with a uniform continuous market that eliminates certain of the differences among the local exchanges. The principal features of the system are the computerized matching of buy and sell orders at the time of entry of the order. Each order is executed as soon as a matching order is entered, but can be modified or canceled until executed. The activity of the market can be continuously monitored by investors and brokers. The Automated Quotation System is operated and regulated by Sociedad de Bolsas, S.A., a corporation owned by the four companies that manage each of the stock exchanges. All trades on the Automated Quotation System must be placed through a brokerage firm, an official stock broker or a dealer firm that is a member of a Spanish stock exchange. Beginning January 1, 2000, Spanish banks were able to become members of a Spanish stock exchange and are therefore able to place trades on the Automated Quotation System.

In a pre-opening session held from 8:30 a.m. to 9:00 a.m. each trading day, an opening price is established for each security traded on the Automated Quotation System based on a real-time auction in which orders can be entered, modified or cancelled but are not executed. During this pre-opening session, the system continuously displays the price at which orders would be executed if trading were to begin. Market participants only receive information relating to the auction price (if applicable) and trading volume permitted at the current bid and offer price. If an auction price does not exist, the best bid and offer price and associated volumes are shown. The auction terminates with a random period of 30 seconds in which share allocation takes place. Until the allocation process has finished, orders cannot be entered, modified or cancelled. In exceptional circumstances (including the inclusion of new securities on the Automated Quotation System) and after giving notice to the CNMV, Sociedad de Bolsas S.A. may establish an opening price without regard to the reference price (the previous trading day's closing price), alter the price range for permitted orders with respect to the reference price and modify the reference price.

The computerized trading hours are from 9:00 a.m. to 5:30 p.m. During the trading session, the trading price of a security is permitted to vary up to a maximum so-called "static" range of the reference price, provided that the trading price for each trade of such security is not permitted to vary in excess of a maximum so-called "dynamic" range with respect to the trading price of the immediately preceding trade of the same security. If, during the trading session, there exist matching bid and ask orders over a security within the computerized system which exceed any of the above "static" and "dynamic" ranges, trading on the security is automatically suspended and a new auction is held where a new reference price is set, and the "static" and "dynamic" ranges will apply over such reference price.

The "static" and "dynamic" ranges applicable to each particular security are set up and reviewed periodically by Sociedad de Bolsas, S.A.

Between 5:30 p.m. and 8:00 p.m., trades may occur outside the computerized matching system without prior authorization from Sociedad de Bolsas S.A., at a price within the range of 5% above the higher of the average price and closing price for the day and 5% below the lower of the average price and closing price for the day if there are no outstanding bids or offers, respectively, on the system matching or bettering the terms of the proposed off-system transaction and, if, among other things, the trade involves more than (euro)300,000 and more than 20% of the average daily trading volume of the stock during the preceding three months. These trades must also relate to individual orders from the same person or entity and be reported to the Sociedad de Bolsas S.A., before 8:00 p.m. At any time trades may take place (with the prior authorization of the Sociedad de Bolsas S.A.) at any price if:

- o the trade involves more than (euro)1.5 million and more than 40% of the average daily volume of the stock during the preceding three months;

- o the transaction derives from a merger or spin-off process, or from the reorganization of a group of companies;

- o the transaction is executed for the purposes of settling a litigation or completing a complex group of contracts; or

- o Sociedad de Bolsas finds other justifiable cause.

Information with respect to the computerized trades between 9:00 a.m. and 5:30 p.m. is made public immediately, and information with respect to trades outside the computerized matching system is reported to the Sociedad de Bolsas by the end of the trading day and published in the Boletin de Cotizacion and in the computer system by the beginning of the next trading day.

Clearance and Settlement System

A new financial act (Ley 44/2002 de Medidas de Reforma del Sistema Financiero) was enacted on November 22, 2002, to increase the efficiency of the Spanish financial markets. The new law introduced a new article, 44-bis to the Ley del Mercado de Valores (the "Spanish Securities Act") under which Sociedad de Sistemas is created.

The Sociedad the Sistemas de Gestion de los Sistemas de Registro, Compensacion y Liquidacion de Valores S.A., or Sociedad de Sistemas, is regulated by the Spanish Securities Act and where appropriate by Royal Decree 505/1987 of April 3, 1987, Royal Decree 166/1992 of February 14, 1992, and by any other related regulation. This company, which is a wholly owned subsidiary of Bolsas y Mercados Espanoles, Sociedad Holding de Mercados y Sistemas Financieros, S.A. (the "Sociedad Holding"), has the following functions:

- o Bookkeeping of securities represented by means of book entries admitted to trading in the Stock Markets or in the Public Debt Book Entry Market.

- o Managing the clearance and settlement system for the brokerage transactions in the stock markets and at the Public Debt Book Entry Market.

- o Providing technical and operational services directly linked to the registry, clearance and settlement of securities, or any other service required by the Sociedad de Sistemas to be integrated with any other registry, clearance, and settlement systems.

The Sociedad de Sistemas will provide the CNMV, the "Banco de Espana", and the "Ministro de Economia", with the information that these entities may request regarding the registry, clearance, and settlements performed within the systems managed by the Sociedad de Sistemas.

Transactions carried out on the Spanish stock exchanges are cleared and settled through the Sociedad de Sistemas.

Only members of the system are entitled to use it, and membership is restricted to authorized broker members of the Spanish stock exchanges, the Bank of Spain (when an agreement, approved by the Spanish Ministry of Economy and Finance, is reached with the Sociedad de Sistemas) and, with the approval of the CNMV, other brokers not members of the Spanish stock exchanges, banks, savings banks and foreign settlement and clearing systems. The clearance and settlement system and its members are responsible for maintaining records of purchases and sales under the book-entry system. Shares of listed Spanish companies are held in book-entry form. The Sociedad de Sistemas, which manages the clearance and settlement system, maintains a registry reflecting the number of shares held by each of its member entities (each, an entidad adherida) as well as the amount of such shares held on behalf of beneficial owners. Each member entity, in turn, maintains a registry of the owners of such shares. Spanish law considers the legal owner of the shares to be:

- the member entity appearing in the records of the Sociedad de Sistemas as holding the relevant shares in its own name; or the investor appearing in the records of the member entity as holding the shares.

The settlement of any transactions must be made three business days following the date on which the transaction was carried out.

Obtaining legal title to shares of a company listed on a Spanish stock exchange requires the participation of a Spanish official stockbroker, broker-dealer or other entity authorized under Spanish law to record the transfer of shares. To evidence title to shares, at the owner's request the relevant member entity must issue a certificate of ownership. In the event the owner is a member entity, the Sociedad de Sistemas is in charge of the issuance of the certificate with respect to the shares held in the member entity's name.

Brokerage commissions are not regulated. Brokers' fees, to the extent charged, will apply upon transfer of title of shares from the Depositary to a holder of ADRs in exchange for such ADSs, and upon any later sale of such shares by such holder. Transfers of ADSs do not require the participation of an official stockbroker. The Deposit Agreement provides that holders depositing shares with the Depositary in exchange for ADSs or withdrawing shares in exchange for ADSs will pay the fees of the official stockbroker or other person or entity authorized under Spanish law applicable both to such holder and to the Depositary.

B. PLAN OF DISTRIBUTION

Not applicable.

C. MARKETS

Please see "--Offer and Listing Details".

D. SELLING SHAREHOLDERS

Not applicable.

