

TELEFONICA S A
Form 20-F
February 27, 2015

As filed with the Securities and Exchange Commission on February 27, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F

(Mark
One)

- REGISTRATION STATEMENT PURSUANT TO SECTION 12(b)
OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934
OR
- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2014
OR
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____
OR
- SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number: 001-09531

TELEFÓNICA, S.A.
(Exact name of Registrant as specified in its charter)

KINGDOM OF SPAIN
(Jurisdiction of incorporation or organization)

Distrito Telefónica, Ronda de la Comunicación, s/n
28050 Madrid, Spain
(Address of principal executive offices)

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(Name, Telephone, E-Mail and/or Facsimile number and Address of Company Contact Person)

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

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

Guarantees** by Telefónica, S.A. of the \$1,250,000,000 Fixed Rate Notes Due 2015; \$900,000,000 Fixed Rate Guaranteed Senior Notes Due 2015; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; \$700,000,000 Fixed Rate Guaranteed Senior Notes Due 2017; \$500,000,000 Floating Rate Guaranteed Senior Notes Due 2017; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2018; \$1,000,000,000 Fixed Rate Notes Due 2019; \$1,400,000,000 Fixed Rate Guaranteed Senior Notes Due 2020; \$1,500,000,000 Fixed Rate Guaranteed Senior Notes Due 2021; \$750,000,000 Fixed Rate Guaranteed Senior Notes Due 2023; \$2,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2036; each of Telefónica Emisiones, S.A.U.; and of the \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2030 of Telefónica Europe, B.V.

New York Stock Exchange

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

**Not for trading, but only in connection with the listing of the \$1,250,000,000 Fixed Rate Notes Due 2015; \$900,000,000 Fixed Rate Guaranteed Senior Notes Due 2015; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2016; \$700,000,000 Fixed Rate Guaranteed Senior Notes Due 2017; \$500,000,000 Floating Rate Guaranteed Senior Notes Due 2017; \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2018; \$1,000,000,000 Fixed Rate Notes Due 2019; \$1,400,000,000 Fixed Rate Guaranteed Senior Notes Due 2020; \$1,500,000,000 Fixed Rate Guaranteed Senior Notes Due 2021; \$750,000,000 Fixed Rate Guaranteed Senior Notes Due 2023; and \$2,000,000,000 Fixed Rate Guaranteed Senior Notes Due 2036; each of Telefónica Emisiones, S.A.U., and the \$1,250,000,000 Fixed Rate Guaranteed Senior Notes Due 2030 of Telefónica Europe, B.V. (each a wholly-owned subsidiary of Telefónica, S.A.)

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 outstanding shares of each class of capital stock of Telefónica, S.A. at December 31, 2014 was:

Ordinary Shares, nominal value 1.00 euro per share: 4,657,204,330

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes No

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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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Securities Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP International Financial Reporting Standards as Issued by the international Accounting Standards Board Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 Item 18

If this is an annual report indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Securities Exchange Act).

Yes No

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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, as amended (the “Securities Act”), Section 21E of the Securities Exchange Act of 1934 (the “Exchange Act”), 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 “will,” “shall,” “target,” “expect,” “aim,” “hope,” “anticipate,” “should,” “may,” “might,” “assume,” “estimate,” “p” and similar language or other formulations of a similar meaning or, in each case, the negative formulations thereof. Other forward-looking statements can be identified in the context in which the statements are made 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,” “Item 5. Operating and Financial Review and Prospects” and “Item 11. Quantitative and Qualitative Disclosures About Market Risk” 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 telecommunications markets;
- trends affecting our business financial condition, results of operations or cash flows;
- acquisitions, investments or divestments which we may make in the future;
 - our capital expenditures plan;
 - our estimated availability of funds;
 - our ability to repay debt with estimated future cash flows;
 - our shareholder remuneration policies;
- supervision and regulation of the telecommunications sectors where we have significant operations;
 - our strategic partnerships; and
- the potential for growth and competition in current and anticipated areas of our business.

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;
- exposure to currency exchange rates, interest rates or credit risk related to our treasury investments or in some of our financial transactions;
 - existing or worsening conditions in the international financial markets;

- the impact of current, pending or future legislation and regulation in countries where we operate, as well as any failure to renew or obtain the necessary licenses, authorizations and concessions to carry out our operations and the impact of limitations in spectrum capacity;
 - compliance with anti-corruption laws and regulations and economic sanctions programs;
 - customers' perceptions of services offered by us;

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- the actions of existing and potential competitors in each of our markets as well as the potential effects of technological changes;
 - failure of suppliers to provide necessary equipment and services on a timely basis;
 - the impact of unanticipated network interruptions including due to cyber-security actions;
 - the effect of reports suggesting that electromagnetic fields may cause health problems;
- the impact of impairment charges on our goodwill and assets as a result of changes in the regulatory, business or political environment;
- potential liability resulting from our internet access and hosting services arising from illegal or illicit use of the internet, including the inappropriate dissemination or modification of consumer data; and
 - the outcome of pending or future litigation or other legal proceedings.

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 do not undertake any obligation to update any forward-looking statements that 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.

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CERTAIN TERMS AND CONVENTIONS

Our ordinary shares, nominal value 1.00 euro per share, are currently listed on each of the Madrid, Barcelona, Bilbao and Valencia stock exchanges (collectively, the “Spanish Stock Exchanges”) and are quoted through the Automated Quotation System under the symbol “TEF.” They are also listed on the London and Buenos Aires stock exchanges. American Depositary Shares (“ADSs”), each representing the right to receive one ordinary share, are listed on the New York Stock Exchange 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.

As used herein, “Telefónica,” “Telefónica Group,” “Group”, the “Company” and terms such as “we,” “us” and “our” refer to Telefónica, S.A. and its consolidated subsidiaries, unless the context requires otherwise.

As used herein, “Atento” means Atento, Inversiones y Teleservicios, S.A. and its consolidated subsidiaries, unless the context requires otherwise.

Below are definitions of certain technical terms used in this Annual Report:

“Access” refers to a connection to any of the telecommunications services offered by us. We present our customer base using accesses as a data point because the integration of telecommunications services in bundled service packages has changed the way residential and corporate customers contract for our services. A single fixed customer may contract for multiple services, and we believe it is more useful to count the number of accesses a customer has contracted for, than to merely count the number of our customers. For example, a customer that has fixed line telephony service and broadband service is counted as two accesses rather than as one customer. For mobile customers, we count each active SIM as an access regardless of the number of services contracted through the SIM, e.g. voice and data.

“ARPU” is the average revenues per user per month. ARPU is calculated by dividing total gross service revenues (excluding inbound roaming revenues) from sales to customers for the preceding 12 months by the weighted average number of accesses for the same period, and then dividing by 12.

“Bundles” refer to combination products that combine fixed services (wirelines, broad bands and television) and mobile services.

“Churn” is the percentage of disconnections over the average customer base during a given period.

“Cloud computing” is the delivery of computing as a service rather than a product, whereby shared resources, software and information are provided to computers and other devices as a utility over a network (typically the Internet).

“Commercial activity” includes the addition of new lines, replacement of handsets, migrations and changes in types of contracts.

“Data ARPU” is the average data revenues per user per month. Data ARPU is calculated by dividing total data revenues (from sources such as Short Message Service (SMS), Multimedia Messaging Services (MMS), other mobile data services such as mobile connectivity and mobile internet, premium messaging, downloading ringtones and logos, mobile mail and wireless application protocol (WAP) connectivity from sales to customers for the preceding 12 months by the weighted average number of accesses for the same period, and then dividing by 12.

“Data revenues” include revenues from SMS, MMS, other mobile data services such as mobile connectivity and mobile internet, premium messaging, downloading ringtones and logos, mobile mail and WAP connectivity from sales to

customers.

“Data traffic” includes all traffic from Internet access, messaging (SMS, MMS) and connectivity services that is transported by the networks owned by Telefónica.

“Final client accesses” means accesses provided directly to residential and corporate clients.

“Fixed telephony accesses” includes public switched telephone network, or PSTN, lines (including public use telephony), and integrated services digital network, or ISDN, lines and circuits. For purposes of calculating our number of

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fixed line accesses, we multiply our lines in service as follows: PSTN (x1); basic ISDN (x1); primary ISDN (x30, x20 or x10); 2/6 digital accesses (x30).

"Fixed termination rates" is an established fixed network tariff that applies when a customer makes a call to someone in a network operated by another operator.

"FTTx" is a generic term for any broadband network architecture that uses optical fiber to replace all or part of the metal local loop typically used for the last mile of telecommunications wiring.

"Gross adds" means the gross increase in the customer base measured in terms of accesses in a period.

"HDTV" or "high definition TV" has at least twice the resolution of standard definition television (SDTV), allowing it to show much more detail than an analog television or digital versatile disc (DVD).

"Incoming revenues" refers to the interconnection revenues derived from the completion of calls made from outside mobile or fixed carriers into Telefónica's network.

"Interconnection revenues" means revenues received from other operators which use our networks to connect to our customers.

"Internet and data accesses" include broadband accesses (including retail asymmetrical digital subscriber line "ADSL," very high bit-rate digital subscriber line "VDSL", satellite, fiber optic and circuits over 2 Mbps), narrowband accesses (Internet service through the PSTN lines) and the remaining non-broadband final client circuits. Internet and data accesses also include "Naked ADSL", which allows customers to subscribe for a broadband connection without a monthly fixed line fee.

"IPTV" (Internet Protocol Television) refers to distribution systems for television subscription signals or video using broadband connections over the IP protocol.

"ISP" means Internet service provider.

"IT", or information technology, is the acquisition, processing, storage and dissemination of vocal, pictorial, textual and numerical information by a microelectronics-based combination of computing and telecommunications.

"Local loop" means the physical circuit connecting the network termination point at the subscriber's premises to the main distribution frame or equivalent facility in the fixed public telephone network.

"LTE" means Long Term Evolution, a 4G mobile access technology.

"M2M", or machine to machine, refers to technologies that allow both mobile and wired systems to communicate with other devices of the same ability.

"Market share" is the percentage ratio of the number of final accesses or operator revenues over the existing total market in an operating area.

"Mobile accesses" includes accesses to the mobile network for voice and/or data services (including connectivity). Mobile accesses are categorized into contract and prepaid accesses.

“Mobile broadband” includes Mobile Internet (internet access from devices also used to make voice calls such as smartphones), and Mobile Connectivity (internet access from devices that complement fixed broadband, such as PC Cards/dongles, which enable large amounts of data to be downloaded on the move).

“MTR” means mobile termination rate, which is the charge per minute or SMS paid by a telecommunications network operator when a customer makes a call to another network operator.

“MVNO” means mobile virtual network operator, which is a mobile operator that is not entitled to use spectrum for the provision of mobile services. Consequently, an MVNO must subscribe to an access agreement with a mobile network operator in order to provide mobile access to their customers. An MVNO pays such mobile network operator for using the infrastructure to facilitate coverage to their customers.

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“Net adds” means the difference between the customer bases measured in terms of accesses at the end of the period and the beginning of the period.

“Non SMS data revenues” means data revenues excluding SMS revenues.

“OTT services” or “over the top services” means services provided through the Internet (such as television).

“Outgoing revenues” refers to mobile voice or data revenues derived from our consumers’ consumed service.

“P2P SMS” means person to person short messaging service (usually sent by mobile customers).

“Pay-TV” includes cable TV, direct to home satellite TV, or DTH, and Internet Protocol TV, or IPTV.

“Revenues” means net sales and revenues from rendering of services.

“Service revenues” means revenues less revenues from handset sales. Service revenues are mainly related to telecommunications services, especially voice revenues and data revenues (SMS and data traffic download and upload revenues) consumed by our customers.

“SIM” means subscriber identity module, a removable intelligent card used in mobile handsets, USB modems, etc. to identify the user in the network.

“Unbundled local loop”, or “ULL” includes accesses to both ends of the copper local loop leased to other operators to provide voice and DSL services (fully unbundled loop, fully UL) or only DSL service (shared unbundled loop, “shared UL”).

“Voice Traffic” means voice minutes used by our customers over a given period, both outbound and inbound.

“VoIP” means voice over Internet protocol.

“Wholesale accesses” means accesses we provide to our competitors, who then sell services over such accesses to their residential and corporate clients.

“Wholesale ADSL” means accesses of broad band or fiber that we provide to our competitors, who then sell services over such accesses to their residential and corporate clients.

In this Annual Report we make certain comparisons in local currency or on a “constant euro basis” or “excluding foreign exchange rate effects” in order to present an analysis of the development of our results of operations from year-to-year without the effects of currency fluctuations. To make comparisons on a local currency basis, we compare financial items in the relevant local currency for the periods indicated as recorded in the relevant local currency for such periods. To make comparisons on a “constant euro basis” or “excluding foreign exchange rate effects,” we convert the relevant financial item into euro using the prior year’s average euro to relevant local currency exchange rate. In addition, we present certain financial information excluding the effects of Venezuela being considered a hyperinflationary economy in 2012, 2013 and 2014 by eliminating all adjustments made as a result of such consideration.

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PRESENTATION OF CERTAIN FINANCIAL INFORMATION

In this Annual Report, references to “U.S. dollars,” “dollars” or “\$,” are to United States dollars, references to “pounds sterling,” “sterling” or “£” are to British pounds sterling, references to “reais” refer to Brazilian reais and references to “euro” “euros” or “€” 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.

Our consolidated financial statements as of December 31, 2013 and 2014, and for the years ended December 31, 2012, 2013 and 2014 included elsewhere in this Annual Report including the notes thereto (the “Consolidated Financial Statements”), are prepared in conformity with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

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PART I

Item 1. Identity of Directors, Senior Management and Advisors

A. Directors and Senior Management

Not applicable.

B. Advisers

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 certain selected consolidated financial data. It is to be read in conjunction with “Item 5. Operating and Financial Review and Prospects” and the Consolidated Financial Statements. The consolidated income statement and cash flow data for the years ended December 31, 2012, 2013 and 2014 and the consolidated statement of financial position data as of December 31, 2013 and 2014 set forth below are derived from, and are qualified in their entirety by reference to the Consolidated Financial Statements. The consolidated income statement and cash flow data for the years ended December 31, 2010 and 2011 and the consolidated statement of financial position data as of December 31, 2010, 2011 and 2012 set forth below are derived from Telefónica, S.A.’s consolidated financial statements for such years, which are not included herein.

Our Consolidated Financial Statements have been prepared in accordance with IFRS as issued by the IASB.

The basis of presentation is described in detail in Note 2 to our Consolidated Financial Statements.

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Millions of euros	2010	2011	2012	2013	2014
Revenues	60,737	62,837	62,356	57,061	50,377
Other income	5,869	2,107	2,323	1,693	1,707
Supplies	(17,606)	(18,256)	(18,074)	(17,041)	(15,182)
Personnel expenses	(8,409)	(11,080)	(8,569)	(7,208)	(7,098)
Other expenses	(14,814)	(15,398)	(16,805)	(15,428)	(14,289)
Depreciation and amortization	(9,303)	(10,146)	(10,433)	(9,627)	(8,548)
OPERATING INCOME	16,474	10,064	10,798	9,450	6,967
Share of (loss) profit of associates	76	(635)	(1,275)	(304)	(510)
Net finance expense	(2,537)	(2,782)	(3,062)	(2,696)	(2,519)
Net exchange differences	(112)	(159)	(597)	(170)	(303)
Net financial expense	(2,649)	(2,941)	(3,659)	(2,866)	(2,822)
PROFIT BEFORE TAX FROM CONTINUING OPERATIONS	13,901	6,488	5,864	6,280	3,635
Corporate income tax	(3,829)	(301)	(1,461)	(1,311)	(383)
PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS	10,072	6,187	4,403	4,969	3,252
Profit after taxes from discontinued operations	–	–	–	–	–
PROFIT FOR THE YEAR	10,072	6,187	4,403	4,969	3,252
Non-controlling interests	95	(784)	(475)	(376)	(251)
PROFIT FOR THE YEAR ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT	10,167	5,403	3,928	4,593	3,001
Weighted average number of shares (thousands)(1)	4,705,217	4,693,707	4,603,539	4,627,912	4,606,389
Basic and diluted earnings per share from continuing operations attributable to equity holders of the parent (euro)(1)	2.16	1.15	0.85	0.99	0.61
Basic and diluted earnings per share attributable to equity holders of the parent (euro)(1)	2.16	1.15	0.85	0.99	0.61
Earnings per ADS (euro)(1)(2)	2.16	1.15	0.85	0.99	0.61
Weighted average number of ADS (thousands)(1)(2)	4,705,217	4,693,707	4,603,539	4,627,912	4,606,389
Cash dividends per ordinary share (euro)	1.30	1.52	0.82	0.35	0.75
Consolidated Statement of Financial Position Data					
Cash and cash equivalents	4,220	4,135	9,847	9,977	6,529
Property, plant and equipment	35,802	35,469	35,021	31,040	33,343
Total assets	129,775	129,623	129,773	118,862	122,299
Non-current liabilities	64,599	69,662	70,601	62,236	62,311
Equity (net)	31,684	27,383	27,661	27,482	30,289
Capital stock	4,564	4,564	4,551	4,551	4,657
Consolidated Cash Flow Data					
Net cash from operating activities	16,672	17,483	15,213	14,344	12,193
Net cash used in investing activities	(15,861)	(12,497)	(7,877)	(9,900)	(9,968)
Net cash used in financing activities	(5,248)	(4,912)	(1,243)	(2,685)	(4,041)

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- (1) The per share and per ADS computations for all periods presented have been presented using the weighted average number of shares and ADSs, respectively, outstanding for each period, and have been adjusted to reflect the stock dividends which occurred during the periods presented, as if these had occurred at the beginning of the earliest period presented, and have also been adjusted for mandatorily convertible notes issued in 2014. In accordance with IAS 33 (“Earnings per share”), the weighted average number of ordinary shares and ADSs outstanding for each of the periods covered has been restated to reflect the issuance of shares pursuant to Telefónica’s scrip dividend in June 2012 and December 2014. As a consequence, basic and diluted earnings per share have also been restated from 2010 to 2013.
- (2) Until January 20, 2011, each ADS represented the right to receive three ordinary shares. Since January 21, 2011, each ADS represents the right to receive one ordinary share. The above figures have been restated accordingly. Figures do not include any charges of the ADS Depositary.

Exchange Rate Information

As used in this Annual Report, the term “Noon Buying Rate” refers to the rate of exchange for euro, 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 February 20, 2015 was \$1.1372= 1.00 euro. 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 1.00 euro.

Noon Buying Rate

Year ended December 31,	Period end	Average (1)	High	Low
2010	1.3269	1.3218	1.4536	1.1959
2011	1.2973	1.4002	1.4875	1.2926
2012	1.3186	1.2909	1.3463	1.2062
2013	1.3779	1.3303	1.3816	1.2774
2014	1.2101	1.3155	1.3816	1.2447
2015 (through February 20, 2015)	1.1372	1.1516	1.2015	1.1279

Source: Federal Reserve Bank of New York.

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

Noon Buying Rate

Month ended	High	Low
August 31, 2014	1.3436	1.3150
September 30, 2014	1.3136	1.2628
October 31, 2014	1.2812	1.2517
November 30, 2014	1.2554	1.2394
December 31, 2014	1.2504	1.2101
January 31, 2015	1.2015	1.1279
February 28, 2015 (through February 20, 2015)	1.1462	1.1300

Source: Federal Reserve Bank of New York.

Monetary policy within the member states of the euro zone is set by the European Central Bank.

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 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 ADSs 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 and recorded (principally the Brazilian real, the pound sterling, the Argentine peso, the Peruvian nuevo sol, the Chilean peso, the Colombian peso, the Mexican peso and the Venezuelan bolívar fuerte). See Note 3 (b) to our Consolidated Financial Statements for information on the exchange rate translation methodology we used in preparing our consolidated financial information.

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B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

The Telefónica Group's business is conditioned by a series of intrinsic risk factors that affect exclusively the Group, as well as a series of external factors that are common to businesses of the same sector. The main risks and uncertainties facing the Company which could affect its business, financial position, reputation, corporate image and brand and its results of operations, must be considered jointly with the information in the Consolidated Financial Statements, and are as follows:

Group-related risks

Worsening of the economic and political environment could negatively affect Telefónica's business.

Telefónica's international presence enables the diversification of its activities across countries and regions, but it is affected by various legislations, as well as the political and economic environments of the countries in which it operates. Any adverse developments or even uncertainties in this regard, including exchange-rate or sovereign-risk fluctuations, may adversely affect the business, financial position, cash flows and/or the performance of some or all of the Group's financial indicators.

With respect to the economic environment, the Telefónica Group's business is impacted by overall economic conditions in each of the countries in which it operates. Economic conditions may adversely affect the level of demand of existing and prospective customers, as they may no longer deem critical the services offered by the Group. Factors such as high debt levels, ongoing restructuring of the banking sector, the implementation of pending structural reforms and continued fiscal austerity measures could hinder more dynamic growth in Europe and, in turn, the consumption and volume of demand for the Group's services, which could materially adversely affect the Group's business, financial condition, results of operations and cash flows.

The soft economic recovery in Europe together with low inflation rates, and the risk of deflation, has led and may still lead to monetary and fiscal easing from key players, with a view to creating a relatively benign scenario for Europe. In this region, the Telefónica Group generated 23.9% of its total revenues in Spain, 14.0% in the United Kingdom and 11.0% in Germany in 2014.

In addition, the Group's business may be affected by other possible effects from the economic crisis, including possible insolvency of key customers and suppliers.

In Latin America, the most important challenge is the exchange-rate risk in Venezuela and Argentina, given the negative impact that a depreciation in their currencies could have on cash flows from both countries. International financial conditions may be unfavorable and may lead to potential periods of volatility linked to the evolution of the developed financial markets (especially long-term interest rates in the United States affected by the U.S. Federal Reserve's intervention that are not discounted in the market), an economic slowdown in Asia (a key region for Latin America) and slow progress with structural reforms projects in the majority of these countries limiting potential for

higher growth rates. Among the most significant macroeconomic risk factors in the region are the high inflation rates, negative economic growth and high internal and external funding needs in Venezuela. These funding needs are significant and are affected by the recent fall in oil prices, which is the main and almost sole source of foreign currency in the country. These factors are affecting Venezuela's competitiveness and may result in a currency

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devaluation. Other risks in the region are Argentina's high level of inflation coupled with a phase of economic slowdown and weak public finances. Moreover, the recent decline in the prices of oil and other commodities could have a negative impact on the external accounts of countries such as Brazil, Chile, Peru and Colombia.

In relation to the political environment, the Group's investments and operations in Latin America could be affected by a series of risks related to economic, political and social factors in these countries, collectively denominated "country risk". For the year ended December 31, 2014, Telefónica Hispanoamérica and Telefónica Brazil represented 26.1% and 22.3% of the Telefónica Group's revenues, respectively. Moreover, approximately 9.6% of the Group's revenues in the telephony business are generated in countries that do not have investment grade status (in order of importance, Argentina, Venezuela, Ecuador, Nicaragua, Guatemala, El Salvador and Costa Rica), and other countries are only one notch away from losing this threshold. It is also significant that, despite clear improvements in Brazil, the uncertainty surrounding the political situation, fiscal policy stimuli and a relatively high inflation rate could result in a rating downgrade that, depending on the extent of such downgrade, could result in strong exchange-rate volatility due to an outflow of investments, especially in relation to fixed-income.

"Country risk" factors include the following:

- government regulation or administrative policies may change unexpectedly, including changes that modify the terms and conditions of licenses and concessions and their renewal (or delay their approvals), which could negatively affect the Group's business in such countries;
- abrupt exchange-rate fluctuations may occur mainly due to high levels of inflation and both fiscal and external deficits with the resulting exchange-rate overvaluation. This movement could lead to strong exchange-rate depreciation in the context of a floating exchange rate regime, a significant devaluation off the back of abandoning fixed exchange rates regimes or the introduction of varying degrees of restrictions on capital movement. For example, in Venezuela, the official U.S. dollar to bolívar fuerte exchange rate is established by the Central Bank of Venezuela and the Minister of Finance, with an alternative market for attracting foreign currency through the Complementary System for Administration of Foreign Currency (Sistema Complementario de Administración de Divisas or "SICAD") regular and selective auctions. In February 2015, a new Exchange Rate Agreement was established, including the regulations for the Foreign Exchange Marginal System (SIMADI), and the Central Bank of Venezuela published on February 18, 2015 a weighted average exchange rate equal to 172.1 bolívares to the U.S. dollar for the markets referred to in chapters II and IV of such Exchange Rate Agreement. Additionally, the acquisition or use of foreign currencies by Venezuelan or Argentinean companies (in some cases) to pay foreign debt or dividends is subject to the pre-authorization of the relevant authorities. Also, the Argentinean peso, despite its recent stability, continues to be under the threat of a sustained accelerated depreciation against the U.S. dollar;
- governments may expropriate or nationalize assets, make adverse tax decisions or increase their participation in the economy and in companies;
- economic-financial downturns, political instability and civil disturbances may negatively affect the Telefónica Group's operations in such countries; and
- maximum limits on profit margins may be imposed in order to limit the prices of goods and services through the analysis of cost structures. For example, in Venezuela, a maximum profit margin has been introduced that will be set annually by the Superintendencia for Defense of Socioeconomic Rights.

Any of the foregoing may adversely affect the business, financial position, results of operations and cash flows of the Group.

The Group's financial condition and results of operations may be adversely affected if it does not effectively manage its exposure to foreign currency exchange rates, interest rates or financial investment risks.

At December 31, 2014, 70% of the Group's net debt (in nominal terms) was pegged to fixed interest rates for a period greater than one year, while 27% was denominated in a currency other than the euro.

To illustrate the sensitivity of financial expenses to a change in short-term interest rates at December 31, 2014: (i) a 100 basis points increase in interest rates in all currencies in which Telefónica has a financial position at that date would lead

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to an increase in financial expenses of 111 million euros, (ii) whereas a 100 basis points decrease in interest rates in all currencies except the euro, the U.S. dollar and the pound sterling (these to zero rates in order to avoid negative rates), would lead to a reduction in financial expenses of 68 million euros. These calculations were made using the same balance position in each currency and same balance position equivalent at such date and bearing in mind the derivative financial instruments arranged.

According to the Group's calculations, the impact on results and specifically changes in the value of a 10% depreciation of Latin American currencies against the U.S. dollar and a 10% depreciation of the rest of the currencies against the euro would result in exchange losses of 76 million euros, primarily due to the weakening of the Venezuelan bolivar and the Argentinean peso. These calculations were made using the same balance position in each currency with an impact on profit or loss at such date, including derivative instruments in place. For the year ended December 31, 2014, 22.8% of the Telefónica Group's operating income before depreciation and amortization (OIBDA) was concentrated in Telefónica Brazil, 26.2% in Telefónica Hispanoamérica and 11.2% in the Telefónica United Kingdom.

The Telefónica Group uses a variety of strategies to manage these risks, mainly through the use of financial derivatives, which themselves also expose us to risk, including counterparty risk. Furthermore, the Group's risk management strategies may not achieve the desired effect, which could adversely affect the Group's business, financial condition, results of operations and cash flows.

Existing or worsening conditions in the financial markets may limit the Group's ability to finance, and consequently, the ability to carry out its business plan.

The performance, expansion and improvement of the Telefónica Group's networks, the development and distribution of the Telefónica Group's services and products, the development and implementation of the Company's strategic plan, the development and implementation of new technologies or the renewal of licenses as well as expansion of our business in countries where we operate may require a substantial amount of financing.

The performance of financial markets in terms of liquidity, cost of credit, access and volatility, continues to be overshadowed by persisting uncertainty regarding certain factors such as the pace of economic recovery, the health of the international banking system and concerns regarding the burgeoning deficits of some European countries. The worsening international financial market credit conditions caused by some of these factors could make it more difficult and more expensive to refinance existing financial debt or arrange new debt if necessary, and more difficult to raise funds from the Group's shareholders, and may negatively affect the Group's liquidity. At December 31, 2014, gross financial debt scheduled to mature in 2015 amounted to 8,491 million euros (which includes the net position of derivative financial instruments and certain current payables), and gross financial debt scheduled to mature in 2016 amounted to 8,407 million euros. Despite having covered gross debt maturities of 2015, 2016 and part of 2017 by available cash and lines of credit at December 31, 2014, possible difficulties in maintaining the current safety margin, or the risk that this could be significantly and unexpectedly exhausted, could force Telefónica to use resources allocated for other investments or commitments for payment of its financial debt, which could have a negative effect on the Group's businesses, financial position, results of operations or cash flows.

In 2013 the Telefónica Group issued bonds mainly (i) in euro totaling 3,250 million euros with an average coupon of 3.690%; (ii) in dollars totaling 2,000 million U.S. dollars with an average coupon of 3.709%; and (iii) in Swiss Francs totaling 225 million Swiss francs with an annual coupon of 2.595%. The Telefónica Group also issued undated deeply subordinated securities in euros totaling 1,750 million euros with an average coupon of 6.902%; and in sterling pounds totaling 600 million sterling pounds with a coupon of 6.750%. In 2014 the Telefónica Group issued bonds mainly in the European market with a maturity of eight years totaling 1,250 million euros with an annual coupon of

2.242%, and bonds with a fifteen-year maturity totaling 800 million euros with an annual coupon of 2.932%. In addition, the Telefónica Group issued undated deeply subordinated securities in 2014 totaling 2,600 million euros with an average coupon of 5.075%.

Despite having its gross debt maturities profile covered for more than two years, obtaining financing on the international capital markets could also be restricted, in terms of access and cost, if Telefónica's credit ratings are revised downwards, either due to lower solvency or operating performance, or as a result of a downgrade in the rating for Spanish sovereign risk by rating agencies. Any of these situations could have a negative impact on the Group's ability to meet its debt maturities.

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Moreover, market conditions could make it harder to renew existing undrawn credit lines, 8% of which, at December 31, 2014, were scheduled to mature prior to December 31, 2015.

In addition, the impact of the sovereign debt crisis and the rating downgrades in certain Eurozone countries should be taken into account. Any deterioration in the sovereign debt markets, doubts about developments in European projects (such as implementation of the banking union project, the results of the elections in Europe, including Spain among others, or progress towards fiscal integration), as well as further credit restrictions by the banking sector could have an adverse effect on the Telefónica Group's ability to access funding and/or liquidity, which could have a significant adverse effect on the Group's businesses, financial position, results of operations and cash flows.

Risks Relating to the Group's Industry

The Group operates in a highly regulated industry which requires government concessions for the provision of a large part of its services and the use of spectrum, which is a scarce and costly resource.

The telecommunications sector is subject to laws and regulations in different countries, and additionally, many of the services the Group provides require the granting of a license, concession or official approval, which usually requires certain obligations and investments to be made, such as those relating to spectrum availability. Among the main risks of this nature are those related to spectrum regulation and licenses/concessions, rates, universal service regulation, regulated wholesale services over fiber networks, privacy, functional separation of businesses and network neutrality.

Thus, as the Group provides most of its services under licenses, authorizations or concessions, it is vulnerable to administrative bodies' decisions, such as economic fines for serious breaches in the provision of services and, potentially, revocation or failure to renew these licenses, authorizations or concessions, or the granting of new licenses to competitors for the provisions of services in a specific market.

In this regards, the Telefónica Group pursues its license renewals in the terms referred in their respective contractual conditions, though it cannot guarantee that it will always complete this process successfully or under the most beneficial terms for the Group. In many cases complying with certain obligations is required, including, among others, minimum specified quality, service and coverage standards and capital investment. Failure to comply with these obligations could result in the imposition of fines, revision of the contractual terms, or even the revocation of the license, authorization or concession. Additionally, the Telefónica Group could be affected by regulatory actions carried out by the antitrust authorities. These authorities could prohibit certain actions, such as new acquisitions or specific practices, create obligations or lead to heavy fines. Any such measures implemented by the competition authorities could result in economic and/or reputational loss for the Group, in addition to a loss of market share and/or harm to the future growth of certain businesses.

Regulation of spectrum and government concessions

In Europe, the amendments by the EU Parliament to the Commission's proposal on the "Digital Single Market" (the "DSM") package of measures are currently being discussed by the European Council. The "DSM" measures include important measures affecting, inter alia, spectrum regulation. Although these measures are not yet final, they could have significant implications as they include new provisions on secondary markets, criteria to apply at auctions, renewals and terms of licenses, etc.

In addition, the main allocation criteria for the 700 MHz band of "Digital Dividend II" (the second spectrum allocation process from television operators to electronic communications services) will be defined in the coming years. This could require new cash outflows ahead of the Group's previously anticipated schedule (it is expected that the spectrum

will be available between 2018 and 2021).

Nevertheless, Germany will be the first country in Europe to award spectrum in the 700 MHz band. On January 29, 2015, the German regulator (“BNetzA”) published respective final decisions on the spectrum allocation proceedings and on the auction conditions of the 700 MHz and 1500 MHz bands. The auction will also include the spectrum corresponding to GSM licenses – the entire 900 MHz band and most of the 1800 MHz band (which will expire at the end of 2016) –. Interested bidders may submit applications by March 6, 2015. The auction (Simultaneous Multi-Round Auction) will take place in the second quarter of 2015.

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On July 4, 2014, BNetzA adopted a decision concerning the frequency aspects of the Telefónica Deutschland Holding AG merger with E-Plus Mobilfunk GmbH & Co KG (“E-Plus”). BNetzA has instructed Telefónica Deutschland (the surviving entity after the merger takes place) to anticipate the termination of its rights of use in the 900 / 1800 MHz bands by December 31, 2015, (instead of December 31, 2016), if Telefónica Deutschland does not reacquire these frequencies at the above-mentioned auction proceeding. Both Telefónica Deutschland and E-Plus have legally challenged this BNetzA decision on August 4, 2014. The German regulator also announced that, once the auction of spectrum mentioned above is over, it will perform a frequency distribution analysis, and determine whether any additional action is needed, particularly in the area of the 2GHz spectrum band granted to Telefonica Deutschland.

In addition, and within the framework of the conditions imposed by the European Commission in connection with the merger, the surviving entity of the merger is obliged to offer up to 2x10 MHz in the 2600 MHz as well as up to 2x10 MHz in the 2100 MHz spectrum band to one potential new mobile network operator. This offer is open to any potential new mobile network operator that had declared a respective interest by December 31, 2014 and to the operator with whom Telefónica Deutschland has signed the network access agreement (Drillisch Group).

On December 26, 2014, the Spanish Government adopted a law in which it delayed, to a maximum period ended on April 1, 2015, the effective delivery of the frequencies in the 800 MHz spectrum which are part of the "Digital Dividend" (the spectrum allocation process from television operators to electronic communications services), and which were expected to be delivered on January 1, 2015 to the already awarded mobile operators. The license term has been extended accordingly to April 24, 2031.

In the United Kingdom a significant increase in the annual license fees charged for the use of the spectrum in 900 MHz and 1800 MHz bands has been proposed by the regulator (the Office of Communications (“Ofcom”). The outcome of it remains uncertain. Separately, the United Kingdom Government announced recently an agreement with the United Kingdom mobile operators, including Telefonica United Kingdom, under which the mobile operators would accept a 90% geographic coverage obligation for voice and text services. Given the agreement, Ofcom has agreed to consider the impact of the geographic coverage obligation on its valuation of annual fees for 900 MHz and 1800 MHz spectrum. This is expected to delay Ofcom’s decision. In addition, on November 7, 2014, Ofcom released a public consultation on the award of 2.3 GHz and 3.4 GHz bands that is expected to take place in late 2015 or early 2016.

In Latin America, spectrum auctions are expected to take place implying potential cash outflows to obtain additional spectrum or to meet the coverage requirements associated with these licenses. Specifically, the procedures expected to take place in 2015 are:

- Peru: The government announced plans to auction the 700 MHz spectrum band in the first half of 2015 (three blocks of 2x15 MHz have been defined).
- Costa Rica: Costa Rica’s government has communicated its intention to auction spectrum in the 1800 MHz and AWS bands during 2015.
- Mexico: The Federal Institute of Telecommunications (Instituto Federal de Telecomunicaciones) (“IFT”) published its Annual Program for Frequency Use and Development 2015. The program specifies IFT’s intention to award Advanced Wireless Services “AWS” concessions during the course of 2015.

Further to the above, certain administrations may not have announced their intention to release new spectrum and may do so during the year. The above does not include processes announced via general statements by administrations, which involve bands not key to Telefónica’s needs. Telefónica may also seek to acquire spectrum on the secondary

market should opportunities arise.

In Argentina, on December 1, 2014, the Secretary of Communication through Resolution 85/2014 officially awarded Telefónica Argentina the block 1710-1720/2110-2120 for a period of 15 years, and the 700 MHz block (703-713/758-768 MHz) is expected to be officially transferred to Telefónica Argentina during 2015.

In the state of São Paulo, Telefónica Brasil provides local and national long-distance Commuted Fixed Telephony Service (CFTS) under the public regime, through a concession agreement, which will be in force until 2025. In this regard, in June 27, 2014, as established in the concession agreement, the National Telecommunications Agency (Agência Nacional de Telecomunicações) (“ANATEL”) issued a public consultation for the revision of the concession agreement. Such public

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consultation revising the concession agreement ended on December 26, 2014 and allowed contributions on certain topics such as service universalization, rates and fees and quality of services, among others. Definitive conditions will be published in 2015.

Additionally, in Colombia the Information and Communication Technologies (“ITC”) Ministry issued a Resolution on March 27, 2014 to renew 850 MHz/1900 MHz licenses for 10 additional years. The reversion of assets and the liquidation of the concession contract will be discussed until May 2015, taking into consideration the terms of the contract, and the Constitutional Court’s review of Law 422 of 1998, which established the reversion of only the radio-electric frequencies.

In Peru, an application for partial renewal of the concessions for the provision of the fixed-line service for another five years has been issued, although assurance has been given by the “Ministry of Transport and Communications” (Ministerio de Transportes y Comunicaciones) in previous renewals, that the concession will remain in force until November 2027. Also, a new law has been enacted establishing mobile virtual network operator (MVNOs) and Rural Mobile Infrastructure Operators (RMIOs) in the Peruvian market.

In Mexico, in light of the constitutional reform resulting from the “Pact for Mexico” political initiative, it is expected that a publicly-owned wholesale network, which will offer wholesale services in the 700 MHz band, will be created. As of today, the funding and the marketing model of this project have not yet been determined.

Telefónica Móviles Chile, S.A. was awarded spectrum on the 700 MHz (2x10 MHz) band in March 2014. A third party provider opposed this allocation of spectrum on the basis that it would exceed the limit spectrum of 60 MHz established by a judgment of the Supreme Court of January 27, 2009. This cap was established for the AWS auction held in 2009, but not for subsequent auctions (2600 MHz and 700 MHz). In a judgment on December 31, 2014, the court of appeals rejected the third party claim. Consequently, the regulator is in a position to adopt a Decree awarding the concession to Telefónica.

The consolidated investment in spectrum acquisitions and renewals in 2014 amounted to 1,294.2 million euros.

The Company’s failure to obtain sufficient or appropriate spectrum capacity in the jurisdictions discussed above or any others in which it operates or its inability to assume the related costs, could have an adverse impact on its ability to launch and provide new services and on the Company’s ability to maintain the quality of existing services, which may adversely affect the Group’s business, financial condition, results of operations and cash flows.

Regulation of wholesale and retail charges

In terms of roaming, the regulated “Eurotariffs” were reduced on July 1, 2014 (in the wholesale market, the price of data was reduced by 67%, the price of call by 50%; and in the retail market, the price of data was reduced by 55%, the price of outgoing voice call by 21%, the price of incoming voice call by 28% and the price of outgoing texts by 25%), as per the regulation approved in 2012. The structural roaming solutions which could lead to a price decrease in the intra-European Union roaming services also took effect in July 2014. Furthermore, the package of DSM measures mentioned above, which is under discussion, also includes a proposal to eliminate European Union roaming charges as of a yet to be determined date. However, the European Parliament proposed the “end of roaming” by December 15, 2015 in a proposal known as “Roaming Like at Home”.

The decreases in wholesale mobile network termination rates (“MTR”) in Europe are also noteworthy. In the United Kingdom, wholesale MTRs have been reduced to 0.845 ppm (pence/minute) from April 1, 2014 (representing a 0.3% reduction compared to the previous rates). In a consultation document published in June 2014, Ofcom has proposed a

further reduction to 0.545 ppm, from April 1, 2015.

In Germany, on September 3, 2014, the BNetzA adopted a proposal to reduce MTRs. The new prices will gradually decrease to 0.0172 euro/minute from December 1, 2014, and in a second stage, from 0.0172 euro/minute to 0.0166 euro/minute from December 1, 2015 until the end of November 2016. The European Commission has requested that the German regulator withdraw or amend its latest decision on mobile termination rates, in force as at the date of this Annual Report. There is a risk that the European Commission will initiate infringement proceedings against Germany, and rates may be further reduced.

In Spain, the National Regulatory & Competition Authority (Comisión Nacional de los Mercados y la Competencia) has adopted a final decision on the third round analysis of the wholesale market for fixed call termination. From November 1,

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2014, a symmetric fixed termination rate (“FTR”) of 0.0817 euro cents/minute applies, based on pure bottom-up long run incremental costs (“BU-LRIC”) meaning that billing must be entirely conducted on a “per second” basis, without a peak/off-peak differentiation. The decision therefore eliminates the asymmetry in FTRs that existed since 2006 when alternative network operators were allowed to charge up to 30% above Telefónica’s per minute local FTR. It also brings forth an important reduction in average termination prices for Telefónica (by 80%) in comparison to the former applicable tariffs.

In Latin America, there are also moves to review MTRs leading to these being reduced. Thus, for example, developments in Mexico are among the most relevant, where the IFT has declared the América Móvil Group a preponderant operator in the telecommunications market. As a result, on March 26, 2014, it introduced, among others, special regulations on asymmetric interconnection rates. In that sense, the Federal Telecommunications and Broadcasting law, effective as of August 13, 2014, imposed several obligations on the preponderant operator, which are quite extensive and, in principle, potentially significantly beneficial to Telefónica’s competitive position, particularly with regards to the measures imposed on preponderant operators (to the extent they nominally retain such qualification). With regards to MTR, Telefónica México filed an administrative appeal against the 2011 resolutions of the Federal Telecommunications Commission of México (Cofetel) regarding mobile network termination rates (representing a 61% reduction compared to the previous rates). As of the date of this Annual Report, no ruling has been made on this appeal. Recently, IFT determined the mobile termination rates for 2012, and Telefónica México filed an injunction against this rate. Once these appeals have been concluded, the rates applied may be further reduced retroactively. As of the date of this Annual Report, IFT has not approved the termination rates for 2013, 2014 or 2015 for Telefónica México.

In Brazil, at the end of 2012, ANATEL launched the “Plano Geral de Metas de Competição” (“PGMC”) regarding fixed-mobile rate adjustment reductions until February 2016 and amending the previous reduction conditions (75% of the 2013 rate in 2014 and 50% of the 2013 rate in 2015). In order to complement reductions and approach the cost of the services according to a financial cost model, on July 7, 2014, ANATEL published reference values for MTR taking effect from 2016 to 2019. Such reductions are approximately 44% per year. Furthermore, there are several legislative initiatives that aim to abolish the basic fee of fixed-telephony service. “Price protection” practices (reimbursement of differences in prices of a product to customers if this falls within a relative short period of time) may also have a negative impact in Telefónica Brasil, in both economic and image terms.

In Chile, a tariff decree was issued to set fixed-line termination charges for the 2014-2019 periods. The new tariff entered into effect on May 8, 2014 and applies a reduction of 37% in prices against those charged for the period prior to such tariff. A tariff decree has been issued for mobile networks covering the 2014-2019 five-year period. Such tariff decree entered into effect on January 25, 2014 and implies a reduction of 74.7% with respect to the previous rates. After a review by the general comptroller (Contraloría General) an additional 1.7% reduction was approved on May 27, 2014.

In Ecuador the rate-related risks relate to a reduction in rural and urban telephony charges, a reimbursement of top-up balances, as well as rounding to the nearest minute.

The implementation of the Enabling Act (Ley Habilitante) in Venezuela also confers full powers to the President to implement price control measures. Under this Act, in January 2014, an organic fair price law was issued, which caps the revenue of related enterprises at 30% of their operating costs. In relation to MTRs with the national operator of reference (Compañía Anónima Nacional Teléfonos de Venezuela) (“CANTV”), these have been reduced by 6% compared to the previous rates. In November 2014, near the end of the term allowing the enactment of laws autonomously granted to the President of the Republic, new important decree-laws were enacted, in particular, the Reform of the Law on Foreign Investment, in which, among other things, new requirements for the return of foreign

investment were established; the Reform of the Antitrust Law, which was predominantly aimed at enhancing monopoly control regulation and increasing penalties for infringement; and the Reform of the Exchange Crimes Law, which increased economic sanctions.

In Colombia, on December 30, 2014, the Colombian regulator (“CRC”) enacted Resolution 4660 establishing a gradual reduction for MTRs. The glide path initiates in 2015 in 32.88 Colombian pesos per minute representing a decrease of 41.7% and then descends approximately 42.2% in 2016 and 42.2% in 2017 (each such reduction being as compared to the previous year). This regulatory measure also imposes asymmetric MTRs to the dominant provider (the América Móvil Group), imposing the final rate established in the glide path from 2015 to 2017. The CRC also regulated the charges for national roaming and the SMS termination rates, setting a reduction of 41.5% in 2015, 39.6% in 2016 and 43.3% in 2017 (each such reduction being as compared to the previous year).

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Regulation of universal services

Further to its formal obligation to review the scope of the Universal Service Directive (the set of basic electronic communication services whose provision is guaranteed to any user requesting it, regardless of its location, with a specified quality at an affordable price), the European Commission is expected to undertake a public consultation in the months following the date of this Annual Report, which may include both the potential inclusion of broadband in its scope and a possible reduction of some of the current universal service obligations. Depending on the terms that will be set forth in the new regulation, implementation at a local level could lead to higher costs for both the universal service provider and the operators forced to finance the universal service.

The last Plano Geral de Metas de Universalização (“PGMU”) was published in Brazil on June 30, 2011 and applies to the 2011-2015 period. This sets goals for public phones, low cost fixed-lines and coverage density in rural and poor areas with 2.5GHz/450 MHz. Also according to such PGMU, the assets assigned to the provision of the services described in the public concession agreement are considered reversible assets. In 2014, ANATEL issued a public consultation with its proposals for the 2015-2020 period universalization targets. The agency’s proposal focuses on reducing the distance between public telephones and backhaul’s expansion.

Regulation of fiber networks

In December 2014, the Spanish National Regulatory & Competition Authority (Comisión Nacional de los Mercados y la Competencia) has conducted a public consultation on the regulatory obligations for broadband market regulation in Spain. As a result of this consultation, the new regulation that will apply to NGN (Next Generation Networks) could be approved in the fourth quarter of 2015 and will last for at least three years. This could increase Telefónica's regulatory obligations in Spain and the ability of other operators to compete in such market.

In Colombia, the regulatory authority CRC published a regulatory project for transmission capacity between municipalities through fiber networks or connectivity to impose open network and elements access through a mandatory offer for those enterprises that have overcapacity and have some unused installed network elements. This project will be discussed in the first half of 2015.

Regulations on privacy

In Europe, a new Data Protection Regulation is undergoing the European legislative process which, as the date of this Annual Report, is not expected to end before mid-2015. This could lead to certain critical provisions laid down in the current draft of the regulation (presently under debate) being worded in such a way that stops or hinders Telefónica from launching some services, that focus on the processing of personal data.

In Brazil, triggered by the approval of Civil Rights Framework for Internet Governance, which provides certain generic rules about data protection, the Ministry of Justice could in the near future, adopt the final version of the Draft Personal Data Protection Act. This could lead to a greater number of obligations for operators in relation to the collection of personal data of telecom services users and further restrictions on the treatment of such data.

Regulation of functional separation

The principles established in Europe’s common regulatory framework, adopted in 2009 and transposed in the national legislation of each Member State in which Telefónica operates could result in greater regulatory pressure on the local competitive environment. Specifically, this framework supports the possibility of national regulators (in specific cases and under exceptional conditions) forcing operators with significant market power and vertically-integrated operators

to separate their wholesale and retail businesses at a functional level. They would therefore be required to offer equal wholesale terms to third-party operators that acquire these products.

Regulation of network neutrality

In Europe, national regulators are seeking to strengthen their supervision of operators with regard to the blocking of access, discrimination of applications or Internet service quality. The European Parliament and the Council are simultaneously debating the draft of the European DSM Regulation proposed by the European Commission that, among other things, deals with the principle of network neutrality. The regulation of network neutrality could directly affect

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possible future business models of Telefónica and may affect the network management or differentiation of characteristics and quality of Internet access service.

Telefónica is present in countries where net neutrality has already been ruled, such as Chile, Colombia, Peru and more recently Brazil, but this remains a live issue and with varying degrees of development in other countries where it operates. In Germany, the Economy Minister withdrew a draft law that it published on June 20, 2013, to regulate net neutrality, especially with regard to the blocking and discrimination of content and Internet services. It plans to submit a new draft after the EU has settled on a position on net neutrality within the DSM approach, which might occur in early 2015. In addition, one German region (Bundesland of Thuringia) has passed a new law (which applies only in such region) with the aim that broadcasting and tele-media may not be blocked, limited or treated differently from other data traffic.

If changes to regulation such as those described above, or otherwise, occur in the various jurisdictions where the Telefónica Group operates, it could have a material adverse effect on its business, financial condition, results of operations and cash flows.

For a detailed description of these regulations see Appendix VII of the Consolidated Financial Statements “Key Regulatory Issues and Concessions and Licenses Held by the Telefónica Group”.

The Telefónica Group is exposed to risks in relation to compliance with anti-corruption laws and regulations and economic sanctions programs.

The Telefónica Group is required to comply with the laws and regulations of various jurisdictions where it conducts operations. In particular, the Group’s international operations are subject to the U.S. Foreign Corrupt Practices Act of 1977 (“FCPA”) and the United Kingdom Bribery Act of 2010 (the “Bribery Act”), and economic sanction programs, including those administered by the United Nations, the European Union and the United States, including the U.S. Treasury Department’s Office of Foreign Assets Control (“OFAC”). The FCPA prohibits providing anything of value to foreign officials for the purposes of obtaining or retaining business or securing any improper business advantage. As part of the Telefónica Group’s business, it may deal with entities, the employees of which are considered foreign officials for purposes of the FCPA. In addition, economic sanctions programs restrict the Group’s business dealings with certain sanctioned countries, individuals and entities.

Although the Group has internal policies and procedures designed to ensure compliance with applicable anti-corruption laws and sanctions regulations, there can be no assurance that such policies and procedures will be sufficient or that the Group’s employees, directors, officers, partners, agents and service providers will not take actions in violation of the Group’s policies and procedures (or otherwise in violation of the relevant anti-corruption laws and sanctions regulations) for which the Group or they may be ultimately held responsible. Violations of anti-corruption laws and sanctions regulations could have a material adverse effect on the Group’s business, reputation, results of operations and financial condition.

Customers’ perceptions of services offered by the Company may put it at a disadvantage compared to competitors’ offerings.

Customers’ perceptions of the assistance and services offered are critical to operating in highly-competitive markets. The ability to predict and respond to the changing needs and demands of customers affects the Company’s competitive position relative to other technology sector companies, and its ability to extract the value generated during this process of transformation. Failure to do so adequately could have an adverse impact on the Group’s business, financial condition, results of operations and cash flows.

Company may not be able to adequately foresee and respond to technological changes and sector trends.

In a sector characterized by rapid technological change, it is essential to be able to offer the products and services demanded by the market and consider the impacts of changes in the life cycle of technical assets, secure margins and select the right investments to make.

The Telefónica Group operates in markets that are highly competitive and subject to constant technological development. Therefore, as a consequence of both of these characteristics, it is subject to the effects of actions by competitors in these markets and to its ability to anticipate and adapt, in a timely manner, to constant technological changes, changes in customer preferences that are taking place in the industry, as well as economic, political and social circumstances.

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Failure to do so adequately could have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

New products and technologies arise constantly, and their development can render obsolete the products and services the Telefónica Group offers and the technology it uses. This means that Telefónica must invest in the development of new products, technology and services so it can continue to compete effectively with current or future competitors, and which may result in the decrease of the Group's profits and revenue margins. In this respect, margins from traditional voice and data business are shrinking, while new sources of revenues are deriving from mobile Internet and connectivity services that are being launched. Research and development costs amounted to 1,111 million euros and 1,046 million euros in 2014 and 2013, respectively; representing an increase of 6.2% from 1,046 million euros in 2013. These expenses represented 2.2% and 1.8% of the Group's consolidated revenue, respectively. These figures have been calculated using the guidelines established in the Organization for Economic Cooperation and Development (OECD) manual. One technology that telecommunications operators, including Telefónica (in Spain and Latin America), are focused on is the new FTTx-type network, which offers broadband access using optical fiber with superior services, such as Internet speed of up to 100MB or HD television services. However, substantial investment is required to deploy these networks, which entails fully or partially substituting copper loop access with optic fiber. While an increasing demand for the capabilities offered by these new networks to end users exists, the high level of the investments requires a continuous analysis of the return on investment.

The explosion of the digital market and entry of new players in communications market, such as MVNOs, Internet companies or device manufacturers, may cause the loss of value of certain assets, and affect the Group's ability to generate income. Therefore, it is necessary to update the business model, encouraging the pursuit of incomes and additional efficiencies to those followed traditionally. Failure to do so adequately could have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

In addition, the ability of the Telefónica Group's IT systems (operational and backup) to respond the Company's operating requirements is a key factor to be taken into account with respect to the commercial development, customer satisfaction and business efficiency.

The Company depends on its suppliers.

The existence of critical suppliers in the supply chain, especially in areas such as network infrastructure, information systems or handsets, with a high concentration in a small number of suppliers, poses risks that may affect the Company's operations, and may cause legal contingencies or damages to the Company's image in the event that inappropriate practices are produced by a participant in the supply chain.

As of December 31, 2014, the Telefónica Group depended on six handset suppliers and 11 network infrastructure suppliers, which together accounted for 80% of the awarded contracts for the year then ended. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own stock shortfalls and business requirements.

If these suppliers fail to deliver products and services to the Telefónica Group on a timely basis, it could jeopardize network deployment and expansion plans, which in some cases could adversely affect the Telefónica Group's ability to satisfy its license terms and requirements, or otherwise have an adverse impact on the Group's business, financial condition, results of operations and cash flows.

Unanticipated network interruptions can lead to quality loss or the interruption of the service.

Unanticipated network interruptions as a result of system failures, including those due to network, hardware or software, stealing of infrastructure elements or cyber-attacks, which affect the quality of or cause an interruption in the Telefónica Group's service, could lead to customer dissatisfaction, reduced revenues and traffic, costly repairs, penalties or other measures imposed by regulatory authorities and could harm the Telefónica Group's image and reputation.

Telefónica attempts to mitigate these risks through a number of measures, including backup systems and protective systems such as firewalls, virus scanners and other physical and logical security. However, these measures are not always effective. Although the Telefónica Group has insurance policies to cover these types of incidents, and the claims and loss in revenue caused by service interruptions to date have been covered by these policies, these policies may not be sufficient to cover all possible monetary losses.