E. DILUTION

Not applicable.

F. EXPENSES OF THE ISSUE

Not applicable.

ITEM 10..ADDITIONAL INFORMATION

A. SHARE CAPITAL

Not applicable.

B. MEMORANDUM AND ARTICLES OF ASSOCIATION

The following summary describes certain material considerations concerning our capital stock and briefly describes certain provisions of our bylaws (estatutos) and Spanish law.

Corporate Objects

Section 4 of Part I of our bylaws sets forth our corporate objects:

- delivery and exploitation of any and all kinds of public and private telecommunication services and, to such end, to design, install, preserve, repair, improve, acquire, dispose of, connect, administer, manage and perform whatever other activities other than those mentioned above with respect to any types of networks, lines, satellites, items of equipment, systems and items of technical infrastructure, both existing or to be created in the future, including the property upon which any and all of the above items are set up;

- delivery and exploitation of any and all types of ancillary or supplementary services, as well as of any services that may stem from communication activities;

- research and development, promotion and application of any and all component principles, items of equipment and systems which are directly or indirectly used in telecommunications;

- manufacturing, production and, generally, any and all forms of industrial activities related to telecommunications; and

- acquisition, disposal and, generally, any and all forms of trade activities related to telecommunications.

Director Qualification

In order to be elected as a director, a person must have held a number of our shares representing a par value of no less than (euro)3,000 for at least three years prior to his or her election. These shares may not be transferred so long as such person remains a director. This requirement does not apply to any person who, at the time of his or her appointment, has either a labor or professional relationship with the company or is expressly exempted from such requirement by a vote of at least 85% of the Board of Directors.

Interested Transactions

When a director has an interest in a transaction, such transaction must be presented to the Nominating, Compensation and Corporate Governance Committee. The Committee delivers an opinion to the Board of Directors about the fairness of the transaction to our shareholders and to us. The interested director may not attend the board meeting at which the related transaction is discussed and noted on.

We do not provide any loans or salary advances to our directors, management or employees.

A director must retire upon reaching the age of 70. Such retirement shall take effect at the first board meeting following the general shareholders' meeting that approves the financial statements for the year in which such director turned 70.

Significant Differences

Corporate Governance Guidelines. In Spain, companies with securities listed on a Spanish Stock Exchange are expected to follow the Olivencia Code of Good Governance and the Aldama Report, which include recommendations for corporate governance guidelines and shareholder disclosure. Additionally, listed companies are now required by law to publish an Annual Report on Corporate Governance and also to publish corporate governance information on their websites. We base our corporate governance procedures on the recommendations of the Olivencia Code and the Aldama Report and also follow the recommendations of the Aldama Report. As part of our corporate governance procedures, we have adopted regulations for our Board of Directors that govern, among other things, director qualification standards, responsibilities, compensation, access to management information, the

Board of Directors purpose and each of our Board Sub-committees purpose and responsibilities. Moreover we have a Regulation of the General Shareholders Meeting that aims to reinforce its transparency providing shareholders with a framework guaranteeing and facilitating exercise of their rights. The Annual Report on corporate governance published by us provides a detailed explanation of our corporate governance procedures and explains the role and duties of our Board of Directors and Board Sub-committees.

Our Annual Report on corporate governance is available at our registered office and on our website at www.telefonica.com. None of the information contained on our website is incorporated in this Annual Report.

Committees. We have an Audit and Control Committee since 1997, composed of two non-executive directors and two directors deemed independent by our Board of Directors. These committees' functions and duties are similar to those required by the NYSE.

U.S. companies listed on the NYSE must also have an audit committee meeting certain specified requirements. Listed foreign private issuers, such as us, must comply with this NYSE rule by July 31, 2005. As of the date of this Annual Report report, our Audit and Control Committee was composed of two non-executive directors and two directors deemed independent by our Board of Directors of Telefonica S.A. This committee's functions and duties are similar to those required by the NYSE.

We have a Nominating, Compensation and Corporate Governance Committee, which is composed of four non-executive directors. The functions, composition and competencies are regulated by the company and are very similar to those required by the NYSE.

Independence of the Board. As of the date of this Annual Report, we had 19 directors, out of which eight have been deemed independent by our Board of Directors. A significant majority of our current directors (14) are non-executive directors. The NYSE rules include detailed criteria for determining director independence. We, in accordance with Spanish recommendations, assess the independence of our directors by evaluating, among other things, (i) the contractual, employment and commercial relations between directors and us, (ii) other Board of Directors positions held by directors, and (iii) the directors familial relationships. The Nominating, Compensation and Corporate Governance Committee evaluates these criteria and notifies the Board of Directors of its decision. Our Board of Directors in turn is responsible for assessing whether a director is deemed independent as reported in our Annual Report on Corporate Governance.

Internal audit function. We have a General Internal Audit Department responsible for internal audit matters and for ensuring the efficiency of the internal audit control process of our different units. This General Internal Audit Department reports directly to the Audit and Control Committee, thus guaranteeing the adequate performance of all its functions.

Non-executive director meetings. Pursuant to the NYSE listing standards, non-executive directors of U.S. listed companies must meet on a regular basis without management present and the company must disclose a method for any interested parties to communicate directly with the non-executive directors. As a group, our non-executive directors do not meet formally without management present. Our Audit and Control Committee, which is composed of two independent and two non-executive directors, has unanimously approved procedures that allow any employee to anonymously and confidentially report instances of fraud, alterations of financial information or specific risks to the company and its subsidiaries. We expect these procedures to be in place within the coming months.

Code of ethics. The NYSE listing standards require U.S. companies to adopt a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers. We have adopted, as required by the Sarbanes Oxley Act, a code of ethics that applies to our principal executive officer, principal financial officer and to our senior financial officers. We also have an Internal Code of Conduct for securities markets issues to prevent insider trading misconducts and to control possible conflicts of interest. In addition, the Regulations of the Board of Directors set out in detail our directors main obligations relating to conflict of interest concerning business opportunities, misappropriation of our assets confidentiality and non-competition.

Description of Telefonica Capital Stock

Description of Share Capital

At April 15, 2005, our issued share capital consisted of 4,955,891,361 ordinary registered shares with a nominal value of (euro)1.00 each. Our shareholders have delegated to the Board of Directors the authority to issue up to 2,274,667,655 new shares. The Board's authorization to issue new shares expires on June 15, 2006.

Meetings and Voting Rights

We hold our ordinary general shareholders' meeting during the first six months of each fiscal year on a date fixed by the Board of Directors. Extraordinary general shareholders' meetings may be called, from time to time, at the discretion of our Board of Directors or upon the request of shareholders representing 5% of our paid-in share capital. We publish notices of all ordinary and extraordinary general shareholders' meetings in the Official Gazette of the Commercial Registry and in at least one newspaper in Madrid at least fifteen days before the relevant meeting.

Each share of Telefonica entitles the holder to one vote. However, only registered holders of shares representing a par value of at least (euro)300, which currently equals at least 300 shares because our shares have a par value of (euro)1 each, are entitled to attend a general shareholders' meeting. Holders of shares representing a par value of less than (euro)300, meaning less than 300 shares, may aggregate their shares by proxy and select a representative that is a shareholder to attend a general shareholders' meeting or delegate his or her voting rights by proxy to a shareholder who has the right to attend the shareholders' meeting. However, under our bylaws, no shareholder may vote a number of shares exceeding 10% of the total outstanding voting capital.