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The telecommunications industry may be affected by the possible effects of electromagnetic fields, emitted by mobile devices and base stations, may have on human health.

In some countries, there is a concern regarding potential effects of electromagnetic fields, emitted by mobile devices and base stations, on human health. This public concern has caused certain governments and administrations to take measures that have hindered the deployment of the infrastructures necessary to ensure quality of service, and affected the deployment criteria of new networks and digital services such as smart meters development.

There is a consensus between certain expert groups and public health agencies, including the World Health Organization (WHO), that states that currently there are no established risks associated with exposure to low frequency signals in mobile communications. However, the scientific community is still investigating this issue especially with respect to mobile devices. Exposure limits for radio frequency suggested in the guidelines of the Protection of Non-Ionizing Radiation Protection Committee (ICNIRP) have been internationally recognized. The mobile industry has adopted these exposure limits and works to request authorities worldwide to adopt these standards.

Worries about radio frequency emissions may discourage the use of mobile devices and new digital services, which could cause the public authorities to implement measures restricting where transmitters and cell sites can be located, how they operate, the use of mobile telephones and the massive deployment of smart meters and other products using mobile technology. This could lead to the Company being unable to expand or improve its mobile network.

The adoption of new measures by governments or administrations or other regulatory interventions in this respect, and any future assessment on the adverse impact of electromagnetic fields on health, may negatively affect the business, financial conditions, results of operations and cash flows of the Telefónica Group.

Possible regulatory, business, economic or political changes could lead to asset impairment.

The Telefónica Group reviews on an annual basis, or more frequently when the circumstances require it, the value of assets and cash-generating units, to assess whether their carrying values can be supported by the future expected cash flows, including, in some cases synergies allowed for in acquisition costs. Potential changes in the regulatory, business, economic or political environment may result in the need to introduce changes to estimates made and to recognize impairments in goodwill, intangible assets or fixed assets. Although the recognition of impairments of property, plant and equipment, intangible assets and financial assets results in a non-cash charge on the income statement, it could adversely affect the results of the Telefónica Group's operations. In this respect, the Telefónica Group has experienced impairments on certain of its investments, affecting its results of operations in the year in which they were experienced. For example, with respect to the investment in Telco, S.p.A. ("Telco"), value adjustments were made in fiscal years 2013 and 2014 with a negative impact of 267 million euros and 464 million euros, respectively.

The Telefónica Group's networks carry and store large volumes of confidential, personal and corporate data, and its Internet access and hosting services may lead to claims for illegal or illicit use of the Internet.

The Telefónica Group's networks carry and store large volumes of confidential, personal and business data, through both voice and data traffic. The Telefónica Group stores increasing quantities and types of customer data in both business and consumer segments. Despite its best efforts to prevent it, the Telefónica Group may be found liable for any loss, transfer, or inappropriate modification of the customer data or general public data stored on its servers or transmitted through its networks, any of which could involve many people and have an impact on the Group's reputation, or lead to legal claims and liabilities that are difficult to measure in advance.

In addition, the Telefónica Group's Internet access and hosting servers could lead to claims for illegal or unlawful use of the Internet. Telefónica, like other telecommunications providers, may be held liable for any loss, transfer or inappropriate modification of the customer data stored on its servers or carried by its networks.

In most countries in which the Telefónica Group operates, the provision of its Internet access and hosting services (including the operation of websites with shelf-generated content) are regulated under a limited liability regime applicable to the content that it makes available to the public as a technical service provider, particularly content protected by copyright or similar laws. However, regulatory changes have been introduced imposing additional obligations on access providers (such as blocking access to a website) as part of the struggle against some illegal or illicit uses of the Internet, notably in Europe.

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Any of the foregoing could have an adverse impact on the business, financial position, results of operations and cash flows of the Group.

Telefónica and Telefónica Group companies are party to lawsuits, tax claims, antitrust and other legal proceedings.

Telefónica and Telefónica Group companies are party to lawsuits, tax claims and other legal proceedings in the ordinary course of their businesses, the financial outcome of which is unpredictable. An adverse outcome or settlement in these or other proceedings could result in significant costs and may have a material adverse effect on the Group's business, financial condition, results of operations, reputation and cash flows. In particular, regarding tax and antitrust claims, the Telefónica Group has open judicial procedures in Peru concerning the clearance of previous years' income tax, for which a contentious-administrative appeal is currently pending, as well as in Brazil, with CADE's (Conselho Administrativo de Defesa Econômica) resolution with regard to the acquisition of a 50% stake in Vivo and with certain open tax procedures, primarily relating to the CIMS (a Brazilian tax on telecommunication services). Further details on these matters are provided in Notes 21 and 17 of the Consolidated Financial Statements.

Item 4. Information on the Company

A. History and Development of the Company

Overview

Telefónica, 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 through one of the world's largest and most modern telecommunications networks;
- focused on providing telecommunications services; and
- present principally in Europe and Latin America.

The following significant events occurred in 2014:

- On February 8, 2013, the Venezuelan bolívar was devalued from 4.3 bolívares per U.S. dollar to 6.3 bolívares per U.S. dollar.

The exchange rate of 6.3 bolívares per U.S. dollar was used in the translation of the financial information of Venezuelan subsidiaries for the entirety of 2013.

During 2014, by virtue of certain Exchange Agreements the allocations conducted through the Complementary System for Administration of Foreign Currency (SICAD I), to which Telefónica Venezuela had access for imports, were expanded and, in addition, a new exchange mechanism with a more widespread use was put in place, called SICAD II.

The exchange rates resulting in the last allocations of SICAD I and SICAD II before December 31, 2014 were 12.0 and 49.988 bolívares per U.S. dollar, respectively.

In the absence of SICAD I auctions since mid-October 2014, and the lack of expectations of new auctions close to 2014 year-end, in a macroeconomic context aggravated by the fall of the oil price, the Company has decided to take as a reference the rate resulting in the allocations conducted through SICAD II for translating the financial statements of the Venezuelan subsidiaries. The Company considers that it is the most representative among the available official exchange rates at 2014 year-end for the monetary translation of the accounting figures of transactions, cash flows and balances.

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The main impacts of using this new exchange rate in the Telefónica Group's consolidated financial statements as of December 31, 2014 were as follows:

- A decrease in equity, within the caption "Translation differences", of approximately 2,950 million euros (see Note 12.f of the Consolidated Financial Statements) as a combined result of the translation to euros at the new exchange rate partially offset by the impact in equity of the inflation adjustment for the period.
- As part of the decrease mentioned in the preceding paragraph, the value in euros of the net financial assets denominated in bolívares decreased by approximately 2,700 million euros, as per the balance as of December 31, 2014.
- The results from the Telefónica's subsidiaries in Venezuela have been translated at the new exchange rate. This implied a reduction in operating income before depreciation and amortization (OIBDA) and profit of the year of, approximately, 1,730 and 660 million euros, respectively.
- On January 28, 2014, after obtaining the relevant regulatory approval, the sale of Telefónica Czech Republic, a.s. ("Telefónica Czech Republic") was completed. As a result of the sale, Telefónica held a 4.9% stake in Telefónica Czech Republic, which it subsequently sold in October 2014 for 160 million euros.
- On February 26, 2014, the Board of Directors of Telefónica approved the implementation of a new organizational structure focused on clients and that incorporates its digital offering as the main focus for commercial policies. The structure aims to give greater visibility to local operations, bringing them closer to the corporate decision-making center, simplifying the global structure and strengthening the cross-cutting areas to make the decision-making process more efficient.

Within this framework, Telefónica created the role of the Chief Commercial Digital Officer, who is responsible for fostering revenue growth. On the cost side, the Company strengthened the role of the Chief Global Resources Officer. Both Officers report directly to the Chief Operating Officer (COO), as do the local business CEOs for Spain, Brazil, Germany and the United Kingdom, in addition to the Latin American Unit, which now excludes Brazil.

- On February 27, 2014, the Board of Directors of Telefónica agreed to determine the amount of the 2014 dividend at 0.75 euro per share, payable in two tranches:
 - 0.40 euro per share in cash in the second quarter of 2015.
 - 0.35 euro per share by means of a "scrip dividend" in the fourth quarter of 2014.
- On May 6, 2014, Telefónica submitted a binding offer for the acquisition of 56% of the share capital of Distribuidora de Televisión Digital, S.A. ("DTS"), directly or indirectly owned by Promotora de Informaciones, S.A. (PRISA).
- On May 7, 2014, Telefónica paid a dividend of 0.40 euro per share in cash (dividend distribution charged against 2014 net income) corresponding to the second tranche of the 2013 dividend which in total amounted to 0.75 euro per share.
- On May 30, 2014, Telefónica's Annual General Shareholders' Meeting took place on second call with the attendance, present or represented, of 54.81% of the share capital. In this meeting, all the resolutions submitted by the Board of Directors for deliberation and approval were approved by majority of votes.

- On June 2, 2014, Telefónica's subsidiary Telefónica de Contenidos, S.A.U. ("Telefónica Contenidos") executed a share purchase agreement with PRISA in connection with PRISA's stake in DTS. The price agreed amounts to 750 million euros, subject to customary adjustments at closing. The closing of this purchase agreement is subject to obtaining the relevant authorization of the competition authorities and to the approval of a representative panel of the banks financing PRISA.
- On July 2, 2014, Telefónica Deutschland received the EU Commission's conditional clearance to acquire the E-Plus Group from the Dutch telecommunication corporation Koninklijke KPN N.V. In connection with such

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conditional clearance, on June 25, 2014, Telefónica Deutschland signed an agreement with the Drillisch Group according to which the latter agreed to acquire, in addition to the agreed capacity to provide services to its existing customers through Telefónica Deutschland's or the E-Plus Group's networks, 20% of the capacity of all mobile networks that belong to Telefónica Deutschland after the acquisition of the E-Plus Group. The 20% capacity will be reached gradually over a 5-year period. In addition, the Drillisch Group will have the right to acquire up to an additional 10% of capacity of the aforementioned mobile networks.

Telefónica Deutschland will grant the Drillisch Group, through a Mobile Bitstream Access model, access to the future joint network of Telefónica Deutschland and the E-Plus Group, as well as to the existing and future technology developments on that network, which the Drillisch Group will be able to offer to its customers. Final clearance for the acquisition was given on August 29, 2014. On October 1, 2014, Telefónica Deutschland completed the acquisition of E-Plus, following its execution of a capital increase intended to fund such acquisition. Telefónica maintains a stake of 62.1% in Telefónica Deutschland, which now includes 100% of the E-Plus Group, while the Dutch company Koninklijke KPN N.V. holds a 20.5% stake, and the rest is free float.

- On July 4, 2014, Telefónica de Contenidos acquired 22% of the share capital of DTS owned by Mediaset España Comunicación, S.A. ("Mediaset") for consideration of 295 million euros.

A payment of 30 million euros has been agreed as consideration for the waiver of Mediaset's pre-emptive rights relating the stake held by PRISA in DTS. Pursuant to the agreement, Mediaset will receive (i) 10 million euros in the event that Telefónica de Contenidos closes the acquisition of the 56% stake of DTS held by PRISA and, in that case, (ii) up to 30 million euros depending on the evolution of the Pay-TV customers in Spain of the Telefónica Group during the four years following the closing of such acquisition.

- On July 7, 2014, Telefónica reached an agreement with Reti Televisive Italiane S.p.A. ("RTI") for the acquisition by Telefónica of an 11.11% stake of the capital of a newly created company, which will consolidate the Pay-TV business of the Mediaset Group in Italy, currently commercialized under the name of "Mediaset Premium". The purchase price is 100 million euros.
- On July 15, 2014, after obtaining the corresponding regulatory authorizations, Telefónica concluded the 100% sale of its stake in Telefónica Ireland, Ltd. to the Hutchison Whampoa Group. The value of the sale amounted to 850 million euros, including an initial cash consideration of 780 million euros received at the closing of the transaction, and an additional deferred payment of 70 million euros, based on the completion of agreed financial objectives.
- On September 19, 2014, Telefónica, S.A. signed an agreement with Vivendi S.A. for the acquisition by Telefónica Brasil, S.A. of Global Village Telecom, S.A. and its holding company GVT Participações, S.A. (jointly "GVT") for a cash consideration of 4,663 million euros, and a payment in shares representing 12.00% of the share capital of Telefónica Brasil, S.A., after its combination with GVT.

As part of the agreement, Vivendi S.A. will acquire from Telefónica 1,110 million ordinary shares in Telecom Italia currently representing 8.3% of Telecom Italia's voting share capital (equivalent to 5.7% of its total share capital), in exchange for 4.5% of Vivendi, S.A.'s capital in Telefónica Brasil, S.A., after its combination with GVT (which represents all of the voting shares and 0.7% of the preferred shares to be received by Vivendi S.A. under the agreement referred to above).

The cash payment for this transaction is expected to be financed via a capital increase by Telefónica Brasil S.A., which Telefónica S.A. intends to subscribe in proportion to its current stake in Telefónica Brasil, S.A. and intends to fund, in turn, via a capital increase.

The final closing of the operation is subject to obtaining the relevant regulatory authorizations (including telecommunication and anti-trust approval). On December 22, 2014, ANATEL approved the acquisition of GVT, although the resolution about the acquisition by Vivendi, S.A. of the 1,110 million of ordinary shares of Telecom Italia is still pending. As of the date of this Annual Report, CADE continues to analyze the process.

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- On September 30, 2014, Telefónica Brasil, S.A. was granted a national block of 2x10 MHz, in the 700 MHz band spectrum auction, called by ANATEL, for the minimum amount reserved to that block, equivalent to 1,927,964,770 reais (approximately 619 million euros).

With this acquisition, Telefónica Brasil, S.A. has reached its goal of ensuring the necessary spectrum for its medium- and long-term expansion of the 4G service in order to meet the growing demand for mobile access to high-speed Internet.

- On October 10, 2014, the Executive Commission of Telefónica's Board of Directors agreed that, at the Executive Commission scheduled for November 14, 2014, the appropriate corporate resolutions to carry out the execution of a free-of-charge capital increase related to shareholder compensation by means of a scrip dividend ("Telefónica's Flexible Dividend"), approved by the Annual General Shareholder's Meeting held on May 30, 2014, should be adopted. On November 14, 2014, the Executive Commission adopted the implementation of such capital increase. As a result, the last five trading sessions prior to November 14, 2014 were considered to determine the market price applicable to the free-of-charge allotment rights purchase price setting formula and to the provisional number of shares to issue formula.
- The free-of-charge allotment rights derived from the capital increase were allotted to Telefónica shareholders appearing as such in the book-entry records of Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A.U. (Iberclear), at 11:59 p.m. Madrid time, on November 18, 2014 (the day of publication of the capital increase notice in the Official Commercial Registry Gazette (Boletín Oficial del Registro Mercantil)).
- On October 27, 2014, following a report of the Nominating, Compensation and Corporate Governance Committee, the Board of Directors of Telefónica approved, with regard to the first cycle (2014-2017) of the long-term incentive plan (which consists in the granting of shares of Telefónica to Telefónica Group executives (including executive directors of Telefónica) as approved by the Annual General Shareholders Meeting held on May 30, 2014, (which determined the maximum possible number of shares to be received by the executive directors of Telefónica at the end of the first cycle of the plan)), the amount of theoretical shares to be assigned to the other executives, and the maximum possible number of shares to be received by them, in the event of fulfilment of the relevant co-investment requirement, and of the achievement of the maximum total shareholder return (TSR) established in the plan.
- On November 10, 2014, Telefónica, through its 100% subsidiary, Telefónica Internacional, S.A.U., sold 597,844,100 shares of China Unicom (Hong Kong) Limited ("China Unicom") as further described under "—Strategic Partnerships—China United Network Communications Group Co., Ltd. (China Unicom)", below.
- On December 9, 2014, the Company announced that, on December 3, 2014, the free-of-charge allotment rights trading period for the free-of-charge capital increase related to Telefónica's Flexible Dividend had ended. The holders of 15.8% of the free-of-charge allotment rights accepted the purchase commitment assumed by Telefónica, S.A. The gross amount paid by Telefónica, S.A. for these rights amounted to 241,542,822.19 euros. The company waived the rights thus acquired, which were amortized.

The holders of 84.2% of the free-of-charge allotment rights were entitled, therefore, to receive new shares of Telefónica, S.A. Nevertheless, the Company waived the free-of-charge allotment rights that corresponded to its treasury shares at the record date (November 18, 2014). Therefore, the final number of ordinary shares with a nominal value of one (1) euro issued in the capital increase was 106,179,744 (2.3% of the Company's share capital as of that date), totaling 106,179,744 euros. As a result, the share capital of Telefónica, S.A. after the capital increase, as registered on December 9, 2014 with the Commercial Registry of Madrid, was 4,657,204,330 euros (4,657,204,330

shares).

The new shares were admitted to listing on the Spanish Stock Exchanges in December 2014 and trading on the Spanish Automated Quotation System began on Friday, December 12, 2014. The new shares were thereafter admitted to listing on the stock exchanges of London, Buenos Aires and Lima.

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Business areas

On February 26, 2014, the Board of Directors of Telefónica, S.A. approved the implementation of a new organizational structure focused on clients and which incorporates the digital offering as the main focus of commercial policies. The structure gives greater visibility to local operators, bringing them closer to the corporate decision-making center, simplifying the Group's global structure and strengthening the cross-cutting areas to improve flexibility and agility in decision making.

Due to the implementation of this new organizational structure, from the beginning of 2014, the new organizational structure has been composed of Telefónica Spain, Telefónica Brazil, Telefónica Germany, Telefónica United Kingdom and Telefónica Hispanoamérica (comprised of our consolidated subsidiaries in Argentina, Chile, Peru, Colombia, Mexico, Venezuela & Central America, Ecuador and Uruguay). All business that is not specifically included in these new segments is part of "Other companies and eliminations". As a result, the Group's segment results have been revised for the 2013 and 2012 fiscal years to reflect this new organization. Because this is an intragroup change, Telefónica's consolidated results for 2013 and 2012 are not affected.

Additionally, as a result of management integrations undertaken in Peru, Argentina and Chile, the revenue breakdown has been reclassified, allocating "inter-company" eliminations within fixed and mobile businesses.

Segment reporting takes into account the impact of the purchase price allocation to assets acquired and the liabilities assumed from the companies included in each segment. The assets and liabilities presented in each segment are those managed by the heads of each segment, irrespective of their legal structure.

The Group manages borrowing activities and taxes centrally. Therefore, it does not disclose the related assets, liabilities, revenue and expenses by reportable segments. In addition, revenue and expenses arising from intra-group invoicing for the use of the trademark and management services have been eliminated from the operating results of each Group segment. These adjustments have no impact on the Group's consolidated results.

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The following chart shows the organizational structure of the principal subsidiaries of the Telefónica Group at December 31, 2014, including their jurisdictions of incorporation and our ownership interest. For further detail, see Exhibit 8.1 to this Annual Report.

- (1) Ownership in Telefónica Móviles España, S.A.U. is held directly by Telefónica, S.A.
- (2) Representing a 91.76% voting interest.
- (3) Ownership in Telefónica International Wholesale Services, S.L. is held 92.51% by Telefónica, S.A. and 7.49% by Telefónica Datacorp, S.A.U.
- (4) Companies held indirectly.
- (5) Ownership in TIWS II is held directly by Telefónica, S.A.

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Telefónica, S.A., the parent company of the Telefónica 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 Group’s portfolio of businesses;
- foster cohesion within the Group; and
- foster synergies among the Group’s subsidiaries.

Our principal executive offices are located at Distrito Telefónica, Ronda de la Comunicación, s/n, 28050 Madrid, Spain, and our registered offices are located at Gran Vía, 28, 28013 Madrid, Spain. Our telephone number is +34 900 111 004.

Capital Expenditures and Divestitures

Our principal capital expenditures during the three years ended December 31, 2014, consisted of additions to property, plant and equipment and additions to intangible assets, including spectrum. In 2014, 2013 and 2012, we made capital expenditures of 9,448 million euros, 9,395 million euros and 9,458 million euros, respectively.

Year ended December 31, 2014

Capital expenditures in 2014 increased 0.6% compared to 2013. Capital expenditures in 2014 included the cost of spectrum mainly in Brazil, Argentina, Venezuela, Colombia and Panama, amounting to 1,294 million euros.

Investment by Telefónica Spain in 2014 amounted to 1,732 million euros. Fiber optic was rolled out rapidly, and by year-end 2014 Telefónica Spain had created more than 10 million “fiber-to-the-house” (“FTTH”) facilities in Spain, increasing its investments in LTE networks. Investment by Telefónica United Kingdom in 2014 amounted to 755 million euros, mainly due to greater LTE coverage – an estimated 58% of the outdoor population - and a network capacity ramped up to cope with denser 3G and 4G traffic. Investment at Telefónica Germany in 2014 amounted to 849 million euros, focusing on its LTE roll-out strategy, securing 61% coverage in 2014. Investment at Telefónica Brazil in 2014 amounted to 2,933 million euros, mainly due to the fact that the mobile segment featured a continuation of LTE roll-outs in 2014, improving network capacity, systems and applications. Investment in the fixed-line network was used to expand roll-out of fiber optic, larger volumes of IPTV customers and corporate projects. Investment by Telefónica Hispanoamérica in 2014 amounted to 2,842 million euros mainly focused on LTE roll-outs in practically all operations in the region. Investment was also allocated to the densification of the 3G network, optimization of fixed-mobile convergence systems, the continuation of ultra broad band (UBB) roll-out for fixed broadband by speed upgrades and network digitalization, television and digital initiatives.

Year ended December 31, 2013

Capital expenditures in 2013 were in line with 2012. Capital expenditures in 2013 included the cost of spectrum mainly in United Kingdom, Brazil, Peru, Colombia and Spain, amounting to 1,224 million euros.

Investment by Telefónica Spain in 2013 amounted to 1,529 million euros, reflecting a high level of investment efficiency, as a result of the improvements in quality indexes, the reduction of complaints and enhanced efficiency in IT. At the end of the year, there was an acceleration in the rollout of fiber optic, and a boost of LTE deployment. Investment by Telefónica United Kingdom amounted to 1,385 million euros mainly due to spectrum investment (719 million euros). Investment by Telefónica Germany amounted to 666 million euros, focusing its efforts on network quality while accelerating investment in LTE network deployment. Investment by Telefónica Brazil amounted to 2,127 million euros mainly due to the expansion and improvement of the mobile networks, both 3G and 4G, as well as the rollout of its fiber network. Investment by Telefónica Hispanoamérica in 2013 amounted to 3,118 million euros, mainly in the mobile

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business and centered primarily on overlay projects and expansion of the coverage, quality and density of 3G networks, as well as the minimum roll-out of LTE (Colombia and Chile), the development of platforms to underpin new VASs, and the optimization of infrastructure and systems developments focusing on self-management. In the fixed line business, funds continued to be earmarked for rolling out UBB through speed upgrades in ADSL, fiber (FTTx) and VDSL in Argentina and Chile, as well as the installation of fixed-mobile convergence systems (Colombia, Chile and Peru).

Year ended December 31, 2012

Capital expenditures in 2012 declined 7.5% compared to 2011. Capital expenditures in 2012 included the cost of spectrum in Brazil, Nicaragua, Chile, Venezuela and Ireland, amounting to 586 million euros. In Telefónica Spain, investments amounted to 1,692 million euros, mainly focused on improvements in quality levels and reduction in the level of complaints. Investment by Telefónica United Kingdom amounted to 748 million euros focusing on increasing its 3G coverage and capacity. Investment by Telefónica Germany amounted to 609 million euros focusing on the development of the LTE network and the increase of capacity in the 3G network. Investment by Telefónica Brazil amounted to 2,444 million euros mainly driven by mobile network expansion. Investments in Telefónica Hispanoamérica amounted to 2,988 million euros focusing on mobile business (mainly with overlay projects, and coverage expansion and enhancing the quality of its 3G networks), as well as on development of new platforms and evolving the existing ones to support new value-added services. In the fixed line business significant investments were made in ultra broad band and speed upgrades in DSL, FTTx and VDSL in Argentina and Chile. In addition, Telefónica Digital made investments throughout 2012 in TV business including new HD channels introduction and commercial launches of OTT services and content delivery network in line with Telefónica Digital initiatives.

Financial Investments and Divestitures

Our principal financial investment in 2014 was the acquisition of E-Plus, which was completed on October 1, 2014, through our subsidiary Telefónica Deutschland for a total purchase price of 7,463 million euros. Our principal divestures in 2014 were the completion of the sales of Telefónica Czech Republic, a.s. on January 28, 2014, Telefónica Ireland, Ltd on July 2, 2014, and the sale of shares representing approximately 2.5% of the share capital of China Unicom for approximately 687 million euros.

There were no significant financial investments in 2013. Our principal divestures in 2013 were the sale of 40.00% of our investment, through Telefónica Centroamérica de Inversiones, S.L., in Guatemala, Salvador, Nicaragua and Panama for 500 million U.S. dollars (equivalent to 377 million euros on the date of execution of the sale) with no impact in the results of the Group given our continued control over the company after the transaction; the agreement to sell 65.9% of our investment in Telefónica Czech Republic, a.s. for 306 Czech crown per share (approximately 2,467 million euros at the date of the agreement), resulting in a capital loss of 176 million euros and the agreement to sell our stake in Telefónica Ireland, Ltd for 850 million euros.

There were no significant financial investments in 2012. Our principal divestures in 2012 were the sale in July 2012 of shares representing 4.56% of the share capital of China Unicom for 10,748 million Hong Kong dollars (approximately 1,142 million euros at that date), resulting in a loss of 97 million euros; the sale of 23.17% of Telefónica Germany Holding, A.G. for 1,499 million euros, with no impact in the results of the Group given we maintain the control over the company after this transaction, and the sale of Atento for 1,051 million euros, including a vendor loan of 110 million euros as well as certain deferred payments for 110 million euros, resulting in a capital gain of 61 million euros.

Public Takeover Offers

Not applicable

Recent Developments

The principal events that have occurred since December 31, 2014, are set forth below:

- On January 23, 2015 Telefónica and Hutchison Whampoa Group agreed to enter into exclusive negotiations for the potential acquisition by the latter of Telefonica UK limited (Telefónica's business in the UK ("O2 UK")) for an indicative price in cash (firm value) of 10.25 billion pounds (approximately 13.5 billion euros); composed of (i) an initial amount of 9.25 billion pounds (approximately 12.2 billion euros) which would be paid at closing and (ii) an additional deferred payment of 1.0 billion pounds (approximately 1.3 billion euros) to be paid once the cumulative cash flow of the combined company in the United Kingdom has reached an agreed threshold.

The exclusivity period will last a specified period, allowing Telefónica and Hutchison Whampoa Group to negotiate definitive agreements, while Hutchison Whampoa Group completes its due diligence.

For information related to our significant financing transactions completed in 2014 and through the date of this Annual Report, see "Item 5. Operating and Financial Review and Prospects—Liquidity and Capital Resources—Anticipated Sources of Liquidity".

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B. Business Overview

The Telefónica Group is one of the world's leading mobile and fixed communications services providers. Its strategy is to become a leader in the new digital world and transform the possibilities it brings into reality.

Telefonica's aim is to reinforce its position as an active player in the digital world capable of seizing all the opportunities afforded by its global scale and its industrial and strategic alliances.

On February 26, 2014, the Board of Directors of Telefónica, S.A. approved the implementation of a new organizational structure focused on clients and which incorporates the digital offering as the main focus of commercial policies. The structure gives greater visibility to local operators, bringing them closer to the corporate decision-making center, simplifying the Group's global structure and strengthening cross-cutting areas to improve flexibility and agility in decision making.

From January 1, 2014 on, and due to the implementation of this new organizational structure, the Group's structure is composed of Telefónica Spain, Telefónica United Kingdom, Telefónica Germany, Telefónica Brazil and Telefónica Hispanoamérica (comprised of our consolidated subsidiaries in Argentina, Chile, Peru, Colombia, Mexico, Venezuela & Central America, Ecuador and Uruguay). These segments include the information related to wireline, wireless, DSL, TV, and other digital services provided in each country or countries. Any services not specifically included in these new segments are part of "Other companies and eliminations".

The Telefónica Group's strategy aims to:

- Improve the customer experience in order to continue increasing accesses.
- Lead growth:
 - o Drive forward the penetration of smart phones in all markets in order to raise the growth rate of mobile data by monetizing their increasingly widespread use.
 - o Defend our competitive positioning, and leverage our customer knowledge.
 - o Develop the growth opportunities that have arisen in an increasingly digital context, such as media, financial services, cloud, security, advertising, M2M, e-Health, etc.
 - o Capture the opportunity in the business segment.
- Continue working on the transformation of the Group's operating model:
 - o Increase the modernization of networks in markets where we operate through technological advances and the acquisition of spectrum.
 - o Maximize the benefits of economies of scale to increase efficiency.
 - o Simplify the operative model.
 - o Reduce legacy cost, especially legacy network costs.

In addition, Telefónica maintains an industrial alliance with China Unicom. Furthermore, in order to potentially unlock the value of Telefónica's scale, the "Partners" program was created in 2011, and now includes five operators (Bouygues, Etisalat, Sunrise, Megafon and O2 CZ). The Telefónica Partners Program is an initiative that makes available to selected operators and under commercial terms a host of services that allows partners to leverage on Telefónica's scale and to cooperate on key business topics (digital services, roaming, services to multinationals, procurement, devices, etc.).

Moreover Telefónica's portfolio was restructured in 2014 through the acquisition of E-Plus by Telefónica Deutschland to form the leading operator in Germany in terms of number of wireless customers. Telefónica is also in the process of acquiring GVT through Telefónica Brazil, subject to regulatory approval, and negotiating the sale of its business in the United Kingdom.

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Other information

Non-controlling interests can be divided into two groups. Firstly, subsidiaries listed in a regulated market, such as Telefónica Brasil or Telefónica Deutschland, where minority shareholdings are widely dispersed and in respect of which Telefónica protects minority interests by complying with the regulations of the related market. Secondly, subsidiaries with a main minority shareholder, with whom agreements are entered into in order to guarantee the protection of such shareholder's rights and, in certain cases (such as Colombia Telecomunicaciones) where there are also specific commitments resulting from corporate transactions (see Note 21.b of the Consolidated Financial Statements).

The Telefónica Group's Spanish companies have adapted their internal processes and payment schedules to the provisions of Law 15/2010 (amended by Law 31/2014) and Royal Decree-Law 4/2013, amending Law 3/2004, which establishes measures against late payment in commercial transactions. Engagement conditions with commercial suppliers in 2014 included payment periods of up to 60 days, according to the terms agreed between the parties. For efficiency purposes, the Telefónica Group's companies in Spain have agreed payment schedules with suppliers, whereby payments are made on set days of each month. Payments to Spanish suppliers in 2014 and 2013 surpassing the established legal limit were the result of circumstances or incidents beyond the payment policies, mainly the delay in issuing invoices (legal obligation of the supplier), the closing of agreements with suppliers over the delivery of goods or the rendering of services, or occasional processing issues. According to such criteria, the average payment period to suppliers of the Telefónica Group's companies in Spain in 2014, according to our best estimates, amounted to 51 days.

The Company has a governance system, which applies to Telefónica's entire structure. Pursuant to the Company's commitment to its shareholders, the Board of Directors, supported by its Committees, manages the Company's business in accordance with the corporate governance rules laid down primarily in the Corporate By-laws, in the Regulation of the General Shareholders' Meeting, and in the Regulation of the Board of Directors. See "Item 16G. Corporate Governance – Significant Differences in Corporate Governance Practices – Corporate governance guidelines."

Telefónica's Board of Directors consists of 18 directors and is responsible for overseeing and controlling the Company's activity. It has sole powers regarding general strategy and policies on corporate governance, corporate social responsibility, remuneration of the Board and senior management, shareholder remuneration, and strategic investments.

In order to strengthen the corporate governance of the Company, the Board of Directors of Telefónica, S.A. has eight committees (including the Executive Commission) which are charged with examining and overseeing areas of particular relevance. Pursuant to its regulation, the Board also confers responsibility for day-to-day management of the businesses to Telefónica's executive bodies (primarily through the Executive Committee) and management team.

Financial Results

2014 highlights

The Group's total accesses rose 5.5% during 2014 to 341 million at December 31, 2014, including the additional accesses it gained following the purchase of the E-Plus Group in Germany. Excluding the E-Plus Group accesses from 2014 results and accesses from Telefónica Czech Republic and Telefónica Ireland from 2013 results, the increase would have been 2.0%. There was high commercial activity focus on high value customers which resulted in the growth of the contract mobile segment ("smartphones" and LTE), fiber and Pay-TV. The volume of fiber accesses also grew, reaching 1.8 million at December 31, 2014. Notably, accesses in Telefónica Hispanoamérica (39% of the

Group's total), increased by 2.5%, and accesses in Telefónica Brazil (28% of the Group's total) increased by 3.0% in 2014.

The evolution of foreign exchange rates impacted negatively our 2014 consolidated financial results, in particular the depreciation of the Argentine peso, Brazilian real and the implicit depreciation of the Venezuelan bolivar.

In its 2014 consolidated financial statements, Telefónica used the exchange rate of the Venezuelan bolívar set at the previously denominated SICAD II, (set at 49.988 Venezuelan bolívar fuerte per U.S. dollar in the last auction), for the purpose of translating the transactions, cash flows and balances related to the investments in Venezuela. The Company has decided to take such exchange rate as a reference, as it considers it to be the most representative among the available exchange rates as of such date, for the monetary translation of the accounting figures of cash flows and balances.

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Accordingly, we estimate that the foreign exchange rate effect and the hyperinflations in Venezuela reduce our revenues and OIBDA in 2014 by 12.1 percentage points and 13.1 percentage points, respectively.

Revenues totaled 50,377 million euros in 2014, down 11.7% compared to 2013, mainly affected by exchange rate differences and the effect of hyperinflation in Venezuela, which reduced year-on-year growth by 12.1 percentage points. Additionally, this decrease was also affected by changes in the composition of the Group (-2.1 p.p.), in particular the sales of Telefónica Czech Republic and Telefónica Ireland and by the acquisition of the E-Plus Group. Excluding these impacts, revenues would have increased by 2.6% year-on-year mainly due to the performance of Telefónica Hispanoamérica, where revenues from mobile data and digital services increased. In order to make comparisons excluding the impact of changes to the scope of consolidation caused by the sales of Telefónica Czech Republic and Telefónica Ireland and the acquisition of the E-Plus Group in 2014, we have excluded the contribution of such entities to revenues in both 2013 and 2014.

The structure of revenues reflects the Company's business diversification. Despite the impact of exchange rates mentioned above, the segments that were the largest contributors to our revenues in 2014 were Telefónica Hispanoamérica, representing 26.1% (-3.4 p.p. compared to 2013), Telefónica Spain, representing 23.9% (+1.2 p.p. compared to 2013), Telefónica Brazil, representing 22.3% (+0.9 p.p. compared to 2013), Telefónica United Kingdom, representing 14.0% (+2.3 p.p. compared to 2013) and Telefónica Germany, representing 11.0% (+2.3 p.p. compared to 2013).

OIBDA reached 15,515 million euros for the year ended December 31, 2014, a fall of 18.7%, mainly due to:

- the effect of exchange rates and hyperinflation in Venezuela (-13.1 p.p.);
- changes to the scope of consolidation (-3.5 p.p.) as a result of the exclusion of Telefónica Czech Republic and Telefónica Ireland, and the inclusion of the E-Plus Group;
- recognition in 2014 of expenditure mainly on the global restructuring program, in accordance with the simplification initiatives that the Group is implementing to meet its targets, totaling 652 million euros (670 million euros excluding exchange rate effects), accounting for a reduction of 3.5 percentage points;
- a higher sale value of non-strategic towers in 2014 compared to 2013 (196 million euros in 2014, mainly in Telefónica Spain, in the amount of 191 million euros, compared to 111 million euros in 2013 accounted for mainly by Telefónica Spain (70 million euros), Telefónica Brazil (29 million euros) and Telefónica Hispanoamérica (11 million euros, in Mexico, Chile and Colombia). This effect accounts for an addition of 0.5 percentage points of OIBDA growth; and
- the impact of the sale of companies in 2013, chiefly the sale agreements for Telefónica Ireland (16 million euros) and Telefónica Czech Republic (176 million euros) (+1 p.p.), and the sale of Hispasat (21 million euros; -0.1 p.p).

Excluding these effects, OIBDA would have increased by 0.2% in 2014 compared to 2013. The OIBDA margin was 30.8% for 2014, down 2.6 percentage points compared to 2013 in reported terms.

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The below table shows the evolution of accesses over the past three years.

ACSESSES

	2012	2013	2014	%Var 12/13	%Var 13/14
Thousands of accesses					
Fixed telephony accesses (1) (2) (3)	40,002.6	39,338.5	36,830.0	(1.7%)	(6.4%)
Internet and data accesses	19,402.6	19,102.0	18,151.7	(1.5%)	(5.0%)
Narrowband	653.2	510.8	373.1	(21.8%)	(27.0%)
Broadband (4)	18,596.2	18,447.8	17,668.5	(0.8%)	(4.2%)
Other (5)	153.1	143.4	110.1	(6.3%)	(23.3%)
Mobile accesses	247,346.9	254,717.2	274,458.0	3.0%	7.8%
Prepay (6) (7)	165,821.9	165,557.0	175,720.4	(0.2%)	6.1%
Contract	81,525.0	89,160.3	98,737.6	9.4%	10.7%
Pay-TV (8)	3,336.2	3,602.2	5,087.2	8.0%	41.2%
Unbundled loops	3,308.8	3,833.4	4,087.3	15.9%	6.6%
Shared ULL	183.5	130.6	94.1	(28.9%)	(27.9%)
Full ULL	3,125.3	3,702.9	3,993.3	18.5%	7.8%
Wholesale ADSL	845.4	866.9	750.1	2.5%	(13.5%)
Other	1,577.1	1,658.2	1,684.1	5.1%	1.6%
Final Clients Accesses	310,088.3	316,759.9	334,526.9	2.2%	5.6%
Wholesale Accesses	5,731.3	6,358.5	6,521.6	10.9%	2.6%
Total Accesses	315,819.6	323,118.4	341,048.5	2.3%	5.5%

Notes:

- Telefónica Czech Republic accesses are de-consolidated from the first quarter of 2014, Telefónica Ireland accesses are de-consolidated from the third quarter of 2014 and E-Plus accesses are consolidated from the fourth quarter of 2014.

- Telefónica Spain mobile accesses include since 2013 the accesses of Tuenti; in 2012 they have been restated with the same criteria.

(1) RTB (includes public use telephony) x1; Basic Access RDSI x1; Primarily Access RDSI; Digital Access 2/6 x30. Includes internal use. Includes "fixed wireless" voice accesses. Includes Voice over IP and Naked DSL.

(2) In the first quarter of 2014, 45 thousands inactive "fixed wireless" accesses were disconnected in Mexico.

(3) In the second quarter of 2014, fixed clients includes 50 thousands additional fixed wireless clients in Peru.

(4) Includes DSL, satellite, optic fiber, cable modem and broadband circuits.

(5) Rest of retail non broadband circuits.

(6) In the first quarter of 2014, 1.9 million inactive accesses were disconnected in Mexico.

(7) In the fourth quarter 2014, 1.8 million inactive accesses were disconnected in Central America.

(8) In the second quarter of 2014, Pay-TV accesses includes 131 thousand "TV Mini" clients in Spain.

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The chart below shows the evolution of accesses by region over the past three years.

Accesses by region (millions)

The Group's strategy is based on capturing growth in its markets, especially on attracting high-value customers.

Mobile accesses totaled 274.5 million in 2014, increasing 7.8% compared to 2013 (a 2.2% increase excluding accesses from the E-Plus Group in 2014 and from Telefónica Czech Republic and in Telefónica Ireland in 2013), driven by the E-Plus Group acquisition and strong growth in the contract segment (+10.7%), which represented 36% of total mobile accesses in 2014 (+1 p.p. year-on-year). Notably, Telefónica Spain has increased its contract segment in 2014 in 77 thousand new accesses (excluding the impact of the disconnection of 569 thousand inactive M2M accesses in the first three months of 2014), a positive number for the first time since 2011.

Smartphone accesses maintained a strong growth rate (up 39.0% at December 31, 2014 compared to December 31, 2013), totaling 90.4 million accesses and reaching a penetration rate over total accesses of 35% (+8 p.p. year-on-year), reflecting the Company's strategic focus on the growth of its data services.

Fixed broadband accesses stood at 17.7 million at December 31, 2014, a decrease of 4.2% year-on-year (+0.8% excluding accesses from Telefónica Czech Republic in 2013). Fiber accesses stood at 1.8 million at December 31, 2014 (a 111.8% increase compared to December 31, 2013).

TV accesses totaled 5.1 million at December 31, 2014, up 41.2% year-on-year (47.6% excluding accesses from Telefónica Czech Republic in 2013). Net adds (new additions to the customer base), excluding accesses from Telefónica Czech Republic, reached 1.6 million in the year.

Telefónica's customer base includes the consumer and business segments, and therefore is not affected by customer concentration risk.

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2014 Consolidated results

The below table shows our consolidated results of operations for the past three years.

	Year ended December 31						Percent Change			
	2012		2013		2014		2013 vs 2012		2014 vs 2013	
	Total revenues	% of Total revenues	Total revenues	% of Total revenues	Total revenues	% of Total revenues	Total	%	Total	%
Millions of Euros										
Revenues	62,356	100.0%	57,061	100.0%	50,377	100.0%	(5,295)	(8.5%)	(6,684)	(11.7%)
Other income	2,323	3.7%	1,693	3.0%	1,707	(3.4%)	(630)	(27.1%)	14	0.9%
Supplies	(18,074)	(29.0%)	(17,041)	(29.9%)	(15,182)	(30.1%)	1,033	(5.7%)	1,859	(10.9%)
Personnel expenses	(8,569)	(13.7%)	(7,208)	(12.6%)	(7,098)	(14.1%)	1,361	(15.9%)	110	(1.5%)
Other expenses	(16,805)	(27.0%)	(15,428)	(27.0%)	(14,289)	(28.4%)	1,377	(8.2%)	1,139	(7.4%)
Operating income before depreciation and amortization (OIBDA)	21,231	34.0%	19,077	33.4%	15,515	30.8%	(2,154)	(10.1%)	(3,562)	(18.7%)
Depreciation and amortization	(10,433)	(16.7%)	(9,627)	(16.9%)	(8,548)	(17.0%)	806	(7.7%)	1,079	(11.2%)
Operating income	10,798	17.3%	9,450	16.6%	6,967	13.8%	(1,348)	(12.5%)	(2,483)	(26.3%)
Share of loss of investments accounted for by the equity method	(1,275)	(2.0%)	(304)	(0.5%)	(510)	(1.0%)	971	(76.2%)	(206)	68.2%
Net financial expense	(3,659)	(5.9%)	(2,866)	(5.0%)	(2,822)	(5.6%)	793	(21.7%)	44	(1.6%)
Corporate income tax	(1,461)	(2.3%)	(1,311)	(2.3%)	(383)	(0.8%)	150	(10.3%)	928	(70.8%)
Profit for the year	4,403	7.1%	4,969	8.7%	3,252	6.5%	566	12.9%	(1,717)	(34.6%)
Non-controlling interests	(475)	(0.8%)	(376)	(0.7%)	(251)	(0.5%)	99	(20.8%)	125	(33.2%)
Profit for the year attributable to equity holders of the parent	3,928	6.3%	4,593	8.0%	3,001	6.0%	665	16.9%	(1,592)	(34.7%)

Year ended December 31, 2014 compared with year ended December 31, 2013

The evolution of foreign exchange rates impacted negatively in 2014 financial results, in particular the depreciation of the Argentine peso, Brazilian real and the implicit depreciation of the Venezuelan bolívar.

In the 2014 consolidated financial statements, Telefónica will use the exchange rate of the Venezuelan bolívar set at the previously denominated SICAD II (set at 49.988 Venezuelan bolívar fuerte per dollar in the last auction), for the purpose of translating the transactions, cash flows and balances related to the investments in Venezuela. The Company has decided to take such exchange rate as a reference, as it considers it to be the most representative among the available exchange rates as of such date, for the monetary translation of the accounting figures of cash flows and balances.

Accordingly, we estimate that the foreign exchange rate affect and hyperinflation in Venezuela, reduce revenue and OIBDA in 2014 by 12.1 percentage points and 13.1 percentage points, respectively.

Year-on-year comparisons of the Group's earnings have also been affected by the acquisition and consolidation of the results of the E-Plus Group since October 1, 2014 and the sale and deconsolidation of the results of Telefónica Czech Republic (deconsolidated as of January, 2014) and Telefónica Ireland (deconsolidated as of July, 2014). Overall, these changes to the scope of consolidation explain 2.1 percentage points of the year-on-year decrease in revenues and 3.5 percentage points of the year-on-year decrease in OIBDA.

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Revenues totaled 50,377 million euros in 2014, decreasing 11.7% compared to 2013, mainly affected by exchange rate differences and the effect of hyperinflation in Venezuela, which caused a 12.1 percentage points reduction in year-on-year growth. Additionally, revenues were also affected by changes to the scope of consolidation (-2.1 p.p.), chiefly the sales of Telefónica Czech Republic and Telefónica Ireland and the acquisition of E-Plus. Excluding these impacts, revenues would have increased by 2.6% year-on-year mainly due to the performance of Telefónica Hispanoamérica, where revenues from mobile data and digital services increased. In order to make comparisons excluding the impact of changes to the scope of consolidation caused by the sales of Telefónica Czech Republic and Telefónica Ireland and the acquisition of the E-Plus Group, we have excluded the contribution of such entities to revenues in both 2013 and 2014.

The structure of revenues reflects Telefónica's business diversification. Despite the impact of exchange rates, as mentioned above, Telefónica Hispanoamérica was the largest contributor to our revenues in 2014, representing 26.1% (-3.4 p.p. compared to 2013). The other segments showed a positive evolution compared to 2013: Telefónica Spain, representing 23.9% (+1.2 p.p. compared to 2013), Telefónica Brazil, representing 22.3% (+0.9 p.p. compared to 2013), Telefónica United Kingdom, representing 14.0% (+2.3 p.p. compared to 2013) and Telefónica Germany, representing 11.0% (+2.3 p.p. compared to 2013).

Mobile data revenues fell by 5.2% in reported terms affected mainly by exchange rate differences and the effect of hyperinflation in Venezuela. Excluding exchange rate differences and the effect of hyperinflation in Venezuela (which accounted for 14.3 p.p. of the year-on-year fall) and changes to the scope of consolidation (which accounted for 0.5 p.p. of the year-on-year fall), revenues from mobile data would have increased by 9.9%. Mobile data revenues accounted for 41% of mobile service revenues in such year, up 3.1 percentage points compared to 2013. Revenue from non-SMS data showed a solid growth of 6.7% in reported terms (+23.9% excluding the impact of exchange rate differences and the effect of hyperinflation in Venezuela (+16.8 p.p.) and changes to the scope of consolidation (-0.1 p.p.)), and accounted for 73% of total data revenue during the year in reported terms (+8.1 p.p. year-on-year).

Other income in 2014 mainly included own work capitalized in our fixed assets, profit from the sale of other assets, and the sale of non-strategic towers of Telefónica Spain, Telefónica Brazil and Telefónica Hispanoamérica.

In 2014, other income increased mainly due to the sale of non-strategic towers (with an impact on OIBDA of 196 million euros), primarily in Telefónica Spain (191 million euros), extraordinary sales of real estate in Telefónica Spain (41 million euros) and recognition of capital gains on the sale of assets belonging to the fixed business in Telefónica United Kingdom once the conditions stipulated in the relevant sales agreement had been met (49 million euros).

Other income in 2013 consisted mainly of the sale of non-strategic towers of Telefónica Brazil, Telefónica Hispanoamérica and Telefónica Spain (113 million euros in other income and 111 million euros in OIBDA), capital gains on the sale of assets belonging to the fixed business of Telefónica United Kingdom (83 million euros) and capital gains on the assets sale of Telefónica Germany (76 million euros), capital gains on the sale of Hispasat (21 million euros).

Total expenses: in 2014 (which include supply costs, personnel costs and other expenses (principally external services and taxes), amounting to 36,569 million euros, down by 7.8% compared to 2013, mainly due to:

- exchange rate differences and the effect of hyperinflation in Venezuela (-11.3 p.p.);
- changes to the scope of consolidation (-1.4 p.p.) caused by the sales of Telefónica Czech Republic and Telefónica Ireland and the acquisition of the E-Plus Group;

- impact of the sale agreements of Telefónica Ireland and Telefónica Czech Republic (-0.5 p.p.) in 2013; and
- the recognition in 2014 of expenditures mainly on the global restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its targets, totaling 652 million euros (670 million euros excluding exchange rate effects), accounting for 1.7 percentage points.

Excluding these impacts, total expenses would have increased by 3.9% in 2014 compared to 2013, mainly due to higher commercial expenditures and outlays on networks and systems.

- Supplies amounted to 15,182 million euros in 2014, down 10.9% against 2013, mainly due to exchange rate differences and the effect of hyperinflation in Venezuela, which decreased supplies expenses by 8.6 percentage points. The year-on-year change was also affected by changes to the scope of consolidation (due to the sales of Telefónica Czech Republic and Telefónica Ireland and from the acquisition of the E-Plus Group, resulting in

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a 1.9 percentage points decrease. Excluding these effects, supplies expenses would have fallen by 0.5% as the result of lower mobile interconnection costs, which more than offset the higher equipment costs of handsets and TV content.

- Personnel expenses totaled 7,098 million euros in 2014, down 1.5% compared to 2013, mainly affected by exchange rate differences and the effect of hyperinflation in Venezuela, (-12.1 p.p.) and changes to the scope of consolidation (-2.4 p.p.) which were mostly offset by the expenditures on the global restructuring program, in accordance with the the simplification initiatives the Group is implementing to meet its targets (+8.1 p.p.). Excluding these impacts, personnel costs rose by 5.2% in 2014 compared to 2013 due to higher prices in some countries.

The average headcount in 2014 was 120,497 employees, down 7.2% compared to 2013 due mainly to the changes in the scope of consolidation (-2.2% excluding changes to the scope of consolidation).

- Other expenses amounted to 14,289 million euros in 2014, down 7.4% as compared to 2013 mainly caused by exchange rate differences and the effect of hyperinflation in Venezuela (-13.9 p.p.). The year-on-year variation was also affected by the impact of value adjustments in the sales of Telefónica Ireland and Telefónica Czech Republic (-1.2 p.p.), changes to the scope of consolidation by the sales of Telefónica Czech Republic and Telefónica Ireland and the acquisition of the E-Plus Group (-0.5 p.p.) and the recognition of integration costs in Telefónica Germany (+0.6 p.p.). Excluding these impacts, other expenses would have increased by 8.1% due to higher commercial costs, higher network costs produced by larger volumes of data traffic and greater outlays on modernization of the network.

OIBDA reached 15,515 million euros for the year ended December 31, 2014, a fall of 18.7%, mainly due to:

- the effect of exchange rates and hyperinflation in Venezuela (-13.1 p.p.);
- changes to the scope of consolidation (-3.5 p.p.) following the exclusion of Telefónica Czech Republic and Telefónica Ireland and the inclusion of the E-Plus Group;
- recognition in 2014 of expenditure mainly on the global restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its targets, totaling 652 million euros (670 million euros at the exchange rate used to calculate 2013 results), accounting a decrease of 3.5 percentage points;
- the impact of the sale of companies in 2013, chiefly the sale agreements for Telefónica Ireland (16 million euros) and Telefónica Czech Republic (176 million euros) (+1 p.p.), and the sale of Hispasat (21 million euros; -0.1 p.p.); and
- a higher sale value of non-strategic towers in 2014 compared to 2013 (196 million euros in 2014, mainly in Telefónica Spain (191 million euros), and 111 million euros in 2013, mainly in Telefónica Spain (70 million euros), Telefónica Brazil (29 million euros) and Telefónica Hispanoamérica (11 million euros, in Mexico, Chile and Colombia)). This effect accounts for 0.5 percentage points of OIBDA growth.

Excluding these effects, OIBDA in 2014 would have increased by 0.2% compared to 2013. The OIBDA margin was 30.8% for 2014, down 2.6 percentage points year-on-year in reported terms.

By region, Telefónica Spain contributed most to the Group's consolidated OIBDA, accounting for 36.6% of the total (+3.3 p.p. compared to 2013), Telefónica Hispanoamérica accounted for 26.2% (-2.8 p.p. compared to 2013), Telefónica Brazil accounted for 22.8% (+2.2 p.p. compared to 2013), Telefónica United Kingdom accounted for

11.2% (+2.7 p.p. compared to 2013) and Telefónica Germany accounted for 4.7% (-2.1 p.p. compared to 2013).

Depreciation and amortization amounted to 8,548 million euros in 2014, a decline of 11.2% compared to 2013, due to lower depreciation of fixed assets, mainly in Brazil. The total depreciation and amortization charges arising from purchase price allocation processes amounted to 708 million euros for the year (-17.3% year-on-year).

Operating income (OI) in 2014 totaled 6,967 million euros, down 26.3% compared to 2013, mainly affected by exchange rate differences and the effect of hyperinflation (-18.8 p.p.), recognition in 2014 of expenditure mainly on

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the global restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its targets (-7.1 p.p.), changes to the scope of consolidation (-4.9 p.p.), consisting of the sale of Telefónica Czech Republic and Telefónica Ireland and the acquisition of the E-Plus Group, and additionally affected by the value adjustment of companies in 2013 (+1.7 p.p.). Additionally, the year-on-year variation was affected by higher sales of non-strategic towers in 2014 as compared to 2013 (+0.9 p.p.). Excluding these effects, operating income would have increased by 1.9% year-on-year.

The share of profit (loss) of investments accounted for by the equity method for the year was a loss of 510 million euros (a loss of 304 million euros in 2013), mainly due to valuation adjustments of Telco, S.p.A. at Telecom Italia, S.p.A. This, along with the contribution to the year's results, had a negative impact of 464 million euros (a loss of 267 million euros in 2013).

Net financial expense amounted to 2,822 million euros in 2014 (-1.6% year-on-year), and includes 293 million euros due to net negative foreign exchange differences primarily as a result of the Company's decision to adopt the SICAD II exchange rate of the Venezuelan bolivar. Excluding this effect, net financial expenses would have fallen 8.2% year-on-year, mainly due to a 9.1% reduction in the average debt, placing the effective cost of debt in 2014 was 5.40%, 6 basis points higher than in 2013. The greater weight of debt in Latin America currencies and repayment and maturity of cheap debt in euros increases the average cost in 47 basis points, while lower rates in Latin America and Europe reduce it in 41 basis points.

Corporate income tax totaled 383 million euros in 2014 on a pre-tax income of 3,635 million euros, implying an effective tax rate of 10.5%, 10.3 percentage points lower year-on-year. This was mainly due to the effect of a review of deferred taxes in Brazil following a change to legislation during the second quarter of 2014, and to a larger recognition of tax credits in Colombia.

Profit attributable to non-controlling interests reduced net profit by 251 million euros in 2014, 33.2% less than in 2013, mainly due to the effect of a review of deferred taxes in Brazil following a change to legislation in 2014, and to a larger recognition of tax credits.

As a result of the foregoing, consolidated net profit for 2014 was 3,001 million euros (down by 34.7% year-on-year).