Any share may be voted by proxy. Proxies must be in writing and are valid only for a single meeting.

Only holders of record five days prior to the day on which a general meeting of shareholders is scheduled to be held may attend and vote at the meeting. Under the deposit agreement for the ADSs, our depositary accepts voting instructions from holders of ADSs. The depositary executes such instructions to the extent permitted by law and by the terms governing the shares. The depositary or its nominee, whichever is applicable, will be entitled to vote by proxy the shares represented by the ADSs.

Shareholders representing, in person or by proxy, at least 25% of our subscribed voting capital constitute a quorum for a general meeting. If a quorum is not present at the first meeting, then the meeting can be held on second call. Regardless of the number of shareholders present at the second meeting, they are deemed to constitute a quorum.

Shareholders representing, in person or by proxy, at least 50% of our subscribed voting capital constitute a quorum on a first call for shareholders' meetings at which shareholders will be voting on any of the following actions:

- issuance of bonds;
- increase or reduction of share capital;
- amendment of corporate purpose;
- any other amendment of our bylaws; or
- merger, split or spin-off of Telefonica.

When a quorum is present on the first call, these special resolutions must be adopted by the affirmative vote of shareholders representing a majority of our present subscribed voting capital.

If a quorum for the meeting is not present after the first call, upon a second call for the meeting, 25% of our subscribed voting capital will constitute a quorum. When shareholders representing less than 50% of the subscribed voting capital are in attendance, these special resolutions must be adopted by a vote of two-thirds of those shareholders present.

A shareholder who owns shares on the record date will not be entitled to vote his/her shares in a general meeting of shareholders if the shareholder, individually or as part of a group, has not complied with the notification requirements relating to the acquisition of additional shares beyond certain threshold amounts.

Dividends

Shareholders vote on final dividend distributions at the shareholders' meeting. Distributable profits are equal to:

- net profits for the year; plus
- profits carried forward from previous years; plus
- distributable reserves; minus
- losses carried forward from previous years; minus
- amounts allocated to reserves as required by law or by our bylaws.

The Board of Directors can make interim dividend payments without a prior shareholder vote on the issue. However, under those circumstances, the dividend is limited to distributable net profits of the current year and is subject to certain legal requirements.

Unclaimed dividends revert to Telefonica five years from their date of payment.

Registration and Transfers

Our shares are in registered book-entry form. Transfers executed through stock exchange systems are implemented pursuant to the stock exchange clearing and settlement procedures carried out by the Spanish clearing institution. Transfers executed outside of stock exchange systems, that is, over the counter, are implemented pursuant to the general legal regime for book-entry transfer, including registration by the Spanish clearing institution.

There are no restrictions with respect to the transfer of our shares.

Liquidation Rights

Under Spanish law, upon our liquidation, the shareholders would be entitled to receive, on a pro rata basis, any assets remaining after the payment of our debts and taxes and liquidation expenses.

C. MATERIAL CONTRACTS

Material Contracts

Agreement with Bellsouth

On March 5, 2004 Telefonica Moviles entered into a stock purchase agreement with BellSouth to acquire 100% of BellSouth's interests in its wireless operations in Argentina, Chile, Peru, Venezuela, Colombia, Ecuador, Uruguay, Guatemala, Nicaragua and Panama.

The effective transfer of the shares of these companies was conditional, among other things, upon the attainment of the required regulatory authorizations in each country and on the approvals, if any, required, from the minority stockholders of the various operators. All the holdings of BellSouth in the operators located in Ecuador, Guatemala and Panama were transferred on October 14, 2004. All holdings in the operators located in Colombia, Nicaragua, Peru, Uruguay and Venezuela were transferred on October 28, 2004. All holdings in the operator in

161

Chile were transferred on January 7, 2005, and the holdings in the Argentinian operator were transferred on January 11, 2005.

Under this agreement the aforementioned operators were valued at $5,850 million and their net debt was assumed. The total acquisition cost for Telefonica Moviles, adjusted by the net debt of all the companies, amounted to (euro)3,252.5 million in 2004 (excluding Chile and Argentina, which were acquired in 2005).

In addition to acquiring BellSouth's wireless operators in Latin America, in compliance with the commitments assumed under the share purchase agreement, Telefonica Moviles launched an offer for the acquisition of the minority interests in these companies, the purchase price in each case being equal to the price agreed with BellSouth.

Other Important Agreements

Agreement with Sogecable

In May 2002, Admira entered into an agreement with Sogecable to integrate Via Digital and Canal Satelite Digital, which is the pay television and satellite broadcast platform of Sogecable. The integration was subject to the satisfaction of certain conditions, including the approval of 100% of the shareholders of Via Digital to subscribe a capital increase through a share exchange and the receipt of several administrative authorizations. Under the agreement, Sogecable issued 28,981,121 new shares in exchange for the total issued and outstanding shares of Via Digital at the date of the exchange. To date, we together with Telefonica de Contenidos own 23.83% of the resulting company. See "Item 4--Information on the Company--Business Overview--Worldwide Audiovisual Content and Media--Telefonica de Contenidos (Formerly Admira)".

Also, on August 7, 2003, Telefonica de Contenidos acquired a commitment, up to a maximum of (euro)80 million, to guarantee compliance with the payment obligations arising for Sogecable under the aforementioned syndicated loan and credit facility, or to indemnify the syndicate of banks and savings banks up to the same amount against the damage and loss that the syndicate may suffer if any of Sogecable's obligations in relation to the contract were to be rendered null, void or ineffective for Sogecable.

See "Item 4--Information on the Company--Business Overview--Worldwide Audiovisual Content and Media--Telefonica de Contenidos (Formerly Admira)".

Uno-e Bank

On January 10, 2003, Terra Networks, S.A. and BBVA entered into an agreement for the integration of the consumer finance line of business of Finanzia Banco de Credito, S.A. and Uno-e Bank, S.A., in terms more suited to their respective interests than those established in the memorandum of understanding of May 15, 2002, which was then rendered void. The definitive agreement was subject to the related internal and administrative authorizations, which had to be granted before June 30, 2003, as a condition for the formalization and execution of the integration transaction. After the integration had taken place, Terra Networks, S.A.'s ownership interest in Uno-e Bank, S.A. was 33% and that of the BBVA Group was 67%.

Atento

On October 24, 2003, BBVA, Telefonica, S.A. and Atento N.V. entered into an Agreement establishing the terms and conditions under which BBVA, through General de Participaciones Empresariales, S.L. (GPE) became a stockholder of Atento N.V. by contributing all the shares of Procesos Operativos, S.A. As a result of the performance of this agreement, Telefonica, S.A. currently owns shares representing 91.35% of the capital stock of Atento N.V., and GPE owns the remaining 8.65%.

162

D. EXCHANGE CONTROLS

Exchange Controls and Other Limitations Affecting Security Holders

Preliminary administrative authorization of certain transactions (Golden Share)

On May 13, 2003, the European Court of Justice ("ECJ") ruled (in the case C-463/00, European Communities Commission vs. The Kingdom of Spain), that the preliminary authorization rules (golden share) set forth in Law 5/1995, requiring prior governmental approval with respect to a limited number of fundamental corporate and control transactions affecting us, were no longer valid. In order to adapt Law 5/1995 to the ECJ's May 13, 2003 ruling, Law 5/1995 was modified by virtue of the twenty-fifth additional provision of Law 62/2003, dated December 31, 2003, governing certain tax, administrative and social matters. This regulation establishes a new post-closing notification model, which, for the purposes of the Telefonica Group, is applicable until February 2007.

The post-closing notification requirements described in Law 5/1995 apply to us, Telefonica Moviles S.A., Telefonica de Espana S.A.U., and Telefonica Moviles Espana S.A.U., and must be observed in the following transactions:

- transfer or encumbrance of strategic assets located in Spain by Telefonica de Espana and Telefonica Moviles Espana. Transactions affecting these assets carried out between Telefonica Group companies are exempt and need only be reported through a written communication to the competent regulatory body;

- transfer or encumbrance of shares or any other securities of Telefonica de Espana by Telefonica S.A., Telefonica Moviles S.A. by Telefonica S.A. and Telefonica Moviles Espana by Telefonica Moviles S.A., when such transactions result in a change of control, or the sale of holdings representing 50% or more;

- substitution of Telefonica Moviles Espana S.A.U.'s business purpose;

- direct or indirect acquisition of our or Telefonica Moviles S.A.'s shares representing 10% or more of each company's share capital.

Financial transactions which do not result in a change of control or in a change of management are exempt from the requirements of Law 5/1995; and

- voluntary winding-up, spin-off or merger need only be reported through a simple written communication, except where these operations affect strategic assets specified in Law 5/1995, which will require the post-closing notification. The above-mentioned transaction between members of the Telefonica Group affecting strategic assets are exempt from the post-closing notification.

Ownership Limitations

The new General Telecommunications Law ("GTL") enacted on November 3, 2003 eliminated existing ownership limitations, which prohibited non-European nationals from owning directly or indirectly more than 25% of our assets or share capital, except under certain circumstances. Article 6 of the new GTL provides for the application of the reciprocity principle under existing international treaties or agreements signed and ratified by Spain. The Spanish government, upon request, may authorize exceptions to the reciprocity principle contained in the new GTL.

Trading by Telefonica in its own Shares or Shares of Companies under its Control

At December 31, 2004, we held 207,245,179 shares of treasury stock, representing 4.18% of our capital stock. At March 31, 2005, we held 247,704,407 shares of treasury stock, representing 5% of our capital stock. We have announced our commitment to dedicate a minimum of (euro)4 billion to the acquisition of our treasury stock over the 2003-2006 period.

The Spanish Corporations Law prohibits the purchase by us and our subsidiaries of shares in the secondary market except in the following limited circumstances:

- the purchase of shares must be authorized by a general meeting of shareholders of Telefonica and, in the case of a purchase of shares by a subsidiary, also by a general meeting of shareholders of the subsidiary;

- the shares so purchased have no economic or voting rights while held by Telefonica and have no voting rights while held by its subsidiaries;

- the purchaser must create reserves equal to the purchase price of any shares that are purchased and, if a subsidiary is the acquirer, the reserve must also be recorded by the parent company; and

- the total number of shares held by Telefonica and its subsidiaries may not exceed 5% of the total capital of Telefonica.

Any acquisition of shares of Telefonica exceeding, or that causes Telefonica's and its subsidiaries' holdings to exceed, 1% of Telefonica's share capital must be reported to the CNMV.

At a general meeting of shareholders held in April 2003, Telefonica's shareholders authorized the Board of Directors to acquire shares of Telefonica for a period of 18 months from the date of authorization. The new authorization also applies to companies under our control. Pursuant to the new authorization, the aggregate nominal value of the shares held by us or any of our subsidiaries cannot exceed 5% of our shareholders' equity. Consistent with applicable Spanish laws and regulations and the authorization of our shareholders, from time to time we or our affiliates engage in transactions involving securities of members of the Telefonica Group. These transactions may include purchases of shares of group members, forward contracts with respect to these shares and other similar transactions. At the general meeting of shareholders held in April 2004, this authorization was extended for an additional 18 months from the date of the meeting.

Other Restrictions on Acquisitions of Shares

A person or group of persons that directly or indirectly exercises beneficial ownership or control of 5% or more of the outstanding shares, or which increases or decreases the number of shares which it owns or controls to an amount which equals or exceeds any multiple of 5% of such outstanding shares, must inform the following entities of such ownership:

- Telefonica;
- the Stock Exchange Management Companies of the Spanish stock exchanges on which the shares are listed;
- the CNMV; and
- in the case of a foreign person or group of persons, the General Directorate of Commercial Policy and Foreign Investments.

A person or group that is a member of our Board of Directors must report any acquisition or transfer, regardless of size, of our capital stock. A person or group of persons that fails to inform any of the above entities after reaching any of the indicated thresholds may incur fines and penalties. Additionally, if a company fails to inform us after reaching ownership or control of 10% of the outstanding shares or increases the shares it controls to equal or exceed any successive multiple of 5%, the rights corresponding to those shares will be suspended until a proper notification to us is made. For reporting requirements concerning acquisitions by us or our affiliates of our shares, see "--Trading by Telefonica in its own Shares or Shares of Companies under its Control" above.

Dividend and Liquidation Rights

At the general meeting of shareholders held on April 11, 2003, we announced a new dividend policy aimed at providing cash dividend payments. The meeting approved a (euro) 0.25 dividend payment per share for 2003. The first payment of (euro) 0.13 per share was made effective on July 3, 2003, and the second payment of (euro) 0.12 per share was made effective on October 15, 2003. At the annual general meeting of shareholders held on April 30, 2004, the shareholders approved the distribution of a dividend of (euro)0.20 per share payable in cash and a distribution of (euro)0.20 as

share premium per share payable in cash. The first payment of (euro)0.20 per share payable from 2003 net income was effective on May 14, 2004 and the second payment of (euro)0.20 per share from Additional Paid- in capital reserve will be made on November 12, 2004.

According to Spanish law and our bylaws, dividends may only be paid out of profits or distributable reserves if the value of our net worth is not, and as a result of such distribution would not be, less than its capital stock. Pursuant to Spanish law, we are required to reserve 10% of our fiscal year net income until the amount in its legal reserve reaches 20% of our capital. Our legal reserve is currently at 20%.

Dividends payable by us to non-residents of Spain ordinarily are subject to a Spanish withholding tax. For the tax implications of dividends, see "--Taxation".

Upon our liquidation, our shareholders would be entitled to receive pro rata any assets remaining after the payment of our debts and taxes and expenses of the liquidation. Any change in the rights of shareholders to receive dividends and payment upon liquidation would require an amendment to our bylaws by resolution adopted by a general meeting of shareholders. If there were more than one class of shares, such amendment would also require the approval of each class of shareholders affected by the amendment.

Preemptive Rights and Increases of Share Capital

Pursuant to the Spanish Corporations Law, shareholders and holders of convertible bonds have preemptive rights to subscribe for any new shares and for bonds convertible into shares. Such rights may not be available under special circumstances if precluded by a resolution passed at a general meeting of shareholders in accordance with Article 159 of the Spanish Corporations Law, or the Board of Directors, if authorized. Further, such rights, in any event, will not be available in the event of an increase in capital to meet the requirements of a convertible bond issue or a merger in which shares are issued as consideration. Such rights:

- are transferable;
- may be traded on the Automated Quotation System; and
- may be of value to existing shareholders because new shares may be offered for subscription at prices lower than prevailing market prices.