Year ended December 31, 2013 compared with year ended December 31, 2012

The main metrics in the income statement were negatively affected in 2013 by exchange rate fluctuations, mainly due to the devaluation of the Venezuelan bolivar and the depreciations of the Brazilian reais and the Argentine peso against the euro. Exchange rates reduced year-on-year revenue and OIBDA growth in 2013 by 7.5 percentage points.

In addition, the Telefónica Group deconsolidated the results from the Atento Group as of the end of November 2012 (following the disposal of the Atento Group during the fourth quarter of 2012), therefore affecting year-on-year comparisons of Telefónica's reported financial results.

Revenues in 2013 totaled 57,061 million euros, decreasing 8.5% in reported terms, mainly affected by the exchange rate differences and the effect of hyperinflation in Venezuela which reduced year-on-year growth by 7.5 percentage points. Additionally, revenues were affected by changes in the consolidation perimeter especially the deconsolidation of the Atento group (-1.7 p.p.). Excluding these impacts, revenue in 2013 would have increased by 0.7% year-on-year.

The structure of revenues reflects the Company's diversification and despite the above-mentioned exchange rate impact, Telefónica Hispanoamérica accounted for 29.5% of total revenues in 2013 (+2.7 p.p. compared with 2012).

Telefónica United Kingdom accounted for 11.7% (+0.4 p.p. compared with 2012), Telefónica Brazil accounted for 21.4% of the total (-0.4 p.p. compared with 2012) and Telefónica Spain accounted for 22.7% (-1.3 p.p. compared with 2012).

Mobile data revenues decreased 0.7% in reported terms. Excluding the impact of exchange rate differences and the effect of the hyperinflation in Venezuela, mobile data revenues would have increased 9.3%. These revenues accounted for 37% of mobile service revenues in 2013, a 3 percentage points growth compared with 2012. Especially noteworthy is the growth in non-SMS data revenues (+11.2% in reported terms and +22.2% excluding the impact of exchange rate

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differences and the effect of hyperinflation in Venezuela), which accounted for 64% of total data revenues in the year in reported terms (+7 p.p. year-on-year).

Other income: mainly includes own work capitalized in our fixed assets, the profit from the sale of other assets, and the disposal of non-strategic towers of Telefónica Brazil, Telefónica Hispanoamérica and Telefónica Spain. The lower level of sales of non-strategic towers compared to 2012 is the main driver for the decrease in other income, decreasing to 1,693 million euros in 2013 from 2,323 million euros in 2012.

Other income in 2013 consisted mainly of the sale of non-strategic towers in Telefónica Brazil, Telefónica Hispanoamérica and Telefónica Spain (113 million euros in other income and 111 million euros in OIBDA), the capital gain from the disposal of the assets of the fixed business of Telefónica United Kingdom (83 million euros), the capital gain from the sale of assets in Telefónica Germany (76 million euros) and the capital gain from the sale of the stake in Hispasat (21 million euros).

In 2012 other income was mainly comprised of income from the sale of non-strategic towers in Telefónica Brazil, Telefónica Hispanoamérica and Telefónica Spain (659 million euros in other income and 643 million euros in OIBDA), the gain from the sale of applications (39 million euros), and the capital gains from the sale of the Atento group (61 million euros), of Rumbo (27 million euros) and the partial sale of Hispasat (26 million euros).

Total expenses, which include supplies, personnel expenses and other expenses (primarily external services and taxes) amounted to 39,678 million euros in 2013. This represented an 8.7% decrease year-on-year in reported terms, which was primarily due to:

- exchange rate differences and the effect of hyperinflation in Venezuela (-7.3 p.p.);
- changes in the consolidation perimeter caused by the disposal of Atento and Rumbo (-1.9 p.p.);
- value adjustments and loss on sale of companies in 2013 and 2012:
- the impact of losses on the sale of companies in 2013, (totaling 192 million euros), primarily from the sale agreements to Telefónica Ireland and Telefónica Czech Republic (+0.4 p.p.);
- the impact of value adjustments and loss on sale of companies in 2012, which totaled an amount of 624 million euros, primarily from the sale of part of our stake in China Unicom and a value adjustment of Telefónica Ireland (-1.4 p.p.); and
- a contractual change in the commercial model for selling handsets in Chile as a result of which we began from September 2012, to record all of the costs of handsets sold immediately rather than capitalizing such costs and depreciating them over the life of the contract (+0.4 p.p.).

Excluding the aforementioned items, total expenses grew 1.2% in 2013 compared with 2012, mainly as a result of the greater commercial activity in Telefónica Brazil and Telefónica Hispanoamérica, focused on capturing high-value customers.

- Supplies stood at 17,041 million euros in 2013, falling 5.7% with respect to 2012, affected to a large degree by exchange rate differences and the effect of hyperinflation in Venezuela, which reduced this item by 7.3 percentage points. Additionally, the year-on-year change is affected by changes in the consolidation perimeter (-1.4 p.p.) and by the contractual change in the commercial model for selling handsets in Chile discussed above (+0.9 p.p.).

Excluding both effects, expenses grew 2%, as a result of the greater commercial activity in Telefónica Brazil and Telefónica Hispanoamérica, both in the mobile segment, due to an increase in the weighting of smartphone sales, and in the fixed business, mainly Pay-TV, which offset the decline in equipment costs of operators in Europe and the lower termination costs at the group level.

- Personnel expenses totaled 7,208 million euros and fell by 15.9% with respect to 2012, mainly affected by the exchange rate differences and the effect of hyperinflation in Venezuela (-6.2 p.p.) and changes in the consolidation perimeter (-13.6 p.p.). Excluding both effects personnel expenses increased by 4% due to the negative impact of inflation in certain Latin American countries, which more than offset declines reported by Telefónica Spain, Telefónica Czech Republic and Telefónica United Kingdom due to savings from workforce restructuring

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programs. This item also reflects restructuring expenses amounting to 156 million euros in 2013 compared to 67 million euros in 2012.

The average headcount in 2013 was 129,893 employees, 3.9% lower than the average in 2012, excluding the impact of the deconsolidation of Atento.

- Other expenses amounted to 15,428 million euros, falling 8.2%, mainly affected by the impact of exchange rate differences and the effect of hyperinflation in Venezuela (-8 p.p.). In addition, it was also affected by the above-mentioned value adjustment in companies in 2012 and 2013 (-2.6 p.p.), expenses associated with the sale of non-strategic towers (-0.1 p.p.) and changes in the consolidation perimeter (+3.5 p.p.). Excluding these effects this item fell 1.1%, explained by the lower costs of operators in Europe, mainly in commercial expenses, systems and networks, due to the efficiency measures carried out especially in Telefónica Spain, which involved simplification of processes, distribution channels and call centers redefinition, internalization of activities, savings from the restructuring plan and temporary cancelation of the corporate contribution to pension plans.

OIBDA reached 19,077 million euros, showing a decline of 10.1%, mainly affected by:

- exchange rate differences and the effect of hyperinflation in Venezuela (-7.5 p.p.);
 - the lower amount of non-strategic towers sold in 2013 compared to 2012 (-2.5 p.p.);
 - changes in the consolidation perimeter mainly caused by the disposal of Atento (-1.0 p.p.);
 - the contractual change in the commercial model for selling handsets in Chile (-0.8 p.p.);
 - value adjustments and loss on sale of companies in 2013 and 2012:
- the impact of the sale of companies mainly the disposal of Telefónica Ireland and Telefónica Czech Republic in 2013 (-1.3 p.p.); and
 - the impact of value adjustments and loss on sale of companies in 2012 totaled 624 million euros, primarily from the sale of part of our stake in China Unicom and a value adjustment of Telefónica Ireland (+2.9 p.p.).

Excluding the aforementioned items, OIBDA for 2013 would have been stable versus the prior year. OIBDA margin was 33.4% in 2013, down 0.6 percentage points year-on-year in reported terms.

By region, Telefónica Spain, accounted for 33.2% of consolidated OIBDA in 2013 (+1 p.p. compared to 2012), while Telefónica Hispanoamérica accounted for 29.0% (+0.8 p.p. compared to 2012) and Telefónica Brazil accounted for 20.7% (-3.7 p.p. compared to 2012).

Depreciation and amortization in 2013 (9,627 million euros) registered a year-on-year drop of 7.7%, mainly due to the exchange rate effects and the sale of the Atento Group, Telefónica Ireland and Telefónica Czech Republic. The depreciation and amortization charges arising from purchase price allocation processes amounted to 856 million euros during 2013 (-11.1% year-on-year).

Operating income in 2013 totaled 9,450 million euros, decreasing 12.5% year-on-year, mainly affected by exchange rate differences and the effect of hyperinflation in Venezuela (-9.6 p.p.). Additionally the year-on-year change was due to the lower amount of non-strategic towers sold in 2013 as compared to 2012 (-4.9 p.p.), changes in the

consolidation perimeter (-1.5 p.p.), the contractual change in the commercial model for selling handsets in Chile in 2012 (-0.9 p.p.), sales of companies (-0.1 p.p.) and the value adjustment of companies in 2013 and 2012 (+4.9 p.p.). Excluding these impacts operating income would have fallen 0.5% year-on-year.

Share of profit (loss) of investments accounted for by the equity method was a loss of 304 million euros in 2013 compared with a loss of 1,275 million euros in 2012 and was affected by adjustments to the value of the stake of Telco, S.p.A. in Telecom Italia, S.p.A and the contribution to results in the year, resulting in a negative impact on “Share of loss of investments accounted for by the equity method” of 267 million euros and 1,277 million euros, respectively.

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Net financial expense amounted to 2,866 million euros in 2013, 21.7% lower than in 2012, of which 111 million euros were due to net negative foreign exchange differences. Excluding this effect, net financial expenses fell 11.8% year-on-year, mainly due to an 11.4% reduction in the average debt. The effective cost of debt in 2013 excluding exchange rate differences was 5.34%, 3 basis points below 2012, with savings from management improvements over the gross cost of debt in euros offsetting the impact on the effective cost from the fact that most of the reduction has been in euros (with below average costs).

Corporate income tax in 2013 stood at 1,311 million euros, on a pre-tax income of 6,280 million euros, implying an effective tax rate of 20.9%, 4.0 percentage points lower year-on-year. This is mainly due to the recognition in 2012 of the tax assessments in Spain.

Profit attributable to non-controlling interests reduced 2013 net profit by 376 million euros and was down 20.7% year-on-year, mainly as a result of the lower profit attributed to minority interests in Telefónica Brazil, affected by the exchange rate.

As a result of the performance of the above items, profit for the period in 2013 was 4,593 million euros (16.9% higher year-on-year).

Segment results

Some of the figures in the table below are compared at a constant exchange rate in order to analyze yearly performance excluding the effect of exchange rate variation. For certain of the financial results discussed below, comparison has been made using the previous year's average exchange rate to convert the figure and by excluding the consideration of Venezuela as a hyperinflationary economy. In these cases a comment of "excluding foreign exchange rate effect" or "excluding foreign exchange rate effect and the consideration of Venezuela as a hyperinflationary economy" (or similar wording) has been indicated.

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Some figures discussed further below have been compared in local currency (LC), taking the financial magnitudes in the relevant local currency as they were registered in the corresponding periods.

	% 2012		% 2013		% 2014		% YoY 12/13		% YoY 13/14	
	Total		Total		Total		Reported	Ex fx (*)	Reported	Ex fx (*)
Millions of euros	2012		2013		2014					
Revenues	62,356		57,061		50,377		(8.5%)	(1.0%)	(11.7%)	0.4%
Telefonica Spain	14,996	24.0%	12,959	22.7%	12,023	23.9%	(13.6%)	(13.6%)	(7.2%)	(7.2%)
Telefonica United Kingdom	7,042	11.3%	6,692	11.7%	7,062	14.0%	(5.0%)	(0.5%)	5.5%	0.2%
Telefonica Germany	5,213	8.4%	4,914	8.6%	5,522	11.0%	(5.7%)	(5.7%)	12.4%	12.4%
Telefonica Brazil	13,618	21.8%	12,217	21.4%	11,231	22.3%	(10.3%)	2.2%	(8.1%)	0.5%
Telefonica Hispanoamérica	16,741	26.8%	16,855	29.5%	13,155	26.1%	0.7%	16.1%	(22.0%)	14.6%
OIBDA	21,231		19,077		15,515		(10.1%)	(2.6%)	(18.7%)	(5.7%)
Telefonica Spain	6,815	32.1%	6,340	33.2%	5,671	36.6%	(7.0%)	(7.0%)	(10.6%)	(10.6%)
Telefonica United Kingdom	1,602	7.5%	1,637	8.6%	1,744	11.2%	2.2%	7.0%	6.5%	1.1%
Telefonica Germany	1,351	6.4%	1,308	6.9%	733	4.7%	(3.2%)	(3.2%)	(44.0%)	(44.0%)
Telefonica Brazil	5,161	24.3%	3,940	20.7%	3,543	22.8%	(23.7%)	(13.0%)	(10.1%)	(1.7%)
Telefonica Hispanoamérica	5,983	28.2%	5,531	29.0%	4,068	26.2%	(7.6%)	8.6%	(26.5%)	14.2%
OIBDA Margin	34.0%		33.4%		30.8%					
Telefonica Spain	45.4%		48.9%		47.2%					
Telefonica United Kingdom	22.7%		24.5%		24.7%					
Telefonica Germany	25.9%		26.6%		13.3%					
Telefonica Brazil	37.9%		32.3%		31.5%					
Telefonica Hispanoamérica	35.7%		32.8%		30.9%					
Operating Income (OI)	10,798		9,450		6,967		(12.5%)	(2.8%)	(26.3%)	(7.5%)
Telefonica Spain	4,752	44.0%	4,437	46.9%	3,866	55.5%	(6.6%)	(6.6%)	(12.9%)	(12.9%)
Telefonica United Kingdom	607	5.6%	621	6.6%	623	8.9%	2.3%	7.2%	0.3%	(4.7%)
Telefonica Germany	118	1.1%	77	0.8%	(693)	(9.9%)	(35.4%)	(35.4%)	n.m.	n.m.
Telefonica Brazil	2,843	26.3%	1,831	19.4%	1,781	25.6%	(35.6%)	(26.6%)	(2.7%)	6.3%
Telefonica Hispanoamérica	3,221	29.8%	3,007	31.8%	2,034	29.2%	(6.6%)	16.8%	(32.4%)	20.9%
Profit for the year attributable to equity holders of the parent	3,928		4,593		3,001					

(*) Excludes exchange rate effects and hyperinflation in Venezuela.

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Revenues and OIBDA contribution by country

We include below certain charts showing the revenues and OIBDA contribution by main countries, and segments, to total consolidated Group revenues and OIBDA for 2012, 2013 and 2014. By way of explanation, total Group revenues and OIBDA are 100% in each year, and in each country or region the percentage represents its contribution to the total Group.

As the preceding charts show, the Telefónica Group has high geographic diversification. During the periods covered by such charts, Telefónica Spain and Telefónica Brazil are the largest single contributors to Group revenue and OIBDA, followed by the United Kingdom, Germany, Argentina, Peru, Mexico and Venezuela and Central America.

Together, these countries accounted for 91.1% of OIBDA and 88.3% of Group revenues in 2014 (89.5% of OIBDA and 85.4% of revenues in 2013 and 89.5% of OIBDA and 84.3% of revenues in 2012, respectively).

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Beginning in 2013 we present figures of Venezuela and Central America together, and figures for previous years have been revised accordingly.

Contribution to Growth by Country

In the charts included below, we show the contribution to revenue and OIBDA year-on-year growth of our segments and the main countries where we operate for 2013 and 2014, excluding foreign exchange rate effects and the effect of hyperinflation in Venezuela. For example, in the chart relating to our revenues for 2014, the drop of -1.7% of Telefónica Spain means that Telefónica Spain's drop in revenues caused a 1.7 percentage points year-on-year decrease in total consolidated revenues in 2014, and the addition of all countries' contributions shown in the chart equals the total Group revenues increase in 2014 (+0.4% in 2014), excluding the impact of exchange rate differences and the effect of hyperinflation in Venezuela.

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The below tables show the evolution of Telefónica's estimated mobile and DSL accesses market share over the past three years:

Evolution of competitive position

	Mobile Market Share		
	(1)		
Telefónica	2012	2013	2014
Spain	36.2%	33.9%	31.2%
United Kingdom	26.6%	26.5%	26.9%
Germany (2)	16.7%	16.9%	36.9%
Brazil	29.1%	28.6%	28.4%
Argentina	29.7%	31.4%	31.3%
Chile	38.8%	38.7%	39.4%
Peru	60.0%	59.7%	55.2%
Colombia	21.6%	24.0%	23.5%
Venezuela	32.9%	32.0%	33.7%
Mexico	19.2%	18.5%	20.8%
Central America	29.7%	31.8%	31.5%
Ecuador	29.3%	32.6%	27.9%
Uruguay	37.4%	35.8%	34.4%

(1) Company estimation.

(2)Germany in 2014 includes E-Plus.

Evolution of competitive position

	DSL Market Share (1)		
	2012	2013	2014
Telefónica			
Spain	48.8%	47.4%	45.1%
Brazil	18.8%	16.3%	16.4%
Argentina	30.9%	30.5%	30.3%
Chile	41.2%	40.2%	39.8%
Colombia	18.1%	18.7%	18.8%

(1) Company estimation.

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Segments Discussion

TELEFÓNICA SPAIN

The below table shows the evolution of accesses in Telefónica Spain over the past three years.

ACCESSES

Thousands of accesses	2012	2013	2014	%YoY 12/13	%YoY 13/14
Fixed telephony accesses (1)	11,723.0	11,089.8	10,447.8	(5.4%)	(5.8%)
Naked ADSL	25.0	22.8	21.3	(9.1%)	(6.6%)
Internet and data accesses	5,779.3	5,899.0	5,928.7	2.1%	0.5%
Narrowband	54.0	38.5	30.9	(28.7%)	(19.6%)
Broadband (2)	5,709.3	5,846.8	5,885.9	2.4%	0.7%
Other (3)	16.0	13.7	11.9	(14.2%)	(13.7%)
Mobile accesses	20,608.7	19,002.1	17,575.4	(7.8%)	(7.5%)
Prepay	5,180.5	4,262.7	3,328.1	(17.7%)	(21.9%)
Contract (4)	15,428.2	14,739.3	14,247.3	(4.5%)	(3.3%)
Pay-TV (5)	710.7	672.7	1,884.7	(5.4%)	180.2%
WLR (6)	481.2	525.8	570.6	9.3%	8.5%
Unbundled loops	3,262.0	3,787.1	4,087.3	16.1%	7.9%
Shared ULL	183.5	130.6	94.1	(28.9%)	(27.9%)
Full ULL (7)	3,078.5	3,656.5	3,993.3	18.8%	9.2%
Wholesale ADSL	652.3	676.8	707.8	3.8%	4.6%
Other (8)	0.5	0.4	0.3	(23.9%)	(28.5%)
Final Clients Accesses	38,821.7	36,663.6	35,836.7	(5.6%)	(2.3%)
Wholesale Accesses	4,396.0	4,990.1	5,366.0	13.5%	7.5%
Total Accesses	43,217.8	41,653.6	41,202.7	(3.6%)	(1.1%)

Notes:

(1) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 digital access x30.

Company's accesses for internal use included. Includes VoIP and Naked ADSL.

(2) Includes ADSL, satellite, optical fiber, cable modem and broadband circuits.

(3) Leased lines.

(4) In the first quarter of 2014, 569 thousand M2M inactive accesses were disconnected.

(5) Since the second quarter of 2014, Pay-TV accesses include 131 thousand "TV Mini" customers.

(6) Wholesale Line Rental.

(7) Includes naked shared loops.

(8) Wholesale circuits.

The results of Telefónica Spain in 2014 showed a softer decline in revenues than in 2013 versus 2012, due in part to a more favorable macroeconomic and competitive environment.

By the end of 2014 the Company became a leader of the Pay-TV market with 1.9 million customers (almost three times higher than in 2013), more than 1 million 100 Mb fiber customers (doubling the figure for 2013) and a mobile contract base showing positive net adds at year-end for the first time since 2011 (excluding the disconnection of 569 thousand M2M accesses during the first quarter of the year).

Telefónica Spain improved its commercial offer throughout the year, offering extra value to the customer. Notably, it launched “Movistar Fusión TV” in April as part of the convergent “Fusión” portfolio, increased the volume of its mobile data and the flexibility to purchase content bundles during the third quarter and launched “Movistar Series” in December, an “a la carta” and multiscreen TV service offering certain TV series, for 7 euros a month (including VAT), just one day after their premiers in the United States. In addition, it improved its mobile-only contract offering by launching the new “VIVE” portfolio in October, which was renewed in February 2015, increasing data volume and introducing new value-added services.

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Telefónica Spain had 41.2 million accesses at the end of December 2014, down 1% year-on-year, mainly due to the disconnection of 569 thousand inactive M2M mobile contract accesses in the first quarter of the year.

“Movistar Fusión” with a customer base of 3.7 million and 1.4 million additional mobile lines, maintained solid year-on-year growth (+27% compared to 2013) and increased its penetration (73% of fixed broadband customer base and 57% of mobile contract customer base in the consumer segment). At the same time, higher value offers (fiber and TV) continued to attract customers. As a result, 21% of Movistar Fusión customers had 100 Mb fiber speed (+8 p.p. year-on-year) and 45% have IPTV (+31 p.p. year-on-year).

By year-end, fiber accesses totaled 1.3 million (more than doubling the figure for 2013) and accounted for 22% of the broadband customer base, and customers with 100 Mb fiber speed, who have higher ARPU (currently a 10 euros price premium) and lower churn (0.5 times) compared with DSL customers, exceeded one million.

The intense pace of fiber deployment reached 10.3 million premises passed at the end of the year.

Pay-TV accesses reached 1.9 million (almost three times higher than in December 2013), reflecting the strong adoption of “Movistar TV”, a key aspect of the new bundle offer with quality content and innovative functionality, making Telefónica the leading Pay-TV operator.

Total mobile accesses stood at 17.6 million, down 8% compared with year-end 2013, affected by the disconnection of 569 thousand inactive M2M mobile contract accesses in the first quarter of the year.

The contract base added 77 thousand net additions in 2014 (excluding the impact of the disconnection of 569 thousand inactive M2M mobile contract accesses), growing for the first time since 2011 (+0.5% year-on-year), mainly driven by churn reduction (-0.2 p.p. year-on-year), with a lower loss of customers due to portability (-30% year-on-year), and the growth of gross additions (+10% year-on-year).

Smartphone penetration stood at 61% of the mobile voice base (+10 p.p. compared to year-end 2013) and significantly boosted data traffic growth to 28% year-on-year in 2014. LTE network rollout continued to progress well and coverage reached 58% of the population at the end of 2014.

CONSOLIDATED RESULTS

Millions of euros

TELEFÓNICA SPAIN	2012	2013	2014	%YoY 12/13	%YoY 13/14
Revenues	14,996	12,959	12,023	(13.6%)	(7.2%)
Wireless Business	6,464	5,121	4,556	(20.8%)	(11.0%)
Mobile service revenues	5,453	4,580	3,888	(16.0%)	(15.1%)
Wireline Business	9,541	8,861	8,543	(7.1%)	(3.6%)
OIBDA	6,815	6,340	5,671	(7.0%)	(10.6%)
OIBDA Margin	45.4%	48.9%	47.2%	3.5 p.p.	(1.8 p.p.)
Depreciation and amortization	(2,063)	(1,903)	(1,805)	(7.7%)	(5.1%)
Operating Income (OI)	4,752	4,437	3,866	(6.6%)	(12.9%)
CapEx	1,692	1,529	1,732	(9.6%)	13.3%
OpCF (OIBDA-CapEx)	5,123	4,811	3,939	(6.1%)	(18.1%)

2014 Results

Revenues totaled 12,023 million euros in 2014 (-7.2% year-on-year). We consider revenue breakdown to be increasingly less relevant given the high penetration level of our convergent offer. However, we continue to report revenue separately for information purposes. Fixed business revenues fell 3.6% year-on-year in 2014, due to lower access and voice revenues, partially offset by higher broadband and new services revenues, mainly TV and IT. Mobile business revenues fell 11.0% year-on-year in 2014 due to the decline in mobile accesses and the 10.1% drop in ARPU, impacted by lower prices in the new tariff portfolio.

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Mobile ARPU is becoming less representative of the Group's business performance, owing to its significant dependence on the allocation of revenue in convergent offers. In 2014 mobile ARPU declined by 10.1% year-on-year, impacted by lower prices in the new tariff portfolio.

TELEFÓNICA SPAIN	2012	2013	2014	%YoY 12/13	%YoY 13/14
Voice Traffic (Million minutes)	36,382	34,428	35,600	(5.4%)	3.4%
ARPU (EUR) (1)	20.6	17.7	15.9	(14.3%)	(10.1%)
Prepay	8.8	7.3	6.2	(17.8%)	(14.5%)
Contract (2)	28.6	24.0	20.6	(16.2%)	(14.2%)
Data ARPU (EUR) (1)	6.5	6.8	7.0	4.4%	3.6%
% non-SMS over data revenues	85.2%	92.1%	95.0%	7.0 p.p.	2.8 p.p.

Notes:

(1) Impacted by the disconnection of 569 thousand inactive M2M accesses in the first quarter of 2014.

(2) Excludes M2M.

Total expenses, which include supplies, personnel expenses and other expenses (mainly subcontract expenses and others) but do not include depreciation and amortization expenses, amounted to 6,987 million euros in 2014, down 1.1% year-on-year, reflecting the control of costs and the transformation efficiency initiatives implemented several years ago. The breakdown by components is as follows:

- Supplies (2,592 million euros) increased 4.2% year-on-year in 2014, mainly reflecting higher spending on handsets and TV content.
 - Personnel expenses (2,139 million euros) increased 1.2% year-on-year in 2014, primarily due to the end of the redundancy program in 2013 and the Company's contribution to its pension plan in July 2014, following its temporary freeze from April 2013 to July 2014. At December 31, 2014, Telefónica Spain's headcount totaled 30,020 employees compared to 29,764 at December 31, 2013.
- Other expenses (2,256 million euros) fell by 8.5% year-on-year in 2014, reflecting the savings resulting from the simplification processes, redefinition of distribution channels and in-sourcing of activities, which more than offset the expenses related to the increased commercial effort in advertising and handset sales.

OIBDA amounted to 5,671 million euros in 2014 (-10.6% year-on-year), affected by the drop in revenues despite the higher commercial effort by Telefónica Spain to capture the growth and value opportunity in the market. Excluding the sale of non-strategic towers for 70 million euros in 2013 and 191 million in 2014, OIBDA fell 12.6% year-on-year in 2014.

2013 Results

In 2013 revenues stood at 12,959 million euros (-13.6% year-on-year), partly affected by the sharp drop in revenues from handset sales (-46.4% year-on-year) due to the removal of subsidies in March 2012.

- Excluding handset sales, revenues in 2013 amounted to 12,417 million euros (-11.2% year-on-year). Excluding the impact of regulation (which imposed interconnection and roaming), these revenues would have fallen 9.6%

year-on-year.

- Revenues from the fixed business fell 7.1% year-on-year in 2013, due to lower access and voice revenues, primarily driven by the loss of accesses, and lower broadband and new service revenues, reflecting the negative performance of broadband ARPU, and affected by the migration of customers to the new tariffs.
- Mobile revenues fell by 20.8% year-on-year in 2013. Mobile service revenue declined by 16.0% year-on-year in 2013 explained by ARPU decline.

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- Telefónica Spain revenue reduction is mainly due to ARPU reductions across services reflecting lower prices of the renewed portfolio and lower customers consumption, and also, as a consequence of declines in accesses (-4% year-on-year), as a consequence of the high competitive pressure in the market.