Shares issuable upon exercise of rights must be registered under the Securities Act of 1933 in order to be offered to holders of ADRs. If we decided not to register the shares, the rights would not be distributed to holders of ADRs. Pursuant to the Deposit Agreement, however, holders of ADRs are entitled to receive their proportionate share of the proceeds, if any, from sale by the Depositary of any rights accruing to holders of ADRs.

E. TAXATION

The following is a general summary of material Spanish and U.S. federal income tax consequences to U.S. Holders (as defined below) of the ownership and disposition of shares or ADSs. This summary is based upon U.S. tax laws, including the U.S. Internal Revenue Code of 1986, as amended (the "Code"), final, temporary and proposed Treasury regulations, rulings, judicial decisions, administrative pronouncements, Spanish tax law, and the Convention Between the United States of America and the Kingdom of Spain for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion With Respect to Taxes on Income, signed February 22, 1990, together with related protocol (the "Treaty"), all as currently in effect and all of which are subject to change or changes in interpretation, possibly with retroactive effect. In addition, the summary is based in part on the representations of the Depositary and assumes that each obligation provided for in or otherwise contemplated by the Deposit

Agreement or any other related agreements will be performed in accordance with its terms.

As used herein, the term "U.S. Holder" means a beneficial owner of one or more shares or ADSs:

(a) who is, for U.S. federal income tax purposes, one of the following:

i. a citizen or resident of the United States,

ii. a corporation (or other entity taxable as a corporation) created or organized in or under the laws of the United States or any political subdivision thereof, or

iii. an estate or trust the income of which is subject to U.S. federal income taxation regardless of its source;

(b) who is entitled to the benefits of the Treaty under the Limitation on Benefits provisions contained in the Treaty;

(c) who holds the shares or ADSs as capital assets for U.S. federal income tax purposes;

(d) who owns, directly, indirectly or by attribution, less than 10% of the share capital or voting stock of Telefonica; and

(e) whose holding is not effectively connected with a permanent establishment in Spain.

This summary does not address tax considerations that may apply to holders that are subject to special tax rules, such as U.S. expatriates, insurance companies, tax-exempt organizations, certain financial institutions, persons subject to the alternative minimum tax, dealers and certain traders in securities or foreign currencies, persons holding the shares or ADSs as part of a straddle, hedging, conversion or other integrated transaction, persons who acquired their shares or ADSs pursuant to the exercise of employee stock options or otherwise as compensation, partnerships or other entities classified as partnerships for U.S. federal income tax purposes or persons whose functional currency is not the U.S. dollar. Such holders may be subject to U.S. federal income tax consequences different from those set forth below.

If a partnership holds shares or ADSs, the tax treatment of a partner generally will depend upon the status of the partner and the activities of the partnership. A partner in a partnership that holds shares or ADSs is urged to consult its own tax advisor regarding the specific tax consequences of owning and disposing of the shares or ADSs.

The U.S. Treasury has expressed concerns that parties to whom ADSs are pre-released may be taking actions that are inconsistent with the claiming of foreign tax credits by U.S. Holders of ADSs. Such actions would also be inconsistent with the claiming of the reduced rate of tax applicable to dividends received by certain non-corporate U.S. Holders. Accordingly, the availability of foreign tax credits to U.S. Holders of ADSs and the reduced tax rate for dividends received by certain non-corporate U.S. Holders, both as described below, could be affected by actions that may be taken by parties to whom ADSs are pre-released. For purposes of the Treaty and U.S. federal income tax, U.S. Holders of American Depositary Receipts will generally be treated as owners of the ADSs evidenced thereby and the shares represented by such ADSs.

This discussion assumes that Telefonica is not, and will not become, a passive foreign investment company ("PFIC"), as discussed below under "United States Federal Income Tax Considerations - Passive Foreign Investment Company Rules."

U.S. Holders of shares or ADSs should consult their own tax advisors concerning the specific Spanish and U.S. federal, state and local tax consequences of the ownership and disposition of shares or ADSs in light of their particular situations as well as any consequences arising under the laws of any other taxing jurisdiction. In particular, U.S. Holders are urged to consult their own tax advisors concerning whether they are eligible for benefits under the Treaty.

Spanish Tax Considerations

Taxation of Dividends

Under Spanish law, dividends paid by a Spanish resident company to a U.S. Holder of shares or ADSs are subject to an income tax withheld at source on the gross amount of dividends, currently at a 15% tax rate.

Taxation of Extraordinary Distributions

On November 12, 2004 we made a special distribution of euro 0.20 per share consisting of a distribution of paid-in surplus. Under Spanish law, this distribution is subject to special tax treatment. In general, the amount of this distribution received in cash is not taxable under Spanish income tax law but instead reduces the acquisition cost of the shares or ADSs for Spanish tax purposes (i.e., in the event of a subsequent sale or disposition of the shares or ADSs, the amount of gain realized will be higher). If the amount of the distribution exceeds the adjusted acquisition cost of a U.S. Holder for the shares or ADSs, that U.S. Holder will be subject to tax on the excess at a rate of 15% and be required to file a Spanish Form 210 along with payment of the tax within one month of the distribution. No amount will be withheld by us in respect of Spanish taxes on this distribution.

Taxation of Capital Gains

Spanish income tax is generally levied at a 35% tax rate on capital gains of non-residents of Spain who are not entitled to the benefit of any applicable treaty for the avoidance of double taxation and who do not operate through a fixed base or a permanent establishment in Spain.

Under the Treaty, capital gains realized by U.S. Holders arising from the disposition of shares or ADSs will not be taxed in Spain provided that the seller has not maintained a direct or indirect holding of 25% or more in our capital during the twelve months preceding the disposition of the shares or ADSs. U.S. Holders will be required to establish that they are entitled to the exemption from tax under the Treaty by providing to the relevant Spanish tax authorities Spanish Form 210 and a certificate of residence on IRS Form 6166 from the IRS stating that to the best knowledge of the IRS, such U.S. Holder is a U.S. resident within the meaning of the Treaty. Spanish law requires that both of these forms be filed within one month from the date the capital gain is realized. Beginning July 5, 2004, U.S. Holders were required to request the IRS Form 6166 certificate of residence by filing IRS Form 8802 with the IRS. The

U.S. Holder must attach to IRS Form 8802 a statement by the U.S. Holder declaring that it was or will be a resident of the United States for the period for which the Treaty benefit is claimed.

Spanish Wealth Tax

Individual U.S. Holders who hold shares or ADSs located in Spain are subject to the Spanish Wealth Tax (Impuesto sobre el Patrimonio) (Spanish Law 19/1991), which imposes tax on property located in Spain on the last day of any year. Shares or ADSs located outside of Spain are not subject to the Spanish Wealth Tax. However, the Spanish tax authorities may argue that all shares of Spanish corporations and all ADSs representing such shares are located in Spain for Spanish tax purposes. If such a view were to prevail, U.S. Holders who held shares or ADSs located in Spain or deemed to be located in Spain on the last day of any year would be subject to the Spanish Wealth Tax for such year at marginal rates varying between 0.2% and 2.5% of the average market value of such shares or ADSs during the last quarter of such year, as published by the Spanish Ministry of Economic Affairs. U.S. Holders should consult their tax advisors with respect to the Spanish Wealth Tax.

Spanish Inheritance and Gift Taxes

Transfers of shares or ADSs on death and by gift to individuals are subject to Spanish inheritance and gift taxes (Impuesto sobre Sucesiones y Donaciones), respectively, if the transferee is a resident of Spain for tax purposes, or if the shares or ADSs are located in Spain at the time of death, regardless of the residence of the heir or beneficiary. The applicable tax rate, after applying all relevant factors, ranges from between 7.65% and 81.6% for individuals. Gifts of shares granted to corporate U.S. Holders are subject to corporate tax which is generally levied at the rate of 35%.

Expenses of Transfer

Transfers of shares or ADSs will be exempt from any transfer tax (Impuesto sobre Transmisiones Patrimoniales) or value added tax. Additionally, no stamp tax will be levied on such transfers.

167

United States Federal Income Tax Considerations

Taxation of Dividends

Distributions received by a U.S. Holder on shares or ADSs, including the amount of any Spanish taxes withheld, other than certain pro rata distributions of shares to all shareholders (including ADS holders), will constitute foreign source dividend income to the extent paid out of Telefonica's current or accumulated earnings and profits (as determined for U.S. federal income tax purposes). The amount of the dividend a U.S. Holder will be required to include in income will equal the U.S. dollar value of the euro, calculated by reference to the exchange rate in effect on the date the payment is received by the Depositary (in the case of ADSs) or by the U.S. Holder (in the case of shares), regardless of whether the payment is converted into U.S. dollars on the date of receipt. If a U.S. Holder realizes gain or loss on a sale or other disposition of euro, it will be U.S. source ordinary income or loss. Corporate U.S. Holders will not be entitled to claim the dividends-received deduction with respect to dividends paid by Telefonica. Subject to applicable limitations and the discussion above regarding concerns expressed by the U.S. Treasury, dividends received by certain non-corporate U.S. Holders in taxable years beginning before

January 1, 2009 will be taxable at a maximum rate of 15%. Non-corporate U.S. Holders should consult their own tax advisors to determine whether they are subject to any special rules that limit their ability to be taxed at this favorable rate.

Spanish taxes withheld from dividends on shares or ADSs at a rate not exceeding the rate provided in the Treaty will be creditable against a U.S. Holder's U.S. federal income tax liability, subject to applicable restrictions and limitations that may vary depending upon the U.S. Holder's circumstances and the discussion above regarding concerns expressed by the U.S. Treasury. Instead of claiming a credit, a U.S. Holder may elect to deduct such Spanish taxes in computing its taxable income, subject to generally applicable limitations. The limitation of foreign taxes eligible for credit is calculated separately with respect to specific classes of income. The rules governing foreign tax credits are complex. Therefore, U.S. Holders should consult their own tax advisors regarding the availability of foreign tax credits in their particular circumstances.

Taxation Upon Sale or Other Disposition of Shares or ADSs

A U.S. Holder will generally recognize capital gain or loss on the sale or other disposition of shares or ADSs, which will be long-term capital gain or loss if the U.S. Holder has held such shares or ADSs for more than one year. The amount of the U.S. Holder's gain or loss will be equal to the difference between such U.S. Holder's tax basis in the shares or ADSs sold or otherwise disposed of and the amount realized on the sale or other disposition. Any gain or loss will generally be U.S. source gain or loss for foreign tax credit purposes.

As discussed under "Spanish Tax Considerations--Taxation of Capital Gains" above, gain realized by a U.S. Holder on the sale or other disposition of shares or ADSs may be subject to Spanish tax unless the U.S. Holder provides the relevant Spanish tax authorities with both a certificate of U.S. tax residence on IRS Form 6166 and Spanish Form 210. Spanish law requires that both of these forms be filed within one month from the date on which the capital gain is realized. U.S. Holders are advised to submit IRS Form 8802 and the accompanying declaration to the IRS well in advance of the date on which the IRS Form 6166 that will be issued by the IRS may be required by the Spanish tax authorities, as there may be delays in obtaining the necessary forms. U.S. Holders should consult their own tax advisors regarding the potential Spanish tax consequences of a sale or other disposition of shares or ADSs and the procedures available for an exemption from such tax.

Passive Foreign Investment Company Rules

Telefonica believes that it was not a PFIC for U.S. federal income tax purposes for its 2004 taxable year. However, since PFIC status depends upon the composition of a company's income and assets and the market value of its assets (including, among others, less than 25% owned equity investments) from time to time, there can be no assurance that Telefonica will not be considered a PFIC for any taxable year. If Telefonica were treated as a PFIC for any taxable year during which a U.S. Holder held a share or ADS, certain adverse tax consequences could apply to the U.S. Holder.

If Telefonica is treated as a PFIC for any taxable year, gain recognized by a U.S. Holder on a sale or other disposition of a share or

ADS would be allocated ratably over the U.S. Holder's holding period for the share or ADS. The amounts allocated to the taxable year of the sale or other disposition and to any year before Telefonica became a PFIC would be taxed as ordinary income. The amount allocated to each other taxable year would be subject to tax at the highest rate in effect for individuals or corporations, as appropriate, and an interest charge would be imposed on the amount allocated to such taxable year. Further, any distribution in respect of shares or ADSs in excess of 125% of the average of the annual distributions on shares or ADSs received by the U.S. Holder during the preceding three years or the U.S. Holder's holding period, whichever is shorter, would be subject to taxation as described above. Certain elections may be available (including a mark-to-market election) to U.S. Holders that may mitigate the adverse tax consequences resulting from PFIC status.

In addition, if Telefonica were to be treated as a PFIC in a taxable year in which it pays a dividend or the prior taxable year, the 15% dividend rate discussed above with respect to dividends paid to certain non-corporate U.S. Holders would not apply.

Information Reporting and Backup Withholding

Payments of dividends and sales proceeds that are made within the United States or through certain U.S.-related financial intermediaries generally are subject to information reporting and to backup withholding unless the U.S. Holder is a corporation or other exempt recipient or, in the case of backup withholding, the U.S. Holder provides a correct taxpayer identification number and certifies that no loss of exemption from backup withholding has occurred. The amount of any backup withholding from a payment to a U.S. Holder will be allowed as a credit against the U.S. Holder's U.S. federal income tax liability and may entitle such U.S. Holder to a refund, provided that the required information is furnished to the IRS.

F. DIVIDENDS AND PAYING AGENTS

Not Applicable.

G. STATEMENTS BY EXPERTS

Not Applicable.

H. DOCUMENTS ON DISPLAY

Where You Can Find More Information

We file Annual Reports on Form 20-F and furnish periodic reports on Form 6-K to the SEC. You may read and copy any of these reports at the SEC's public reference room in Washington, D.C. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. Our SEC filings are also available to the public from commercial document retrieval services. Some SEC filings of ours are also available at the website maintained by the SEC at "http://www.sec.gov".

Our ADSs are listed on the New York Stock Exchange under the symbol "TEF". You may inspect any periodic reports and other information filed with the SEC by us at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

As a foreign private issuer, we are exempt from the rules under the Exchange Act which prescribe the furnishing and content of proxy statements, and our officers, directors and principal shareholders are exempt from the reporting and "short-swing" profit recovery provisions contained in Section 16 of the Exchange Act.

We are subject to the informational requirements of the Spanish securities commission and the Spanish stock exchanges, and we file reports and other information relating to our business, financial condition and other matters with the Spanish securities commission and the Spanish stock exchanges. You may read such reports, statements and other information, including the annual and biannual financial statements, at the public reference facilities maintained in Madrid and Barcelona. Some of our Spanish securities commission filings are also available at the website maintained by the Spanish securities commission at http://www.cnmv.es.