ARPU decreased 14.3% year-on-year in 2013, affected by the 60% cut in the mobile termination rate since July 1, in addition to the cuts implemented in April 2013 (-13%) and October 2012 (-8%). The drop in ARPU also reflects lower prices of the new tariff portfolio and lower customer usage. However, it is worth noting that the ARPU of individual services is less representative following the launch of “Movistar Fusión”, as it is affected by the defined allocation of convergent product revenues between the fixed and mobile businesses.

Total expenses, which include supplies, personnel expenses and other expenses (mainly subcontract expenses and others) but do not include depreciation and amortization expenses, amounted to 7,064 million euros in 2013, 18.2% less than in 2012, mainly due to a reduction in commercial costs, mainly as a result of the elimination of handset subsidies and other savings arising from the various efficiency improvement programs. The breakdown by components is as follows:

- Supplies declined 23.9% year-on-year in 2013 to 2,486 million euros, mainly due to lower handset costs as a consequence of the new commercial policy and lower mobile interconnection costs.
- Personnel expenses amounted to 2,113 million euros in 2013, down 6.1% year-on-year as a result of the savings derived from the redundancy program and from the temporary removal of Telefónica Spain’s contribution to the pension plan beginning in April 2013. At December 31, 2013, Telefónica Spain’s headcount totaled 29,764 employees, compared to 31,434 at December 31, 2012.
- Other expenses amounted to 2,464 million euros in 2013, down by 20.9% compared to 2012 due to lower commercial expenses and the savings from Telefónica Spain’s simplification process, as well as the redefinition of the distribution channel and call centers and the in-sourcing of activities.

OIBDA stood at 6,340 million euros in 2013, showing a year-on-year decline of 7.0%. The OIBDA decrease is explained by the revenue decrease, partially offset by costs reduction, especially the continued reduction in commercial costs after the handset subsidy removal policy, and other savings arising from several efficiency programs (such as simplification of processes, distribution channel and call centers redefinition, internalization of activities, savings from the restructuring personnel plan and temporary cancelation of the corporate contribution to pension plans).

Excluding the sale of non-strategic towers for 60 million euros in 2012 and 70 million euros in 2013, OIBDA decreased by 7.2%.

TELEFÓNICA UNITED KINGDOM

ACCESSES

Thousands of accesses	2012	2013	2014	%YoY 12/13	%YoY 13/14
Fixed telephony accesses (1)	377.4	208.2	228.0	(44.8%)	9.5%
Internet and data accesses	560.1	14.8	19.2	(97.4%)	29.8%
Broadband	560.1	14.8	19.2	(97.4%)	29.8%
Mobile accesses	22,864.2	23,649.0	24,479.1	3.4%	3.5%
Prepay	10,962.9	10,764.7	10,761.2	(1.8%)	(0.0%)

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Contract	11,901.3	12,884.3	13,717.9	8.3%	6.5%
Final Clients Accesses	23,801.7	23,872.0	24,726.4	0.3%	3.6%
Wholesale Accesses (2)	40.5	31.6	-	(22.1%)	-
Total Accesses	23,842.2	23,903.6	24,726.4	0.3%	3.4%

Notes:

(1) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 digital access x30.

Company's accesses for internal use included. Includes VoIP and Naked ADSL.

(2) From the first quarter of 2014, the company stopped offering a wholesale service.

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Telefónica and the Hutchison Whampoa Group agreed to commence exclusive negotiations for a possible Whampoa Group purchase of O2 UK on January 23, 2015.

Total accesses were 24.7 million at year-end 2014 (+3.4% year-on-year). Mobile accesses increased by 3.5% year-on-year to 24.5 million by year-end 2014, boosted by the continued expansion of contract customers and a stable pre-pay segment. In this way, the proportion of contract customers rose 2 percentage points year-on-year to account for 56% of total mobile accesses. Contract net additions totaled 0.8 million customers in 2014 as a result of good performance, despite fierce competition. Contract customer churn improved by 0.1 percentage points year-on-year in 2014 to 1.0%. Smartphone penetration (as a percentage of mobile internet data tariff over total mobile customers) rose by 3 percentage points with respect to year-end, to 52%.

Telefónica United Kingdom continues the deployment of its LTE network, reaching 58% outdoor coverage at year end, and keeps focusing on offering a positive network experience to 4G customers.

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CONSOLIDATED RESULTS

Millions of euros				%YoY 12/13		%YoY 13/14	
TELEFÓNICA UNITED KINGDOM	2012	2013	2014€	LC	€	LC	
Revenues	7,042	6,692	7,062	(5.0%)	(0.5%)	5.5%	0.2%
Mobile service revenues	6,060	5,461	5,397	(9.9%)	(5.7%)	(1.2%)	(6.2%)
OIBDA	1,602	1,637	1,744	2.2%	7.0%	6.5%	1.1%
OIBDA Margin	22.7%	24.5%	24.7%	1.7 p.p.	1.7 p.p.	0.2 p.p.	0.2 p.p.
Depreciation and amortization	(995)	(1,016)	(1,121)	2.1%	6.9%	10.3%	4.7%
Operating Income (OI)	607	621	623	2.3%	7.2%	0.3%	(4.7%)
CapEx	748	1,385	755	85.3%	94.0%	(45.5%)	(48.3%)
OpCF (OIBDA-CapEx)	854	252	989	(70.5%)	(69.1%)	n.m.	n.m.

2014 Results

Total revenues in 2014 increased 5.5% year-on-year to 7,062 million euros in reported terms (+0.2% year-on-year excluding foreign exchange rate effects).

- Mobile service revenues reached 5,397 million euros, down 1.2% year-on-year in reported terms (-6.2% excluding foreign exchange rate effects) negatively affected by the “Refresh” model, mobile termination rate cuts and roaming regulation. Excluding the impacts of, mobile termination rate cuts, (+0.4 p.p.), roaming regulation (+0.5 p.p.) and the new commercial model “Refresh” (+6.5 p.p.), mobile service revenues would have increased by 1.3% year-on-year as a result of the growth in mobile accesses and price stabilization. The “Refresh” model translates into more revenue from handset sales (even where the number of units sold are not increased), since handset sales are fully recognized upfront.
- Non-SMS data revenues rose 23.9% year-on-year (+17.6% year-on-year excluding foreign exchange rate effects), accounting for 57.9% of data revenues (+8.0 p.p. year-on-year).
- Data revenue recorded an increase of 1.5% year-on-year in 2014. Data revenue in 2014 accounted for 57% of mobile service revenue, 4 percentage points more than 2013.

ARPU fell by 3.9% year-on-year in 2014 (-8.8% excluding the effect of foreign exchange rates), adversely affected by the “Refresh” model. Excluding the effect of regulation and the “Refresh” model (+7.2 p.p.), ARPU would have decreased by 1.6% year-on-year. Voice ARPU fell 12.5% in reported terms (-16.9% excluding the effect of foreign exchange rates). Data ARPU increased by 3.6% in reported terms (-1.6% year-on-year excluding the effect of foreign exchange rates).

TELEFÓNICA UNITED KINGDOM	2012	2013	2014	%YoY LC 12/13	%YoY LC 13/14
Voice Traffic (Million minutes)	48,250	48,479	49,096	0.5%	1.3%
ARPU (EUR)	22.5	19.6	18.8	(8.8%)	(8.8%)
Prepay	9.6	7.7	7.3	(16.0%)	(9.3%)
Contract (1)	40.3	35.0	33.1	(9.1%)	(10.1%)
Data ARPU (EUR)	11.4	10.4	10.8	(4.5%)	(1.6%)
% non-SMS over data revenues	46.8%	50.0%	57.9%	3.2 p.p.	8.0 p.p.

Notes:

(1) Excludes M2M.

Mobile voice traffic in 2014 remained stable compared to 2013, while data traffic increased by 72%, driven by higher penetration of smartphones and higher usage per customer.

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Total expenses were 5,502 million euros in 2014, up by 4.7% year-on-year in reported terms, impacted by the foreign exchange rate in 5.3 percentage points. Excluding this impact, expenses would have decreased by 0.6%. The breakdown by components is as follows:

- Supplies increased by 3.4% year-on-year in 2014 in reported terms to 3,520 million euros, impacted by the foreign exchange rate (+5.2 p.p.). Excluding this impact, supplies would have decreased by 1.8%, mainly due to lower interconnection costs.
- Personnel expenses were down by 15.3% year-on-year in 2014, amounting to 460 million euros, impacted by the exchange rate (+4.3 p.p.). Excluding this impact, personnel costs would have been down by 19.6%, as a result of the outsourcing of the customer service facility. Personnel expenses were also affected by restructuring costs (5 million euros in 2014 and 48 million euros in 2013).
 - Other expenses were 1,521 million euros in 2014, a 16.1% year-on-year increase in reported terms, with an exchange rate impact of 5.9 percentage points. Excluding this impact, other expenses would have increased by 10.3% as a result of the outsourcing of the customer service facility.

OIBDA totaled 1,744 million euros, up by 6.5% in reported terms (+1.1% excluding the foreign exchange rate impact), due to higher revenues and cost control partially offset by the negative contribution of the “Refresh” model.

2013 Results

Total revenues amounted 6,692 million euros in 2013, down 5.0% year-on-year in reported terms (-0.5% excluding exchange rate differences) reflecting the disposal of the fixed consumer business as well as the “Refresh” model contribution (+5.8 p.p. in 2013). The “Refresh” model translates into more revenue from handset sales (even where the number of units sold do not increase), since handset sales are fully recognized upfront.

- Mobile service revenues in 2013 totaled 5,461 million euros, a decrease of 9.9% year-on-year in reported terms (-5.7% excluding the impact of exchange rate differences) negatively affected by the “Refresh” model, mobile termination rate cuts and roaming regulation. Excluding the impact of mobile termination rate cuts (+2.4 p.p.) and roaming regulation (+0.6 p.p.), as well as the impact of the “Refresh” model (+1.3 p.p.), the mobile service revenues would have decreased 1.3% year-on-year due to the pressure on ARPU.
- Non-SMS data revenues grew 0.8% year-on-year (+5.5% year-on-year excluding exchange rate differences) accounting for 50% of data revenues in 2013 (+3 p.p. year-on-year).
- The decline of SMS volumes led data revenue to decline 1.2% year-on-year in 2013. In 2013, data revenues accounted for 53% of mobile service revenues, an increase of 2 percentage points compared to the previous year.
- ARPU fell 12.9% year-on-year (-8.8% year-on-year excluding the impact of the exchange rate differences) negatively impacted by the “Refresh” model, as well as mobile termination rate cuts and roaming regulation. Excluding the impact of regulation, ARPU would have decreased by 5.5% year-on-year. Voice ARPU fell 17.1% in reported terms (-13.2% excluding exchange rate differences and -8.4% excluding additionally the effect of regulations). Data ARPU fell 8.8% in reported terms (-4.5% excluding exchange rate differences).

Mobile voice traffic remained relatively stable with respect to the previous year.

Total expenses amounted to 5,256 million euros in 2013, decreasing 6.1% year-on-year in reported terms, (affected by the foreign exchange rate difference in -4.4 p.p.). Excluding this effect, total expenses would have decreased 1.7% year-on-year. The breakdown by components is as follows:

- Supplies amounted to 3,403 million euros, decreasing 5.8% year-on-year affected by foreign exchange rate differences (-4.4 p.p.). Excluding this effect, supplies would have decreased 1.4% mainly due to the reduction of interconnection costs.

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- Personnel expenses amounted to 543 million euros in 2013, a decrease of 1.6% in reported terms, affected by foreign exchange rate differences (-4.6 p.p.). Excluding this effect, personnel expenses would have increased by 3.0%, affected by 48 million euros of restructuring expenses.
- Other expenses were 1,310 million euros and decreased by 8.7% in reported terms, affected by foreign exchange rate differences (-4.3 p.p.). Excluding this effect these costs would have decreased 4.4%, due to lower commissions and benefits of the “Refresh” model.

OIBDA stood at 1,637 million euros in 2013, representing a year-on-year increase of 2.2% in reported terms (+7.0% excluding the impact from exchange rate differences). Year-on-year performance was positively affected by the capital gain of 83 million euros from the fixed consumer business disposal offset partially by the negative impact of restructuring expenses (48 million euros). In addition, OIBDA performance reflects the acceleration in the recording of hardware sales from the “Refresh” model, partially mitigated by the higher upfront commercial costs resulting from the model.

TELEFÓNICA GERMANY

ACCESSES

Thousands of accesses	2012	2013	2014	%YoY 12/13	%YoY 13/14
Fixed telephony accesses (1)	2,249.0	2,124.9	2,036.4	(5.5%)	(4.2%)
Internet and data accesses	2,678.9	2,516.1	2,387.0	(6.1%)	(5.1%)
Narrowband	302.6	271.7	243.2	(10.2%)	(10.5%)
Broadband	2,376.3	2,244.3	2,143.8	(5.6%)	(4.5%)
Mobile accesses	19,299.9	19,401.0	42,124.9	0.5%	117.1%
Prepay	9,191.3	9,114.9	23,350.7	(0.8%)	156.2%
Contract	10,108.5	10,286.1	18,774.1	1.8%	82.5%
Final Clients Accesses (2)	24,284.9	24,042.0	46,548.3	(1.0%)	93.6%
Wholesale Accesses	1,087.9	1,125.0	1,113.3	3.4%	(1.0%)
Total Accesses	25,372.8	25,166.9	47,661.5	(0.8%)	89.4%

Notes:

(1) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 digital access x30.

Company’s accesses for internal use included. Includes VoIP and Naked ADSL.

(2) 2012 includes 57.2 thousand of Pay-TV accesses.

The results of the E-Plus Group have been fully consolidated with Telefónica Germany since October 1, 2014 (once the acquisition was completed, following its announcement in 2013). As a result, mobile accesses reached 42.1 million at the end of 2014, up by 117% year-on-year, making us the largest operator on the German market in terms of mobile customers according to the Company’s estimates. At the date of consolidation, the E-Plus Group accounted for 22.6 million accesses.

The German market remained competitive in 2014, with pressure on commercial expenses and focus on bundled voice and data tariffs, oriented to capture higher-value customers and develop the current base of customers by increasing their consumption. Bundle offers were also brought on to the market by our main competitors in the second half of 2014.

As part of its strategy of development and monetization of data traffic, Telefónica Germany continued to step up its investment in LTE. It finished the year with 62% coverage of outdoor population, and increased the volume of handsets and users of this technology.

The main brands operated by Telefónica Germany, via its “O2 Blue All-in” and “Base All-in” portfolios, have maintained prices focused on increasing the value of our customers, with a view to increasing the proportion of higher-value customers.

Contract mobile customers grew by 83% year-on-year, impacted by the incorporation of the E-Plus Group, reaching 18.8 million accesses. The proportion of contract accesses reached 45%, impacted by the higher proportion of pre-pay customers among the E-Plus Group customer base. Smartphone penetration reached 29% in 2014, with a considerable volume of LTE customers.

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Retail broadband accesses stood at 2.1 million in December 2014 (-4.5% year-on-year).

CONSOLIDATED RESULTS

Millions of euros

TELEFÓNICA GERMANY	2012	2013	2014	%YoY 12/13	%YoY 13/14
Revenues	5,213	4,914	5,522	(5.7%)	12.4%
Wireless Business	3,845	3,673	4,375	(4.5%)	19.1%
Mobile service revenues	3,152	2,989	3,580	(5.2%)	19.8%
Wireline Business	1,363	1,235	1,138	(9.4%)	(7.8%)
OIBDA	1,351	1,308	733	(3.2%)	(44.0%)
OIBDA Margin	25.9%	26.6%	13.3%	0.7 p.p.	(13.4 p.p.)
Depreciation and amortization	(1,233)	(1,231)	(1,426)	(0.1%)	15.7%
Operating Income (OI)	118	77	(693)	(35.4%)	n.m.
CapEx	609	666	849	9.4%	27.5%
OpCF (OIBDA-CapEx)	743	642	(116)	(13.5%)	n.m.

2014 Results

Total revenues amounted to 5,522 million euros in 2014, up by 12.4% due mainly to the consolidation of the E-Plus Group since October 1, 2014, and offset in part by the lower service revenues during the rest of the year.

- Mobile service revenues totaled 3,580 million euros in 2014, up by 19.8% year-on-year due mainly to the consolidation of the E-Plus Group since October 1, 2014 and offset in part by the lower voice and SMS revenues during the rest of the year. Telefónica Germany continued to focus on data revenues, which increased 24.3% and accounted for 50.1% of mobile service revenues. Non-P2P SMS data revenues accounted for 71% of the total data revenues (+4.7 p.p. year-on-year), increasing 33% year-on-year.
- Fixed telephony revenues fell by 7.8% year-on-year in 2014 to stand at 1,138 million euros. The main reason for this was a decline in fixed broadband customers (partially mitigated by VDSL growth) and transit business revenues, impacting slightly on the margin.

ARPU was negatively affected by the consolidation of the E-Plus Group and decreased by 7.1% year-on-year in 2014, reducing its year-on-year decline compared to 2013, due to the smaller proportional impact of migration to new tariffs, and the various actions undertaken with respect to the Telefónica Germany's customer base in order to boost income and data leverage.

TELEFÓNICA GERMANY	2012	2013	2014	%YoY 12/13	%YoY 13/14
Voice Traffic (Million minutes)	29,519	30,152	41,186	2.1%	36.6%
ARPU (EUR)	13.8	12.7	11.8	(7.9%)	(7.1%)
Prepay	5.5	5.1	5.4	(6.8%)	4.5%
Contract (1)	21.5	19.6	18.4	(9.0%)	(5.9%)
Data ARPU (EUR)	6.2	6.2	5.9	0.7%	(3.9%)
% non-SMS over data revenues	56.7%	66.5%	71.2%	9.8 p.p.	4.7 p.p.

Notes:

(1) Excludes M2M.

Total expenses were 4,895 million euros in 2014, up by 29.7% year-on-year due mainly to the consolidation of the E-Plus Group since October 1, 2014. Telefónica Germany recorded a 409 million euros provision for the restructuring process resulting from the integration of the E-Plus Group. The breakdown by component is as follows:

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- Supplies stood at 2,144 million euros, up by 9.5% year-on-year due mainly to the consolidation of the E-Plus Group since October 1, 2014. There were lower interconnection costs arising from a decrease in SMS volumes and lower interconnection rates, partially offset by higher handset purchases (mainly towards the end of the year).
- Personnel expenses amounted to 828 million euros during the year, up by 97.7% due mainly to the consolidation of the E-Plus Group since October 1, 2014. In addition, personnel expenses were impacted by the recognition of an expenditure of 321 million euros, related to the provision for the restructuring process resulting from the integration of the E-Plus Group.
- Other expenses amounted to 1,923 million euros during the year, up by 37.5% mainly impacted by the change of perimeter and the recognition of an expenditure of 87 million euros related to the provision for the restructuring process resulting from the integration of the E-Plus Group. Excluding these impacts, other expenses would have been impacted by higher commercial costs.

OIBDA fell 44% year-on-year to stand at 733 million euros in 2014. OIBDA was impacted by the recognition of an expenditure of 409 million euros related to the provision for the restructuring process resulting from integration of the E-Plus Group.

2013 Results

Revenues totaled 4,914 million euros in 2013, down 5.7% year-on-year. This decline is partly attributable to the reduction in termination rates. Excluding this impact, revenues would have fallen 3.5% in 2013, with ongoing headwinds coming from customer base repositioning and the acceleration of declines in SMS volumes. Handset revenues decreased by 1.4% year-on-year in 2013 mainly due to the increasing share of attractive affordable handsets in the market, including selective bundle offers of selected smartphones with high value mobile data tariffs.

- Mobile service revenues stood at 2,989 million euros in 2013, a year-on-year decrease of 5.2%. Excluding the impact of the reduction in termination rates, mobile service revenues would have fallen by 1.5% year-on-year in 2013, mainly as a result of the increase in tariff renewals in the customer base and the lower volume of SMS traffic, which were not offset by the growth in data revenues. Telefónica Germany continued to monetize its data revenues with an increase in non-P2P SMS data revenue of 21.7% during the year, accounting for 67% of total data revenue (+10 p.p. year-on-year). As a result, mobile data revenues in 2013 increased 3.7% year-on-year to account for 48% of mobile service revenues (+4 p.p. year-on-year).
- Fixed telephony revenues decreased 9.4% year-on-year in 2013, to 1,235 million euros despite the increasing adoption of VDSL. This is mainly the result of the decline in DSL customer base (mitigated by an increasing uptake of VDSL) and a further reduction of revenues from the low margin voice transit business.

ARPU decreased by 7.9% year-on-year in 2013, mainly as a result of the reduction in mobile termination rates. Excluding this impact, ARPU would have declined by 4.3% in 2013 on the back of tariff migrations, acceleration of the decrease in SMS volumes and an increasing share of discounted online channel activities, which was partly offset by the increasing demand for mobile data services.

Voice ARPU decreased by 14.9% year-on-year in 2013, mainly as a result of regulatory changes (lower roaming and interconnection rates) and the migration of customer to current tariffs. Data ARPU grew 0.7% year-on-year, as a result of the increased penetration of mobile broadband, despite the negative impact of lower SMS volumes.

Mobile voice traffic showed year-on-year growth of 2.1%, derived from the growth in the contract customer base.

Total expenses amounted to 3,775 million euros in 2013, decreasing 3.8% year-on-year. The breakdown by component is as follows:

- Supplies amounted to 1,958 million euros, decreasing 8.1% year-on-year, mainly driven by a reduction in interconnection expenses.
- Personnel expenses amounted to 419 million euros, decreasing 9.9% year-on-year as a result of an accumulation of activities at the end of 2012.

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- Other expenses stood at 1,398 million euros in 2013, increasing by 5.4% year-on-year, due mainly to the higher commercial cost incurred in retention and advertising activities.

OIBDA stood at 1,308 million euros in 2013, registering a decline of 3.2% due to the pressure in revenues, the higher commercial costs and certain handset promotions, offset in part by the capital gains obtained from asset sales totaling 76 million euros (46 million euros of fiber assets and 30 million euros of the related hosting business, Telefónica Online Services).

TELEFÓNICA BRAZIL

ACCESSES

Thousands of accesses	2012	2013	2014	%YoY 12/13	%YoY 13/14
Fixed telephony accesses (1)	10,642.7	10,747.8	10,743.4	1.0%	(0.0%)
Internet and data accesses	3,964.3	4,102.0	4,082.6	3.5%	(0.5%)
Narrowband	137.9	92.1	73.7	(33.2%)	(19.9%)
Broadband (2)	3,748.4	3,936.7	3,939.8	5.0%	0.1%
Other (3)	78.1	73.2	69.0	(6.2%)	(5.8%)
Mobile accesses	76,137.3	77,240.2	79,932.1	1.4%	3.5%
Prepay	57,335.1	53,551.9	51,582.4	(6.6%)	(3.7%)
Contract	18,802.2	23,688.3	28,349.7	26.0%	19.7%
Pay-TV	601.2	640.1	770.6	6.5%	20.4%
Final Clients Accesses	91,345.4	92,730.0	95,528.6	1.5%	3.0%
Wholesale Accesses	24.4	18.8	25.9	(22.8%)	37.5%
Total Accesses	91,369.8	92,748.9	95,554.5	1.5%	3.0%

Notes:

- (1) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 digital access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.
- (2) Includes ADSL, optical fiber, cable modem and broadband circuits.
- (3) Retail circuits other than broadband.

During 2014, Telefonica Brazil strengthened its leadership in the high-value mobile segments, both in contract and LTE, driven by improvements in its networks and continuous innovation of its commercial offers. With respect to the fixed business, it made progress in its transformation process, speeding up deployment of the fiber network and increasing the number of TV accesses.

In the mobile segment, Telefonica Brazil captured more than 50% of the new contract customers on the market according to Anatel and achieved a market share of 38.9% as of December 2014 according to Anatel. Contract plans were simplified throughout the year offering larger volumes of data, minutes and SMS in exchange for higher levels of ARPU.

In its fixed business, the company has maintained its strategic focus on fiber deployment, with 4.1 million premises passed with fiber and 375 thousand homes connected, and also on increasing Pay-TV accesses (up 20.4% year-on-year).

CONSOLIDATED RESULTS

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Millions of euros			%YoY 12/13		%YoY 13/14		
TELEFÓNICA BRAZIL	2012	2013	2014€	LC	€	LC	
Revenues	13,618	12,217	11,231	(10.3%)	2.2%	(8.1%)	0.5%
Wireless Business	8,573	8,092	7,618	(5.6%)	7.5%	(5.9%)	2.9%
Mobile service revenues	8,167	7,608	7,228	(6.8%)	6.1%	(5.0%)	3.8%
Wireline Business	5,045	4,125	3,613	(18.2%)	(6.8%)	(12.4%)	(4.2%)
OIBDA	5,161	3,940	3,543	(23.7%)	(13.0%)	(10.1%)	(1.7%)
OIBDA Margin	37.9%	32.3%	31.5%	(5.6 p.p.)	(5.6 p.p.)	(0.7 p.p.)	(0.7 p.p.)
Depreciation and amortization	(2,318)	(2,109)	(1,762)	(9.0%)	3.7%	(16.5%)	(8.7%)
Operating Income (OI)	2,843	1,831	1,781	(35.6%)	(26.6%)	(2.7%)	6.3%
CapEx	2,444	2,127	2,933	(13.0%)	(0.9%)	37.9%	50.7%
OpCF (OIBDA-CapEx)	2,717	1,813	610	(33.3%)	(24.0%)	(66.4%)	(63.2%)

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2014 Results

Revenues in 2014 totaled 11,231 million euros, an 8.1% year-on-year fall in reported terms. Excluding the effect of exchange rate differences, revenues would have grown by 0.5% year-on-year, mainly due to the positive performance of the mobile business (up 2.9% year-on-year), which offset the decline in fixed telephony revenues (down 4.2% year-on-year).

- Revenues from the mobile business totaled 7,618 million euros in 2014, falling by 5.9%. Excluding the effect of exchange rate differences, revenues from the mobile business would have increased by 2.9% due to the positive evolution of service revenues (up 3.8% year-on-year) as a result of the good performance of outbound revenues, which in turn increased as a result of an increase in the customer base and the increased proportion of data revenues. This trend was partially offset by falling handset sales (an 11.9% decline year-on-year) and lower inbound revenues affected by lower interconnection tariffs.
- Fixed telephony revenues totaled 3,613 million euros, down by 12.4%, although excluding the effect of exchange rates the decrease would have been 4.2%. This decrease was mainly due to the reduction of the fixed-mobile retail rate and the fixed by mobile substitution, bringing down our fixed telephony revenues despite a stable fixed customer base and greater minutes packages. This trend was partially offset by the increase of the broadband and new services revenues that grew 4.0% helped by the increase of accesses connected with fiber, with a higher ARPU, and the growth of the Pay-TV accesses.

The mobile ARPU decreased 8.8% year-on-year in reported terms. Excluding the effect of exchange rate differences, it would have decreased 0.6% year-on-year as a consequence of the negative impact of the reduction in the mobile termination rates. We believe the better quality of the clients' base is reflected in an increase of the outbound ARPU and a 16.0% growth of the data ARPU.

TELEFÓNICA BRAZIL	2012	2013	2014 12/13	%YoY 12/13	%YoY 13/14
Voice Traffic (Million minutes)	113,955	115,698	127,412	1.5%	10.1%
ARPU (EUR)	8.9	8.0	7.3	2.3%	(0.6%)
Prepay	5.0	4.5	3.9	1.5%	(4.3%)
Contract (1)	23.1	18.8	15.7	(7.3%)	(8.7%)
Data ARPU (EUR)	2.4	2.5	2.6	18.9%	16.0%
% non-SMS over data revenues	62.0%	67.0%	77.4%	5.0 p.p.	10.4 p.p.