We have appointed Citibank, N.A. to act as depositary for the Telefonica ADSs. Citibank will, as provided in the deposit agreement, arrange for the mailing of summaries in English of such reports and communications to all record holders of the ADSs of Telefonica. Any record holder of Telefonica ADSs may read such reports, notices or summaries thereof, and communications at Citibank's office located at 111 Wall Street, New York, New York 10043.

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to diverse financial market risks due to (i) our business activities, (ii) the debt acquired to finance our business, (iii) our shareholdings in various companies, and (iv) other related financial instruments that we have entered into.

The main market risks that affect the companies in the Telefonica Group are:

- Exchange rate risk. This risk arises mainly due to (i) our international presence and resulting investments in Latin America, and (ii) debt denominated in currencies other than the euro or denominated in the currencies of countries where our businesses are located.

- Interest rate risk. This risk arises mainly due to fluctuations in the interest rates affecting (i) the financial costs associated with variable interest rate debt (or debt with short term maturity and foreseeable renewal), and (ii) the value of our long-term liabilities with fixed interest rates (the market value of this debt rises when interest rates drop).

- Share price risk. This risk arises mainly due to (i) the variation in value of our shareholdings in other companies that are not globally or proportionally consolidated, (ii) derivatives affecting our shareholdings, (iii) our own shares held in our portfolio (treasury shares) and (iv) derivatives affecting our own shares or the shares of companies in which we hold or may hold an interest.

We also face liquidity risk and "country risk". Liquidity risk arises due to the possible imbalances between our capital needs (due to operating and financial expenses, investment, debts that have matured, dividends committed) and our sources of funds (revenue, divestments, financing commitments with financial institutions, operations on capital markets).

"Country risk", which is directly related to market and liquidity risks, consists of the possibility of either, loss of value of the assets or decrease of cash flows generated by such assets and transferred to us. This risk is a direct consequence of political, economic and social instability in the countries in which the Telefonica Group operates, especially Latin America.

The Telefonica Group actively manages the above mentioned risks, in order to:

- stabilize cash flows to facilitate financial planning in order to meet our capital requirements;
- facilitate the understanding and the prediction of our future results by investors;
- protect the value of our equity and the value of the investment made.

In the event any of these objectives conflict with each other, our management evaluates the policy to be followed in each particular situation. In our risk management we use derivative financial instruments, mainly related to exchange rates, interest rates and share prices.

Exchange Rate Risk

Our objective in exchange rate risk management is that, in the event of depreciation of local Latin American currencies, potential losses in the value of the assets related to our business are offset by savings from the reduction in the euro value of our debt denominated in Latin American currencies.

Our exchange rate rate risk management endeavors to ensure that, in the event of depreciation Latin American currencies, the decrease in the euro value of our debt denominated in non-euro currencies covers the decrease in expected cash flows for a two-year period. However, our ability to accomplish this objective is limited due to the the limited availability of appropriate debt instruments denominated in certain currencies, such as the Venezuelan bolivar, or due to high transaction costs associated with entering into debt instruments denominated in Latin currencies compared to the expected depreciation of such currencies. Our estimates show that the depreciation of Latin American currencies versus the euro throughout 2003 and 2004 has resulted in a decrease of (euro)236 million of cash outflow generated by us over the last two years. This esimate is calculated by comparing real figures in euro for our cash flows in 2003 and 2004 with the value in euro that cash flows would have been in 2003 and 2004 if the Latin American exchange rates had remained at year 2002 rates. However, depreciation of Latin American currencies and the U.S. dollar versus the euro in 2003 and 2004 has reduced the cost of our debt resulting in savings of approximately (euro)1.08 billion when translating our debt denominated in local currency to euro. Thus, the accumulated cash flow loss over the last two years has been offset by the debt savings. For the year ended December 31, 2004 we estimate that the depreciation of Latin American currencies and the U.S. dollar versus the euro resulted in a loss of cash flows of (euro)18 million, which was offset by savings of (euro)223 million resulting from the reduction of the cost of our debt denominated in such currencies when measured in euros.

The protection against future depreciation of Latin American currencies in relation to the euro is based on incurring in debt denominated in Latin American currencies. Excluding Mexico (which is a net receiver of cash flow), at December 31, 2004, our debt denominated in Latin American currencies (other than the Mexican peso) amounted to (euro)3.38 billion and was equivalent to 2.1 times the cash flow generated by our Latin American operations (excluding Mexico). However, our debt denominated in Latin American currencies is not uniformly distributed in proportion to the cash flows generated by our Latin American operations in such currencies. Consequently, our future ability to generate savings from our debt denominated in Latin American currencies will depend on where and to what extent depreciation of such currencies versus the euro takes place. For example, at December 31, 2004 we had more assets in Venezuela denominated in the local currency then debt denominated in the local currency. These assets would lose value if the Venezuelan bolivar were to depreciate against the euro and such losses would not be fully offset by savings from the reduction of the cost of our debt denominated in the Venezuelan bolivar measured in euros.

Also, we protect against the loss of value of our Latin American assets due to depreciation versus the euro by incurring U.S. dollar denominated debt. At December 31, 2004 our net debt (gross debt minus short-term financial assets) denominated in U.S. dollars was equivalent to (euro)2.4 billion, excluding certain U.S. dollar denominated instruments entered into to finance the acquisition of BellSouth's Latin American wireless operations.

Another essential element of our exchange rate management policy is to minimize negative financial results due to exchange rate variations while still maintaining open currency positions (under strict risk supervision). Difficulties in minimizing this risk have arisen due to the difficulty in hedging external U.S. dollar denominated debt incurred by our subsidiaries in Argentina through derivative contracts. The external U.S. dollar denominated debt of our Argentine subsidiaries was (euro)652 million at December 31, 2004.

Tabular description of market rate sensitive instruments

At December 31, 2004 we did not maintain any financial instruments for trading purposes, although certain instruments could be classified as held for trading purposes if the relationship between us and the counterparty was not explicitly documented or if both parties considered the instrument to be held for trading. The tables below describe the financial instruments bearing market risk (interest rate risk and foreign exchange risk) for the companies consolidated in the Telefonica Group. Financial instruments reflected in this table comprise debt, temporary financial investments, cash, bank balances and associated derivatives without an optionality feature (mainly interest rate swaps, cross currency swaps and currency forwards). This information has been prepared as follows:

- The debt obligations are divided according to their final characteristics after taking into account the effect of the associated derivative instruments. They are classified according to the currency in which they are denominated, within the following categories:
  - Euro
  - America: U.S. dollar and Latin American currencies
  - Asian currencies
  - African currencies
- The table below also shows the total foreign currency exchange rate exposure for each currency. Each such currency category is further divided into interest rate features:
  - Floating rate interest
  - Fixed rate interest
  - Interest rate bounded with options

In addition, a calendar describing the maturity dates is given for each combination of currency and interest rate feature. Each column shows the notional amount of each debt obligation taking into account associative derivatives maturing in the year indicated at the top of the column through a five-year period. The notional amount outstanding after such five-year period is shown as an aggregate amount in the next column. The column "Total" aggregates all of the notional amounts. Notional amounts do not include accrued interest, except for zero coupon bonds, which include accrued interest from inception to the date of each table. The fair value columns show the value for (i) the underlying debt,(ii) the derivatives linked to the underlying debt, and (iii) the total (the sum of the two previous values).