Notes:

(1) Excludes M2M.

Total expenses totaled 7,949 million euros in 2014, falling 7.3% in reported terms, with an impact of 8.6 percentage points due to the exchange rate effect. Excluding this impact, total expenses would have increased by 1.3%. The breakdown by component is as follows:

- Supplies (2,680 million euros) were down by 14.3% in 2014, with an impact of 8 percentage points due to the exchange rate effect. Excluding this impact, supply costs would have fallen by 6.3% due to lower interconnection expenditure associated with regulatory changes and lower handset costs.
- Personnel expenses (976 million euros) were down by 5.8% in 2014, with an impact of 8.8 percentage points due to the exchange rate effect. Excluding this impact and the recognition in 2014 of expenditure on the global

restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its

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targets (+7.2 p.p.), personnel costs would have been down by 4.2% as a result of the staff restructuring programs and voluntary redundancies in 2013, which had an impact of 51 million euros in 2013.

- Other expenses (4,292 million euros) were down by 2.7% in 2014, with an impact of 9.1 percentage points due to the exchange rate effect. Excluding this effect, other operating expenses would have increased by 6.4%, driven by higher commercial and fiber acquisition costs, higher network deployment and fixed/mobile system improvement costs.

OIBDA stood at 3,543 million euros in 2014, a fall of 10.1% (down 1.7% excluding exchange rates effects). This decrease was mainly due to exchange rate effects and, to a lesser extent, expenses incurred as a result of the recognition in 2014 of expenditure on the global restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its targets (totaling 68 million euros and mainly accruing during the fourth quarter of 2014), the lower gains derived from the sale of non-strategic towers in 2014 (1 million euros) compared to 2013 (29 million euros), higher personnel costs, increased networks costs, higher handsets and customer service costs, due in part to the higher business volumes. Excluding the effect of exchange rate differences, the sale of non-strategic towers and the expenses incurred as a result of Telefónica's global restructuring program, OIBDA would have increased by 0.9%, a 0.1 percentage points improvement on the margin compared to 2013.

The OIBDA margin stood at 31.5% in reported terms for 2014.

2013 Results

Revenues totaled 12,217 million euros, 10.3% less than 2012. Excluding the effect of exchange rate differences, revenues increased 2.2% year-on-year, mainly due to the strong performance of the mobile business (up 7.5% year-on-year), offsetting the decline in fixed revenues (down 6.8% year-on-year).

- 2013 wireless business revenues amounted to 8,092 million euros, down 5.6%. Excluding the effect of exchange rate differences, however, they would have grown 7.5%, boosted by handset sales revenues (up 35.4% year-on-year). This increase was due to the higher weight of smartphone sales and the growth of service revenues (up 6.1% year-on-year) as a result of the growth in outgoing service revenues, which was attributable to the growth of the customer base and the greater weighting of data revenues; all of which was partially offset by a reduction in mobile termination rates, which had an adverse impact on incoming revenues.
- Revenues from the fixed business amounted to 4,125 million euros, down 18.2%. Excluding the effect of exchange rate differences, they would have decreased by 6.8%, affected by the reduction in the fixed-mobile retail tariff as well as by intense competition in the fixed broadband and Pay-TV businesses.

Mobile ARPU decreased 10.5% year-on-year in reported terms. Excluding the effect of exchange rate differences, it would have increased 2.3% year-on-year as a consequence of a better quality of the customer base, partially offset by the negative impact of the reduction in the mobile termination rates.

Total expenses, which include supplies, personnel expenses and other expenses (mainly subcontract expenses and others) but do not include depreciation and amortization expenses, amounted to 8,575 million euros in 2013, 6.5% less than in 2012 in reported terms and 6.5% higher than in 2012 in local currency. The breakdown by components is as follows:

- Supplies amounted to 3,128 million euros, increasing 1.6% year-on-year in reported terms and 15.8% in local currency, mainly due to higher content costs and higher site lease costs for the deployment of towers and due to our

sale and leaseback of towers;

- Personnel expenses amounted to 1,036 million euros in 2013, down 7.2% year-on-year in reported terms and increasing 5.7% in local currency affected by personnel restructuring costs (51 million euros); and
- Other expenses amounted to 4,411 million euros, a decrease of 11.4% compared to 2012 in reported terms, with an increase of 0.9% in local currency mainly due to expenses related to customer service, associated with higher commercial activity.

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OIBDA totaled 3,940 million euros in 2013, down 23.7% in reported terms (-13.0% excluding the effect of exchange rate differences). This performance was mainly due to the lower gains derived from the sale of non-strategic towers in 2013 (29 million euros) compared to 2012 (445 million euros). Excluding the impact of the sale of non-strategic towers and the impact of exchange rate differences, OIBDA would have decreased by 5.5%, losing 2.6 percentage points of margin with respect to 2012.

OIBDA margin stood at 32.3% in reported terms for 2013.

TELEFÓNICA HISPANOAMÉRICA

ACCESSES

Thousands of accesses	2012	2013	2014 12/13	%YoY 12/13	%YoY 13/14
Fixed telephony accesses (1) (2) (3)	13,510.7	13,778.5	13,374.4	2.0%	(2.9%)
Internet and data accesses	4,768.2	5,137.7	5,433.8	7.8%	5.8%
Narrowband	71.2	33.4	25.2	(53.1%)	(24.5%)
Broadband (4)	4,667.0	5,074.9	5,379.4	8.7%	6.0%
Other (5)	30.0	29.4	29.2	(1.9%)	(0.6%)
Mobile accesses	100,458.2	107,266.9	110,346.5	6.8%	2.9%
Prepay (6)(7)	79,806.4	84,524.1	86,698.0	5.9%	2.6%
Contract	20,651.8	22,742.7	23,648.5	10.1%	4.0%
Pay-TV	1,825.7	2,133.5	2,431.9	16.9%	14.0%
Final Clients Accesses	120,562.6	128,316.6	131,586.6	6.4%	2.5%
Wholesale Accesses	22.7	22.7	16.4	0.2%	n.m.
Total Accesses T. Hispanoamérica	120,585.3	128,339.3	131,603.0	6.4%	2.5%

Notes:

(1) PSTN (including public use telephony) x1; ISDN basic access x1; ISDN primary access; 2/6 Digital Access x30. Company's accesses for internal use included. Voice fixed wireless accesses included.

(2) In the first quarter of 2014, 45 thousand fixed wireless inactive accesses were disconnected in Mexico.

(3) In 2014, fixed telephony accesses include 50 thousand "fixed wireless" additional customers in Peru.

(4) Includes ADSL, optical fiber, cable modem and broadband circuits.

(5) Retail circuits other than broadband.

(6) In the first quarter of 2014, 1.9 million inactive accesses were disconnected in Mexico.

(7) In the fourth quarter of 2014, 1.8 million inactive accesses were disconnected in Central America.

Total accesses closed at 131.6 million at year-end (+2.5% year-on-year).

Regarding commercial operations in mobile business:

Mobile accesses totaled 110.3 million (+2.9% year-on-year) thanks to strong contract segment growth, which expanded by 4.0% year-on-year. Growth was particularly strong in Ecuador (+13.4% year-on-year), Peru (+13.6% year-on-year) and Chile (+4.5% year-on-year). In the pre-pay segment (+2.6% year-on-year), growth was driven mainly by Colombia (+8.7% year-on-year), Mexico (+7.1% year-on-year) and Peru (+3.7% year-on-year), despite disconnection of 1.9 million inactive accesses in Mexico and 1.8 million inactive accesses in Central America, as well as more restrictive criteria for customer registration in certain countries in the region.

Total net adds amounted 3.1 million in 2014, with a year-on-year increase in customer additions during the year (+4%) and strong commercial activity in Mexico and Chile. Annual churn stood at 3.4% in 2014, affected by the disconnection of inactive accesses and more restrictive criteria for prepay customer registration.

Growth of smartphones (+32% year-on-year) continued to be the main driver of accesses growth, with a penetration over mobile accesses of 26% (+6 p.p. year-on-year), and an increase in pre-pay customers (+2.6%). Penetration of

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smartphones was particularly successful in Mexico (+11 p.p.), Venezuela and Central America (+9 p.p.), Colombia (+5 p.p.) and Chile (+5 p.p.).

Total ARPU grew by 10.6% during the year, due to increases in voice traffic (+16.0%) as a result of higher volumes of minutes by customer (+5.4%), and increased data traffic (+65.3%), both of which are mainly attributable to the higher penetration of smartphones and larger average consumption per access.

Regarding the fixed business:

Traditional business accesses stood at 13.4 million, with a decrease of 2.9% year-on-year, affected by the erosion of traditional business in the region, including access losses in Venezuela and Central America (-9.7% year-on-year), Chile (-4.6% year-on-year), Peru (-3.1% year-on-year) and Argentina (-2.2% year-on-year). On the other hand, Colombia did not show signs of such erosion and achieved an increase in customers in 2014 (+1% year-on-year).

Broadband accesses totaled 5.4 million at year-end 2014 (+6% year-on-year), after reaching net adds of 0.3 million accesses during 2014, in line with the commercial activity and churn in 2013. The penetration by fixed broadband accesses over traditional business accesses was 40% (+3 p.p. year-on-year). The mix of accesses focused on higher speeds, and accesses with speeds in excess of 4 Mb accounted for 49.9% (+12 p.p. year-on-year).

Pay-TV accesses accounted 2.4 million (+14% year-on-year) after net adds of 0.3 million accesses, with an improvement in all the countries of the region that offer the service. Growth was particularly positive in Venezuela and Central America (+21% year-on-year), Colombia (+19.7% year-on-year) and Chile (+19.5% year-on-year).

CONSOLIDATED RESULTS

Millions of euros				%YoY 12/13		%YoY 13/14	
TELEFÓNICA HISPANOAMÉRICA	2012	2013	2014€	LC(*)	€	LC(*)	
Revenues	16,741	16,855	13,155	0.7%	16.1%	(22.0%)	14.6%
Wireless Business	12,724	13,020	9,578	2.3%	19.1%	(25.7%)	16.5%
Mobile service revenues	11,470	11,510	8,454	0.4%	15.9%	(25.7%)	17.5%
Wireline Business	4,424	4,272	3,604	(3.4%)	7.6%	(10.1%)	8.4%
OIBDA	5,983	5,531	4,068	(7.6%)	8.6%	(26.5%)	14.2%
OIBDA Margin	35.7%	32.8%	30.9%	(2.9 p.p.)	(2.3 p.p.)	(1.9 p.p.)	(0.1 p.p.)
Depreciation and amortization	(2,762)	(2,524)	(2,034)	(8.6%)	(2.0%)	(19.4%)	5.3%
Operating Income (OI)	3,221	3,007	2,034	(6.6%)	16.8%	(32.4%)	20.9%
CapEx	2,988	3,118	2,842	4.3%	21.3%	(8.8%)	42.5%
OpCF (OIBDA-CapEx)	2,995	2,413	1,226	(19.4%)	4.1%	(49.2%)	(24.1%)

Note:

(*) Excludes the effect of hyperinflation in Venezuela.

2014 Results

Revenues amounted to 13,155 million euros in the year 2014, falling 22% year-on-year in reported terms, mainly due to the effect of exchange rates and hyperinflation in Venezuela (-36.1 p.p.). Excluding these effects, revenues would have increased by 14.6% year-on-year, thanks to a good performance of the fixed and mobile data revenues, as well as the mobile voice revenues, in both cases due to the increase in our customer base, higher usage per customer and higher data penetration, despite the negative impact of interconnection tariffs (which subtracted 1.6 p.p. from year-on-year growth).

- Mobile service revenues decreased by 25.7% in reported terms, mainly due to the effect of exchange rates and hyperinflation in Venezuela (-43.2 p.p.) and the negative impact of interconnection tariffs (-2.4 p.p.). Excluding these effects, service revenues would have increased by 17.5% year-on-year. Below is additional information by country:
- In Argentina, mobile service revenues were down by 19.8% in reported terms. Excluding the effect of exchange rates they would have been up by 19.3% as a result of the good performance of voice and data revenues, despite the negative impact of certain billing changes implemented (which implied the billing by seconds after the first thirty seconds of the call), and the greater use and penetration of data.

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- In Peru, mobile service revenues increased by 7.8% in reported terms. Excluding the effect of exchange rates they would have increased by 13.4%. Growth was mainly driven by the higher customer base and the increase of data scale (non-SMS data revenues were up 42.7% in the year), following the launch of LTE, helping to increase average revenue per customer.
- In Mexico, mobile revenues increased by 5.4% in reported terms. Excluding the effect of exchange rates they would have increased by 10%, as a result of to the new interconnection scenario which led to competitive offers that have driven up customers' voice and data consumption.
- In Venezuela and Central America, mobile service revenues were down by 65.1% in reported terms. Excluding the effect of exchange rates and hyperinflation in Venezuela they would have increased by 36.8%, mainly due to 25% price increases for all services as of July in Venezuela, and the expansion of mobile data services leveraged in non-SMS data revenues growth (+68%), which accounted for 76% of data revenues (+12 p.p. year-on-year).
- Data revenues in the segment were down by 24.4%, due to the effect of exchange rates and hyperinflation in Venezuela. Revenues would have been up by 23% excluding these effects, mainly due to the growth of non-SMS data revenues (+43.4%), which accounted for 74% of data revenues (+11 p.p. year-on-year).
- Fixed business revenues decreased by 10.1% in reported terms in the year, due to the effects of exchange rates (-18.5 p.p.). Excluding this effect, fixed revenues would have increased by 8.4% year-on-year in 2014, driven by broadband and new services revenues (-2.6% year-on-year in reported terms, +16.2% excluding exchange rate effects). The revenues from broadband and new services, accounted for 60% of fixed revenues (+5 p.p. year-on-year). The acceleration of growth in fixed revenues was particularly notable in Argentina, where there was a substantial increase in access and voice revenues (due to higher ARPU).

Total expenses stood at 9,342 million euros in 2014, down by 19.2% in reported terms, as a result mainly of the exchange rate effect and hyperinflation in Venezuela (-33.8 p.p.), which was partially offset by a provision of 99 million euros relating to the recognition in 2014 of expenditure on the global restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its targets. Excluding these effects, total expenses would have increased by 14.1%. Below is additional information by country:

- Argentina: expenses stood at 2,294 million euros, a decrease of 15.9% in reported terms. Excluding the effect of exchange rates, expenses would have grown by 25.1% due to general price increases, although the company continues to make an effort to contain costs and mitigate the effects of high inflation.
- Peru: expenses stood at 1,718 million euros, up by 5.9% in reported terms. Excluding the effect of exchange rates, expenses would have been up by 11.4% due to higher commercial costs driven from the pressure of competition on the Peruvian market.
- Venezuela and Central America: expenses stood at 975 million euros, down by 61.3% in reported terms. Excluding the effect of exchange rates and hyperinflation in Venezuela, expenses would have increased by 36.7%, mainly due to higher prices in general, and the effect of greater expenditure in U.S. dollars for provided services and equipment purchases, being affected by the negative impact of the currency depreciation in Venezuela.

By component, variation is explained by:

- Supplies (3,841 million euros) fell by 22.9% in 2014 in reported terms. Excluding the effect of exchange rates and hyperinflation in Venezuela (-27.6 p.p.), expenses would have grown by 4.7%. The increase is due to handsets costs

caused by sales of high-end equipment which more than offset lower mobile termination rates in Chile, Colombia, Peru and Mexico.

- Personnel expenses (1,525 million euros) were down by 12.7% in reported terms, but would have been up by 27.6% excluding the negative impact of 39.5 percentage points caused by the effect of exchange rates and hyperinflation in Venezuela. The increase in these costs is due to a general rise of inflation in certain countries in the region. The recognition of expenditures relating to the global restructuring program, in accordance with the simplification initiatives that the Group is implementing to meet its targets, added 6.3 percentage points to the variation.

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- Other expenses (3,976 million euros) fell by 17.7% in reported terms. Excluding the effect of exchange rates and hyperinflation in Venezuela (+38.2 p.p.) and sales of non-strategic towers in 2013 (-0.1 p.p.), these expenses increased by 21.1%, mainly due to higher voice and data traffic and higher sales campaigns costs.

This brought OIBDA to 4,068 million euros in 2014, down by 26.5% in reported terms, due to:

- Exchange rate differences and hyperinflation in Venezuela (-40.1 p.p.).
- Recognition of the global restructuring program costs (99 million euros; -2 p.p.), in accordance with the simplification initiatives the Group is implementing to meet its targets.
 - The non-strategic towers sales (4 million euros in 2014 and 11 million euros in 2013; -0.1 p.p.).

Excluding these impacts, OIBDA would have increased by 16.4%.

The OIBDA margin stood at 30.9% for the year, down by 1.9 percentage points year-on-year in reported terms, although excluding the effect of exchange rates and hyperinflation in Venezuela, the impact of global restructuring program, in accordance with the simplification initiatives the Group is implementing to meet its targets, and sales of non-strategic towers, it would have been up by 0.5 percentage points. The increase was due to a higher margin in all countries in the region, with the exception of Venezuela and Uruguay, and particularly good margin performances in Mexico, Colombia and Chile.

2013 Results

Revenues in 2013 amounted to 16,855 million euros in 2013, with a 0.7% year-on-year growth in reported terms, mainly due to exchange rate differences and the effect of hyperinflation in Venezuela. Excluding these factors, which reduced growth by 15.2 percentage points, growth would have been 16.1%. This performance reflects the positive performance of mobile service revenues, which rose by 15.9% in the year excluding the impact of exchange rates differences and the effect of hyperinflation in Venezuela (decrease 0.4% in reported terms), due to the good performance of data revenue and despite the negative impact of changes in regulations. The main countries that explained this deviation were:

- In Argentina, mobile service revenues fell by 2.1% in reported terms, although excluding the effect of exchange rates these would have increased by 21.2% year-on-year as a result of growth of the higher customer base as well as the and higher consumption level, principally data. In this way, data revenues were up by 5.7% in reported terms, although stripping out the effect of exchange rates they would have increased by 30.8% year-on-year in 2013. These accounted for 48% of service revenues (+3 p.p. year-on-year). This increase was mainly due to higher non-SMS data revenue (60.8% year-on-year, accounting for 49% of mobile data revenues (+9 p.p. year-on-year)).
- In Peru, mobile service revenues were up by 4.8% in reported terms, although excluding the effect of exchange rates they would have increased by 10.8% year-on-year in 2013 despite the negative impact of regulatory changes affecting fixed-mobile calls. Excluding the negative impact of the regulatory changes, the revenues would have grown 13.4% year-on-year in 2013. This increase was principally driven by data revenues, up by 28.4% in reported terms and up 35.8% year-on-year, excluding the effect of exchange rates. Additionally, these revenues continue to represent a growth opportunity as a result of the solid increase in non-SMS data revenues, up by 65% year-on-year and accounting for 81% of mobile data revenues in the year (+14 p.p. year-on-year).

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In Venezuela and Central America, mobile service revenues increased by 4.4% in reported terms, although excluding the effect of exchange rates and hyperinflation in Venezuela, these would have increased by 34.6% year-on-year, due to the boost of mobile data services and the growth of voice traffic. Data revenues accounted for 29.9% of mobile service revenues. This evolution is boosted by the strong increase in non-SMS data revenue (+56.1% year-on-year), accounting for 64% of data revenues (+7 p.p. year-on-year).

- The mobile service revenue growth was driven by the expansion of data in the region, reflected 42.8% in 2013 in non-SMS data revenues, excluding exchange rate differences and the effect of hyperinflation in Venezuela

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(17% in reported terms). Voice revenues dropped 5.2% year-on-year in reported terms but were up 11.6% year-on-year without exchange rate differences and the impact of hyperinflation in Venezuela, due to the sharp increase in traffic.

- Revenues from handset sales amounted to 1,510 million euros and fell 20.3% in reported terms, mainly as a result of the impact of exchange rate differences and the effect of hyperinflation in Venezuela. Excluding these effects, growth would have been 47.4%, growing in all countries in the region as result of the growth in smartphones.
- Revenues from the fixed business fell 3.4% in reported terms, affected by exchange rate differences and the effect of hyperinflation in Venezuela. Excluding this effect, revenues from the fixed business increased 7.6% year-on-year.

Total expenses, which include supplies, personnel expenses and other expenses (mainly subcontract expenses and others) but do not include depreciation and amortization expenses, stood at 11,562 million euros in 2013, growing 3.3% in reported terms, affected by:

- Exchange rate differences and the effect of hyperinflation in Venezuela (-14.3 p.p.);
 - The sale of non-strategic towers (-0.1 p.p.);and
- Contractual changes in the commercial model for selling handsets in Chile (+1.5 p.p.).

Excluding these effects, total expenses would have grown 16.2%. The change in total expenses is explained by:

- Argentina: expenses stood at 2,728 million euros, up by 2% year-on-year in reported terms. Excluding the effect of exchange rates, costs would have grown by 26.3% due to general price increases, although the company continues to make an effort to contain costs mitigating the effects of the high inflation.
- Peru: expenses stood at 1,621 million euros, up by 3.5% year-on-year in reported terms. Excluding the effect of exchange rates, expenses would have grown by 9.5%. Excluding the effect of exchange rates and the sale of non-strategic towers, expenses would have increased by 10.0% due to higher commercial costs related to high-value customers, higher content costs, increased personnel costs due to profit-sharing (employees receive a percentage of the net profit) and larger tax costs, due to the 1% tax on profits from the TV and broad band businesses.
- Venezuela and Central America: expenses stood at 2,520 million euros, up by 4.0% year-on-year in reported terms. Excluding the effect of exchange rates and hyperinflation in Venezuela, expenses would have increased by 33.6%, mainly due to the general price level, as well as due to the effect of the greater expenditure in U.S. dollars for services rendered and handset purchases, impacted by the impact of the depreciation of the Venezuelan bolívar.

The breakdown by components explaining the 16.2% variation is as follows:

- Supplies increased to 4,983 million euros, an increase of 8.3% year-on-year in reported terms affected by the exchange rate differences and the effect of hyperinflation in Venezuela (-14.6 p.p.) and contractual changes in the commercial model for selling handsets in Chile (+3.6 p.p.). Excluding both effects, supply cost would have grown by 19%. The decline of MTR expenses (net of exchange rate differences and the effect of hyperinflation in Venezuela) did not offset the growth in costs, due to the greater commercial activity in the mobile business, with a higher weight of smartphone sales, and at the fixed business, with higher content costs associated with the sharp rise in Pay-TV accesses, and increased expenses associated with the provision of data services.

- Personnel expenses stood at 1,746 million euros (+1.1% year-on-year in reported terms) growing 17.2% excluding the impact of exchange rates differences and the effect of hyperinflation in Venezuela. This year-on-year growth is mainly due to the impact of inflation in some countries in the segment.
- Other expenses were 4,834 million euros, declining 0.7% in reported terms, affected by the exchange rate differences and the effect of hyperinflation in Venezuela (-13.3 p.p.) and the sale of non-strategic towers (-0.2 p.p.).

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Excluding both effects, other expenses grew 13.0%, due to the higher sales commissions and customer service expenses associated with increased commercial activity.

OIBDA stood at 5,531 million in 2013, showing a reported year-on-year decline of 7.6%, affected by:

- Exchange rate differences and the effect of hyperinflation in Venezuela (-16.1 p.p.).
- Contractual changes in the commercial model for selling handsets in Chile (-2.8 p.p.).
 - The sale of non-strategic towers (-2.1 p.p.).

Excluding the aforementioned items, OIBDA growth would have been 14.3%.

The OIBDA margin stood at 32.8% for the full year, down 2.9 percentage points year-on-year in reported terms; primarily due to the negative evolution of the exchange rates and lower sales of non-strategic towers in 2013 (11 million euros compared to 139 million euros in 2012).

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Our services and products

Mobile business

Telefónica offers a wide variety of mobile and related services and products to personal and business customers. Although they vary from country to country, Telefónica's principal services and products are as follows:

- **Mobile voice services:** Telefónica's principal service in all of its markets is mobile voice telephony.
- **Value added services:** Customers in most of the markets have access to a range of enhanced mobile calling features, including voice mail, call hold, call waiting, call forwarding and three-way calling.
- **Mobile data and Internet services:** Current data services offered include Short Messaging Services, or SMS, and Multimedia Messaging Services, or MMS, which allow customers to send messages with images, photographs, sound recordings and video recordings. Customers may also receive selected information, such as news, sports scores and stock quotes. Telefónica also provides mobile broadband connectivity and Internet access. Through mobile Internet access, customers are able to send and receive e-mail, browse the Internet, download games, purchase goods and services in m-commerce transactions and use Telefónica's other data and software services.
- **Wholesale services:** Telefónica has signed network usage agreements with several MVNOs in different countries.
- **Corporate services:** Telefónica provides business solutions, including mobile infrastructure in offices, private networking and portals for corporate customers that provide flexible online billing.
- **Roaming:** Roaming agreements allow Telefónica customers to use their mobile handsets when they are outside their service territories, including on an international basis.
- **Fixed wireless:** Telefónica provides fixed voice telephony services through mobile networks in Brazil, Venezuela, Argentina, Peru, Mexico, Ecuador, El Salvador, Guatemala and Nicaragua.
- **Trunking and paging:** Telefónica provides digital mobile services for closed user groups of clients and paging services in Spain and most of its operations in Latin America.

Fixed-line telephony business

The principal services Telefónica offers in its fixed businesses in Europe and Latin America are:

- **Traditional fixed telecommunication services:** Telefónica's principal traditional fixed telecommunication services include PSTN lines; ISDN accesses; public telephone services; local, domestic and international long-distance and fixed-to-mobile communications services; corporate communications services; supplementary value added services (including call waiting, call forwarding, voice and text messaging, advanced voicemail services and conference-call facilities); video telephony; business oriented value-added services; intelligent network services; leasing and sale of handset equipment; and telephony information services.
- **Internet and broadband multimedia services:** The principal Internet and broadband multimedia services include Internet service provider service; portal and network services; retail and wholesale broadband access through ADSL, naked ADSL (broadband connection without the monthly fixed line fee); narrowband switched access to Internet for universal service, and other technologies. Telefónica also offers high-speed Internet services through fiber to the

home (FTTH) in certain markets (primarily Spain, Brazil and Chile) and VDSL-based services (primarily Spain and Germany). Telefónica also offers VoIP services in some markets.

- Data and business-solutions services: the data and business-solutions services principally include leased lines; virtual private network, or VPN, services; fiber optics services; the provision of hosting and application, or ASP, service, including web hosting, managed hosting, content delivery and application, and security services; outsourcing

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and consultancy services, including network management, or CGP; and desktop services and system integration and professional services.

- Wholesale services for telecommunication operators: the wholesale services for telecommunication operators principally include domestic interconnection services; international wholesale services; leased lines for other operators' network deployment; and local loop leasing under the unbundled local loop regulation framework). It also includes bit stream services, bit stream naked, wholesale line rental accesses and leased ducts for other operators' fiber deployment.

Digital services

The main highlights in services developed by Telefónica Digital in 2014 are:

- Video/TV services: IPTV services (Internet protocol), over-the-top network television services, and cable and satellite TV. In certain markets, advanced Pay-TV services are offered, such as high-definition TV (HDTV), Multiroom (allowing clients to watch different TV channels in different rooms) and Digital Video Recording (DVR).
- M2M: Includes both M2M connectivity services and end-to-end products in different countries including in-house developments, as the "smart" M2M solution, which enables "smart" meter communications services.
- e-Health services or telecare: These services allow tele-assistance through connectivity services to chronic patients, and other eHealth services.
- Financial services and other payment services: These services allow customers to make transfers, payments and mobile recharges among other transactions through prepaid accounts or bank accounts.
- Security services: Includes services such as the "Latch" applications, which allow consumers to remotely switch their digital services on and off.
- Cloud computing services: These services include the Instant Servers services, Telefónica's new global public cloud service for corporate clients. This entails high-performance virtual servers that are optimized for mobile and corporate applications (both fixed and mobile).
- Advertising: Includes advertising products based on SMS and IT Technologies such as SMS campaigns or bulk SMS sales to corporations, mobile portals and any other advertising related activities.
- Big Data: Includes the product "Smart Steps" which helps retailers, municipalities and public security bodies to understand the influx of people. Anonymous mobile data network and aggregates are used to calculate the influx of people in an area.
- Future Communications: Includes "TU Go", Movistar's exclusive application that lets clients have the same number on all their devices and communicate among such devices via Wi-Fi.