170

SENSITIVITY TO INTEREST RATES AND EXCHANGE RATES OF DEBT OBLIGATIONS
AT DECEMBER 31, 2004

(in millions of euro, except percentages)

	MATURITY DATES							FA
	2005	2006	2007	2008	2009	Subsequent	TOTAL	Under De
EURO	5,755	2,125	534	774	1,286	4,960	15,434	12,
Floating Rate	(3)	6	(286)	(47)	(2)	137	(195)	2,
Spread-Ref Euribor	(776.70)%	34.24%	(0.05)%	5.36%	(72.67)%	3.12%	(12.95)%	-
Fixed Rate	5,309	2,111	812	814	788	4,599	14,433	8,
Interest Rate	4.58%	3.97%	5.27%	4.16%	4.24%	6.07%	4.96%	-
Bounded Rate	448	8	8	8	500	224	1,195	
AMERICA	200	739	740	1,054	907	1,635	5,275	8,
Instruments in USD	(1,776)	23	316	235	629	1,600	1,026	7,
Floating Rate	(699)	(155)	45	73	--	(5)	(742)	2,
Spread	(0.33)%	(0.66)%	3.81%	1.20%	--	(10.38)%	(0.87)%	-
Fixed Rate	(428)	179	271	152	61	1,387	1,621	5,
Interest Rate	7.34%	9.77%	9.43%	7.24%	5.02%	7.89%	8.33%	-
Instruments in ARS	133	59	54	--	--	--	246	
Floating Rate	66	16	1	--	--	--	82	
Spread	--	2.40%	--	--	--	--	0.47%	-
Fixed Rate	68	43	54	--	--	--	164	
Interest Rate	8.83%	8.64%	9.27%	--	--	10.38%	8.92%	-
Instruments in BRL	493	307	117	544	49	9	1,518	
Floating Rate	15	260	117	544	49	9	993	
Spread	(7.68)%	(0.95)%	(2.06)%	(0.50)%	(5.59)	--	(1.16)%	-
Fixed Rate	478	48	--	--	--	--	525	-
Interest Rate	15.68%	--	--	--	--	--	14.26%	-
Instruments in CLP	241	11	80	173	63	--	567	(
Floating Rate	368	--	--	16	14	--	398	-
Spread	--	--	--	(0.28)%	(0.33)%	--	(0.02)%	-
Fixed Rate	(127)	11	80	157	49	--	169	(
Interest Rate	3.42%	3.30%	4.45%	4.80%	5.07%	--	5.66%	-
Instruments in UFC	390	27	2	83	151	12	666	
Floating Rate	300	25	--	81	--	--	406	
Spread	0.03%	0.33%	--	0.95%	--	--	0.23%	-
Fixed Rate	91	2	2	2	151	12	260	

Interest Rate	6.74%	6.49%	6.49%	6.49%	3.50%	6.17%	4.83%	-
Instruments in PEN	393	119	75	14	10	12	623	
Floating Rate	137	2	--	--	--	--	138	-
Spread	--	--	--	--	--	--	--	-
Fixed Rate	256	117	75	14	10	12	484	
Interest Rate	5.08%	6.06%	6.33%	7.94%	7.00%	5.00%	5.63%	-
Instruments in COP	132	101	30	--	--	--	264	
Fixed Rate	129	5	--	--	--	--	134	
Interest Rate	0.35%	4.00%	--	--	--	--	0.50%	-
Instruments in MXN	192	92	66	5	5	3	364	
Floating Rate	88	3	11	3	3	1	108	-
Spread	(0.37)%	(0.52)%	(0.66)%	(0.52)%	(0.52)%	(0.52)%	(0.41)%	-
Fixed Rate	104	89	55	3	3	1	256	
Interest Rate	8.09%	7.75%	7.93%	8.83%	8.83%	8.83%	7.96%	-
Instruments in GTQ	1	--	--	--	--	--	1	
Fixed Rate	1	--	--	--	--	--	1	
Interest Rate	10.50%	--	--	--	--	--	10.50%	-
ASIA	(1)	--	1	--	--	--	(0)	
Instruments in JPY	(1)	--	1	--	--	--	(0)	
Floating Rate	0	0	1	--	--	--	1	
Spread	3.79%	3.79%	3.79%	3.79%	--	--	3.79%	-

171

	MATURITY DATES							FA
	2005	2006	2007	2008	2009	Subsequent	TOTAL	Under De
Fixed Rate	(2)	--	--	--	--	--	(2)	
Interest Rate	--	--	--	--	--	--	--	
AFRICA	31	--	--	--	--	--	31	-
Instruments in MAD	31	--	--	--	--	--	31	-
Fixed Rate	--	--	--	--	--	--	31	-
Interest Rate	4.23%	--	--	--	--	--	4.23%	-
TOTAL	5,984	2,864	1,274	1,828	2,193	6,595	20,739	20,
Total Floating Rate	400	162	(113)	669	63	142	1,323	5,
Total Fixed Rate	5,786	2,695	1,379	1,141	1,062	6,011	18,074	14,
Total Bounded Rate	(202)	8	8	18	1,068	442	1,342	
EXCHANGE RATE OPTIONS ..	(25)	--	--	--	--	--	(25)	-
OTHER LIABILITIES								
NET DEBT								

The table below is an extract of the previous table that shows the sensitivity to interest rates originated by our position on interest rate swaps.

SENSITIVITY TO INTEREST RATES AT DECEMBER 31, 2004

DETAIL FOR INTEREST RATE SWAPS

(in millions of euro, except percentages)

	MATURITY DATES						
	2005	2006	2007	2008	2009	Subsequent	
EURO	--	--	(0)	(0)	--	--	
Fixed to floating	--	--	--	(0)	--	--	
Receiving leg	(1,085)	(34)	(241)	(640)	3	(135)	(
Average Interest Rate	2.23%	5.77%	5.72%	4.94%	6.37%	6.74%	
Paying leg	1,085	34	241	640	(3)	135	
Average Spread	(0.01)%	(0.51)%	0.05%	(0.71)%	0.11%	(0.04)%	
Floating to fixed	--	--	(0)	--	--	--	
Receiving leg	(1,905)	(1,130)	(615)	(1,199)	(326)	(1,550)	(
Average Spread	0.00%	--	0.08%	(0.18)%	--	--	
Paying leg	1,905	1,130	615	1,199	326	1,550	
Average Interest Rate	0.65%	2.94%	4.81%	4.22%	3.55%	3.90%	
Floating to floating	--	--	(0)	--	--	--	
Receiving leg	(290)	(28)	(57)	--	(300)	(92)	
Average Spread	0.34%	--	0.26%	--	0.63%	0.20%	
Paying leg	290	28	57	--	300	92	
Average Spread	0.29%	0.15%	0.33%	--	0.11%	0.10%	
USD	--	--	--	--	--	--	
Fixed to floating	--	--	--	--	--	--	
Receiving leg	(758)	--	--	--	--	(477)	(
Average Interest Rate	7.31%	--	--	--	--	4.71%	
Paying leg	758	--	--	--	--	477	
Average Spread	0.53%	--	--	--	--	--	
Floating to fixed	--	--	--	--	--	--	
Receiving leg	(132)	(44)	(44)	(49)	(27)	(519)	
Average Spread	0.01%	0.08%	0.08%	0.08%	--		