Sales and Marketing

Our sales and marketing strategy is aimed toward reinforcing our market position, generating brand awareness, promoting customer growth and achieving customer satisfaction. We use a variety of marketing initiatives and

programs, including those that focus on customer value, with in-depth market segmentation; programs to promote customer loyalty; pricing initiatives aimed toward stimulating usage, including segmented packages and innovative tariff options; and initiatives that are responsive to the latest market trends, including those aimed toward boosting demand for our mobile Internet and mobile broadband offerings. In connection with these and our other sales and marketing initiatives, we market our products through a broad range of channels, including television, radio, billboards, telemarketing, direct mail and Internet advertising. We also sponsor a variety of local cultural and sporting events in order to enhance our brand recognition.

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Competition

The telecommunications industry is competitive and consumers generally have a choice of mobile and fixed line operators from which to select services. We are a global telecommunications services provider and face significant competition in most of the markets in which we operate. In Europe, our largest competitor is Vodafone and in Latin America, our largest competitor is América Móvil. Newer competitors, including handset manufacturers, MVNOs, internet companies and software providers, are also entering the market and offering integrated communications services.

We compete in our markets on the basis of the price of our services; the quality and range of features; the added value we offer with our service; additional services associated with those main services; the reliability of our network infrastructure and its technological attributes; and the desirability of our offerings, including bundled offerings of one type of service with another and, in the case of the mobile industry, in some of the markets offerings that include subsidized handsets.

To compete effectively with our competitors, we need to successfully market our products and services and to anticipate and respond to various competitive factors affecting the relevant markets, such as the introduction of new products and services, different pricing strategies and changes in consumer preferences. See “Risk Factors – Risks Relating by the Group’s Industry – The Group operates in a highly regulated industry which requires government concessions for the provision of a large part of its services and the use of spectrum, which is a scarce and costly resource.

Strategic Partnerships

China Unicom

Since 2005, we have had a stake in China Unicom and its predecessor company. On September 6, 2009 we entered into a strategic alliance agreement with China Unicom, which provides, among other areas for cooperation, joint procurement of infrastructure and client equipment, common development of mobile service platforms, joint provisions of service to multinational customers, roaming, research and development, sharing of best practices and technical, operational and management know-how, joint development of strategic initiatives in the area of network evolution, joint participation in international alliances and exchanges of senior management. In furtherance of this strategic alliance we entered into a subscription agreement with China Unicom, pursuant to which we increased our voting interest in the share capital of China Unicom to 8.06% and China Unicom obtained 0.87% voting interest in our share capital in October 2009.

Pursuant to the strategic alliance agreement mentioned above, China Unicom has agreed to use its best endeavors to maintain a listing of all the issued ordinary shares of China Unicom on the Hong Kong Stock Exchange. For so long as the strategic alliance agreement with us is in effect, China Unicom shall not (i) offer, issue or sell any significant number of its ordinary shares (including treasury shares), or any securities convertible into or other rights to subscribe for or purchase a significant number of China Unicom’s ordinary shares (including treasury shares), to any current major competitor of Telefónica or (ii) make any significant investment, directly or indirectly, in any current major competitor of Telefónica. We made similar undertakings.

The initial term of the strategic alliance agreement between us and China Unicom terminated on September 6, 2012 and it is subject to automatic annual renewals, subject to either party’s right to terminate on six months’ notice. Also,

the strategic alliance agreement may be terminated by China Unicom if our shareholding in China Unicom drops below 5% of its issued share capital or if China Unicom's shareholding in us drops below 0.5% of our issued share capital. In addition, the strategic alliance agreement is subject to termination in the event either party is in default and automatically terminates on a change in control of China Unicom.

On January 28, 2011, China Unicom completed its acquisition of 21,827,499 Telefónica shares.

On June 10, 2012, Telefónica, S.A. through its 100% subsidiary, Telefónica Internacional, S.A.U., and China United Network Communications Group Company Limited ("Unicom Parent") through a 100% owned subsidiary, signed an agreement for the acquisition by this last company of 1,073,777,121 shares of China Unicom-Hong Kong-Limited, owned by Telefónica, equivalent to 4.56% of the issued share capital of China Unicom.

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On July 21, 2012 the aforementioned agreement was complemented by a Supplemental Agreement which determined the acquisition of the shares at a price of HK\$10.02 per share, for a total amount of HK\$10,759,246,752.42 (approximately 1,142 million euros). The transaction was completed on July 30, 2012.

On November 10, 2014, Telefónica, through its 100% subsidiary, Telefónica Internacional, S.A.U., sold 597,844,100 shares of China Unicom, representing 2.5% of the share capital of the company, by means of a block trade, at a price of HK\$11.14 per share, for a total amount of HK\$6,660 million, approximately 687 million euros at the exchange rate as at the date of the sale.

Further to the sale, Telefónica maintains its commitment to the strategic alliance with China Unicom.

As of the date of this Annual Report, Telefónica's shareholding in China Unicom amounts 2.51% of its capital stock. Furthermore, Mr. César Alierta, chairman of Telefónica, S.A. is a member of the Board of Directors of China Unicom while Mr. Chang Xiaobing, chairman of China Unicom, is a member of the Board of Directors of Telefónica.

Telecom Italia

Through a series of transactions from 2007 to 2009, Telefónica acquired an indirect holding of 10.49% in the voting shares of Telecom Italia (7.21% of the dividend rights) through its holdings in Telco.

On June 16, 2014, the three Italian shareholders of Telco requested the initiation of the process of "demerger" (spin off) of the company, as provided in their shareholders agreement. Implementation of the demerger, approved by the General Meeting of Shareholders of Telco held on July 9, 2014, remains subject to obtaining the required anti-trust and telecommunications approvals (including those from Brazil and Argentina). Once the aforementioned approvals are obtained, this decision will be implemented by transferring all the current stake of Telco in Telecom Italia to four newly created companies. The share capital of each of these companies will belong in its entirety to each of the shareholders of Telco and each of these companies will receive a number of shares of Telecom Italia proportional to the current economic stake in Telco of each respective shareholder.

The application process of the aforementioned anti-trust and telecommunications approvals (including those in Brazil and Argentina) to proceed to the "demerger" (spin off) of Telco started, once the corresponding corporate documents were entered into in Italy. On December 22, 2014, Anatel gave its approval to the spin off, though CADE and Argentina are still analyzing the process.

Furthermore, on July 24, 2014, Telefónica issued 750 million euros bonds mandatorily exchangeable into ordinary shares of Telecom Italia maturing on July 24, 2017, representing, as of that date, 6.5% of its current voting share capital. The bonds may be exchanged in advance of the transfer of the shares, except under certain circumstances where the company may opt to redeem the bonds in cash. As a result of this transaction, Telefónica, after the Telco demerger and the later transfer of the underlying shares of the bonds, will reduce its stake in Telecom Italia which will be between 8.3% and 9.4% in Telecom Italia current voting share capital.

It is also significant that, within the framework of the GVT transaction (see "Item 4. Information on the Company—History and Development of the Company") on September 18, 2014, Vivendi, S.A. will acquire from Telefónica 1,110 million ordinary shares in Telecom Italia representing 8.3% of Telecom Italia's voting share capital (equivalent to 5.7% of its total share capital), in exchange for 4.5% of Vivendi, S.A.'s capital in Telefónica Brasil, S.A., after its combination with GVT (which represents all of the voting shares and 0.7% of the preferred shares to be received by Vivendi S.A. in connection with the GVT transaction). The final closing of the operation is subject to obtaining the relevant regulatory authorizations (including telecommunication and anti-trust approval).

The Telecom Italia group is principally engaged in the communications sector and, particularly, in telephone and data services on fixed lines for final and wholesale customers, in the development of fiber optic networks for wholesale customers in the provision of broadband services and Internet services, in domestic and international mobile telecommunications (especially in Brazil), in the television sector using both analog and digital terrestrial technology and in the office products sector. Telecom Italia operates primarily in Europe, the Mediterranean basin and in South America.

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For more information, please see “Item 5. Operating and Financial Review and Prospects —Operating Results—Significant Factors Affecting the Comparability of our Results of Operations in the Period Under Review” and “Item 10. Additional Information—Material Contracts.” Telco, through which we hold our stake in Telecom Italia, is included in our Consolidated Financial Statements using the equity method.

Regulation

Please see Appendix VII to our Consolidated Financial Statements.

Licenses and Concessions

Please see Appendix VII to our Consolidated Financial Statements.

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.

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Disclosure Pursuant to Section 219 of the Iran Threat Reduction and Syria Human Rights Act

Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012 added Section 13(r) to the Exchange Act. Section 13(r) requires an issuer to disclose in its annual or quarterly reports filed with the SEC whether the issuer or any of its affiliates has knowingly engaged in certain activities, transactions or dealings with the Government of Iran, relating to Iran or with designated natural persons or entities involved in terrorism or the proliferation of weapons of mass destruction during the period covered by the annual or quarterly report. Disclosure is required even when the activities were conducted outside the United States by non-U.S. entities and even when such activities were conducted in compliance with applicable law.

The following information is disclosed pursuant to Section 13(r). None of these activities involved U.S. affiliates of Telefónica.

Roaming Agreements

Various of our subsidiaries have entered into roaming agreements with Iranian telecommunication companies, certain of which are or may be owned or controlled by the government of Iran. Pursuant to such roaming agreements our subsidiaries' customers are able to roam in the particular Iranian network (outbound roaming) and customers of such Iranian operators are able to roam in our relevant subsidiary's network (inbound roaming). For outbound roaming, our subsidiaries pay the relevant Iranian operator roaming fees for use of its network by our customers, and for inbound roaming the Iranian operator pays the relevant subsidiary roaming fees for use of its network by its customers.

Our subsidiaries were party to the following roaming agreements with Iranian telecommunication companies in 2014:

- (1) Telefónica Móviles España ("TME"), our Spanish directly wholly-owned subsidiary, has respective roaming agreements with (i) Mobile Telecommunication Company of Iran ("MTCI"), (ii) MTN Irancell ("Irancell"), (iii) Taliya ("Taliya") and (iv) Telecommunications Kish Co. ("TKC").

During 2014, TME recorded the following revenues related to these roaming agreements: (i) 20,337.27 euros from MTCI, (ii) 3,290.74 euros from Irancell, (iii) none from Taliya and (iv) none from TKC.

TME also holds a Roaming Hub agreement through its 55% directly-owned subsidiary, Link2One, a.e.i.e. ("L2O"). Under this agreement, L2O provides a roaming hub service to Irancell enabling the latter to maintain a relationship with other members of the hub. Some members of the hub are also entities of the Telefónica Group. Under this roaming hub service, for 2014, L2O has billed Irancell 114,428.69 euros.

- (2) Telefónica Germany GmbH & Co. OHG ("TG"), our German 62.37% indirectly-owned subsidiary, has a roaming agreement with MTCI. TG recorded 156,966.00 euros in roaming revenues under this agreement in 2014.
- (3) Telefónica Brasil ("TB"), our Brazilian 73.96% indirectly owned subsidiary, has a roaming agreement with Irancell. TB recorded 0.90 U.S. dollars in roaming revenues under this agreement in 2014.
- (4) Telefónica UK Ltd ("TUK"), our English directly wholly-owned subsidiary, has a roaming agreement with Irancell. TUK recorded 1,558.34 euros in roaming revenues under this agreement in 2013.
- (5) Pegaso Comunicaciones y Sistemas, S.A. de C.V. ("PCS"), our Mexican directly wholly-owned subsidiary, has a roaming agreement with Irancell. PCS recorded no revenues under this agreement in 2014.

- (6)Telefónica Argentina, S.A. and Telefónica Móviles Argentina, S.A. (together TA), our Argentinean directly wholly-owned subsidiaries, have a roaming agreement with Irancell. TA recorded 43.96 U.S. dollars in roaming revenues under this agreement in 2014.
- (7)Telefónica Celular de Nicaragua, S.A. (“TCN”), our Nicaraguan 60% indirectly-owned subsidiary, has a roaming agreement with Irancell. TCN recorded no revenues under this agreement in 2014.
- (8)E-Plus Mobilfunk GmbH& Co. KG (“E-Plus”), our German 100% indirectly-owned subsidiary, has respective roaming agreements with MTCI, Irancell and Taliya. During 2014, E-Plus recorded the following revenues related to these roaming agreements: 1,415 euros from Irancell and none from Taliya.

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The net profit recorded by our subsidiaries pursuant to these agreements did not exceed the related revenues recorded thereunder.

The purpose of all of these agreements is to provide our customers with coverage in areas where we do not own networks. For that purpose, we intend to continue maintaining these agreements.

International Carrier Agreement

Telefónica de España has an international carrier agreement with Telecommunication Company of Iran (“TCI”).

Pursuant to this agreement, both companies interconnect their networks to allow international exchange of telephone traffic. Telefónica de España recorded 10,594 euros in revenues under this agreement in 2014. The net profit recorded by Telefónica de España pursuant to this agreement did not exceed such revenues.

The purpose of this agreement is to allow exchange of international telephone traffic. Consequently, we intend to continue maintaining this agreement.

C. Organizational Structure

See “—History and Development of the Company” and “—Business Overview.”

D. Property, Plant and Equipment

Our central headquarters for the Telefónica Group are located in “Distrito Telefónica,” in Madrid, Spain.

Fixed Networks

We own fixed networks in Spain, Latin America and Europe, having an incumbent role in Spain, Argentina (the greater Buenos Aires metropolitan area and the southern portion of the country), Brazil (São Paulo), Chile, Peru and Colombia.

Following market trends, competitive environments, evolution of technologies and new multimedia and broadband services demanded by our customers, we have upgraded our networks in recent years in the following manners:

- progressive introduction of broadband access technologies over copper: ADSL, ADSL2+, VDSL2, etc., increasing the bandwidth capacity provided to our broadband clients several times in the last ten years;
- introduction of fiber access technologies (xPON) across different deployment scenarios: fiber to the home (FTTH), fiber to the building (FTTB), fiber to the curb (FTTC), fiber to the node (FTTN), etc., increasing the access speed up to 100 Mbps;
- service support based on powerful Internet Protocol/ Multiprotocol Label Switching (IP/MPLS) backbones, providing full connectivity to the rest of the network layers, such as access and control, to support services for business and customer market segments (fixed and mobile);
- migration of the legacy time division multiplexing (TDM) switching networks (PSTN and ISDN) to new generation network (NGN) over all-IP packet networks;

- migration from legacy transport technologies, such as asynchronous transfer mode (ATM), frame relay (FR), low-rate leased lines, plesiochronous digital hierarchy (PDH) and synchronous digital hierarchy (SDH), to the new generation of optical transport ones, such as dense wavelength division multiplexing (DWDM), coarse wavelength division multiplexing (CWDM) and new generation-synchronous digital hierarchy (NG-SDH);
- introduction of IMS (Internet Multimedia Subsystem) in many countries to simplify the control of the network and ease the deployment of new services over the all-IP converged network;

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- empowerment of the intelligence of the network to better manage its use, to avoid saturations and frauds and to identify new business opportunities;
- convergence of fixed and mobile networks, services and support systems from both technological and operational points of view; and
- deployment of new services such as Pay-TV, to customers connected through broadband accesses in Spain, Germany, Chile and Brazil.

Mobile Networks

We operate mobile networks in Spain, the United Kingdom, Germany, Brazil, Argentina, Venezuela, Chile, Peru, Colombia, Mexico, Guatemala, Panama, El Salvador, Nicaragua, Costa Rica, Ecuador and Uruguay.

We use a number of mobile technologies in the countries in which we operate, namely: GSM and UMTS in Spain, the United Kingdom, Germany, and Latin America; and LTE in Germany, Spain, the United Kingdom, Brazil, Chile, Colombia, Peru, Mexico and Uruguay. We continue the work of upgrading our mobile networks in line with market trends, the demand of new services from customers and the evolution of technologies. The main steps we are currently taking include:

- evolution of broadband into mobile access using technologies such as UMTS, HSDPA, HSUPA/HSPA+ and LTE;
- deployment of new services such as mobile television and distribution services for next generation music, video and games;
- exploration of the adequacy of new technologies such as HSPA and LTE to provide mobile accesses with increased bandwidth, in particular:
 - HSPA: we have extended our coverage up to the majority of the urban/suburban areas, and we have increased the capacity of the network by upgrading the network technology to the latest available releases of UMTS standards 3GPP REL 6, REL 7 and REL 8;
 - LTE: together with main vendors and sharing experience with other operators, we have extensively analyzed the opportunities that LTE will bring, as 4G mobile technology is used to complement current network technology by creating higher capacity at lower relative cost by user/traffic unit. In this regard, during 2014 we have extended the commercial operations with this technology in Germany, Spain, the United Kingdom, Brazil and Chile, and started to offer commercial service in Colombia, Peru, Mexico and Uruguay, while we have continued extensive trials in in the rest of Latin America with the objective of launching LTE services during 2015 in more countries.
 - convergence of fixed and mobile networks, services and support systems from both technological and operational points of view.

Satellite communications

The services provided using satellite platforms include television contribution signal to feed cable and IPTV head ends, DTH television, VSAT mainly for telephony and Internet access in rural areas, emergency solutions, corporate communications and international communications.

Submarine cables

We are one of the world's largest submarine cable operators. We participate in approximately 25 international underwater cable systems (nine of which are moored in Spain) and own eleven domestic fiber optic cables.

There are submarine cable connections between Spain and Africa, America, Asia and Europe, respectively, which are jointly owned by us with other telecom operators. The SAM-1 cable, which we own, has a length of approximately 22,000 kilometers underwater and 3,000 kilometers terrestrial and links different countries such as the United States, Puerto Rico, Ecuador, Guatemala, Peru, Chile, Brazil, Argentina and Colombia.

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The principal services using the capacity of submarine cables are voice circuits, Internet and dedicated circuits for international traffic and for corporations and business customers.

Item 4A. Unresolved Staff Comments

Not applicable.

Item 5. Operating and Financial Review and Prospects

A. Operating Results

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 IFRS as issued by the IASB.

On February 26, 2014, the Board of Directors of Telefónica, S.A. approved the implementation of a new organizational structure focused on clients and which incorporates the digital offering as the main focus for commercial policies. The structure gives greater visibility to local operators, bringing them closer to the corporate decision-making center, simplifying the Group's global structure and strengthening the cross-cutting areas to improve flexibility and agility in decision making.

Within this framework, Telefónica has created the role of the Chief Commercial Digital Officer, who is responsible for fostering revenue growth. On the cost side, the Company has strengthened the role of the Chief Global Resources Officer. Both Officers report directly to the Chief Operating Officer (COO), as well as the local operators in Spain, Brazil, Germany and the United Kingdom, in addition to the Hispanoamérica unit (which now excludes Brazil).

Due to the implementation of this new organizational structure, from the beginning of 2014, the new organizational structure is composed of Telefónica Spain, Telefónica United Kingdom, Telefónica Germany, Telefónica Brazil and Telefónica Hispanoamérica (comprised of Argentina, Chile, Peru, Colombia, Mexico, Venezuela & Central America, Ecuador and Uruguay). All that is not specifically included in these new segments is part of "Other companies and eliminations". As a result, the Group's segment results have been revised for the year 2012 and 2013 to reflect the above-mentioned new organization. Because this is an intragroup change, Telefónica's consolidated results for 2012 and 2013 are not affected.

Additionally, as a result of management integrations undertaken in Peru, Argentina and Chile, the revenue breakdown has been reclassified, allocating "inter-company" eliminations within fixed and mobile businesses.

Non-GAAP financial information

Operating income before depreciation and amortization

Operating income before depreciation and amortization, or OIBDA, is calculated by excluding depreciation and amortization expenses from our operating income 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 OIBDA 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. OIBDA also allows us to compare our results with those of other companies in the telecommunications sector without considering their asset structure. We use OIBDA to track our business evolution and establish operational and strategic targets. OIBDA is also a measure commonly reported and

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widely used by analysts, investors and other interested parties in the telecommunications industry. OIBDA is not an explicit measure of financial performance under IFRS and may not be comparable to other similarly titled measures for other companies. OIBDA should not be considered an alternative to operating income 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 our OIBDA to operating income for the periods indicated.

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Year ended December 31,

Millions of euros	2012	2013	2014
Operating income before depreciation and amortization	21,231	19,077	15,515
Depreciation and amortization expense	(10,433)	(9,627)	(8,548)
Operating income	10,798	9,450	6,967

The following tables provide a reconciliation of OIBDA to operating income for us and each of our business areas for the periods indicated.

2014

Millions of euros	Telefónica Spain	Telefónica United Kingdom	Telefónica Germany	Telefónica Brazil	Telefónica Hispano américa	Other companies and eliminations	Total Group
Operating income before depreciation and amortization	5,671	1,744	733	3,543	4,068	(244)	15,515
Depreciation and amortization expense	(1,805)	(1,121)	(1,426)	(1,762)	(2,034)	(400)	(8,548)
Operating income	3,866	623	(693)	1,781	2,034	(644)	6,967

2013

Millions of euros	Telefónica Spain	Telefónica United Kingdom	Telefónica Germany	Telefónica Brazil	Telefónica Hispano américa	Other companies and eliminations	Total Group
Operating income before depreciation and amortization	6,340	1,637	1,308	3,940	5,531	321	19,077
Depreciation and amortization expense	(1,903)	(1,016)	(1,231)	(2,109)	(2,524)	(844)	(9,627)
Operating income	4,437	621	77	1,831	3,007	(523)	9,450

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2012

Millions of euros	Telefónica Spain	Telefónica United Kingdom	Telefónica Germany	Telefónica Brazil	Telefónica Hispano américa	Other companies and eliminations	Total Group
Operating income before depreciation and amortization	6,815	1,602	1,351	5,161	5,983	319	21,231
Depreciation and amortization expense	(2,063)	(995)	(1,233)	(2,318)	(2,762)	(1,062)	(10,433)
Operating income	4,752	607	118	2,843	3,221	(743)	10,798

Net financial debt and net debt

We calculate net financial debt by deducting the positive mark-to-market value of derivatives with a maturity beyond one year from the relevant balance sheet date and other interest-bearing assets (each of which are components of non-current financial assets and trade and other receivables in our consolidated statement of financial position), current financial assets and cash and cash equivalents from the sum of (i) current and non-current interest-bearing debt (which includes the negative mark-to-market value of derivatives with a maturity beyond one year) and (ii) other payables (a component of current and non-current trade and other payables in our consolidated statement of financial position). We calculate net debt by adding to net financial debt those commitments related to employee benefits. We believe that net financial debt and net debt are meaningful for investors because they provide an analysis of our solvency using the same measures used by our management. We use net financial debt and net debt to calculate internally certain solvency and leverage ratios used by management. Neither net debt nor net financial debt as calculated by us should be considered an alternative to gross financial debt (the sum of current and non-current interest-bearing debt) as a measure of our liquidity.

The following table provides a reconciliation of our net financial debt and net debt to gross financial debt at the dates indicated:

Millions of euros	12/31/2014	12/31/2013	12/31/2012
Non-current interest-bearing debt	50,688	51,172	56,608
Current interest-bearing debt	9,094	9,527	10,245
Gross financial debt	59,782	60,699	66,853
Non-current trade and other payables	1,276	1,145	1,639
Current trade and other payables	210	99	145
Non-current financial assets	(6,267)	(4,468)	(5,605)
Trade and other receivables	(453)	–	–
Current financial assets	(2,932)	(2,117)	(1,926)
Cash and cash equivalents	(6,529)	(9,977)	(9,847)
Net financial debt	45,087	45,381	51,259
Net commitments related to employee benefits	1,976	2,270	2,036
Net debt	47,063	47,651	53,295

Significant Factors Affecting the Comparability of our Results of Operations in the Periods Under Review

Please see “Comparative information and main changes in the consolidation scope” in Note 2 to our Consolidated Financial Statements.

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Significant Changes in Accounting Policies

Please see Note 3(n) to our Consolidated Financial Statements.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the amounts reflected in the Consolidated Financial Statements and accompanying notes. We base our estimates on historical experience, where applicable, and other assumptions that we believe are reasonable under the circumstances. Actual results may differ from those estimates under different assumptions or conditions.

We consider an accounting estimate to be critical if:

- it requires us to make assumptions because information was not available at the time or it included matters that were highly uncertain at the time we were making our estimate; and
- changes in the estimate or different estimates that we could have selected may have had a material impact on our financial condition, results of operations or cash flows.

The various policies that are important to the portrayal of our financial condition, results of operations and cash flows include:

- accounting for long-lived assets, including goodwill;
 - deferred taxes;
 - provisions;
 - revenue recognition; and
- exchange rate used to remeasure Venezuelan bolívar fuerte (BsF)-denominated items.

Accounting for long-lived assets, including goodwill

Property, plant and equipment and intangible assets, other than goodwill, are recorded at acquisition cost. If such assets are acquired in a business combination, the acquisition cost is the estimated fair value of the acquired property, plant and equipment or intangible assets. Property, plant and equipment and intangible assets with definite useful lives are depreciated or amortized on a straight-line basis over their estimated useful lives.

Intangible assets with indefinite useful lives are not amortized, but are, instead, subject to an impairment test on a yearly basis and whenever there is an indication that such assets may be impaired.

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. We believe that the estimates we make to determine an asset's useful life are "critical accounting estimates" because they require our management to make estimates about technological evolution and competitive uses of assets.

When an impairment in the carrying amount of an asset occurs, non-scheduled write-downs are made. We perform impairment tests of identifiable intangible and long-lived assets whenever there is reason to believe that the carrying value may exceed the recoverable amount, which is the higher of the asset's fair value less costs to sell and its value in use. Furthermore, previously recognized impairment losses may be reversed when changes in the estimates used to determine the asset's recoverable amount indicate that an impairment loss recognized in prior periods no longer exists or may have decreased.

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The determination of whether the impairment of long-lived and intangible assets is necessary involves the use of significant estimates and judgment that includes, but is 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, which requires the estimation of the future expected cash flows, discount rates and the fair value of the assets.

Specifically, management has to make certain assumptions in respect of uncertain matters, such as growth in revenues, changes in market prices, operating margins, and technology developments and obsolescence, discontinuance of services and other changes in circumstances that indicate the need to perform an impairment test. Management's estimates about technology and its future development require significant judgment because the timing and nature of technological advances are difficult to predict.

Goodwill arises when the cost of a business combination exceeds the acquirer's interest in the net fair value of the identifiable assets acquired and liabilities assumed at the acquisition date. Goodwill is not amortized, but is, instead, subject to an impairment test on a yearly basis and whenever there is an indication that the goodwill may be impaired.

Non-scheduled write-downs of goodwill are made when an impairment in the carrying amount of goodwill occurs. We review, on a regular basis, the performance of our cash-generating units. We compare the carrying amount of the cash-generating unit to which the goodwill has been allocated with its recoverable amount. The determination of the recoverable amount of the cash-generating unit 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 change in the facts and circumstances that we relied upon in making our estimates may have a material impact on our operating results and financial condition.

Deferred taxes

Management assesses the recoverability of deferred tax assets on the basis of estimates of our future taxable profit. The recoverability of deferred tax assets ultimately depends on our ability to generate sufficient taxable profit during the periods in which the deferred tax assets are utilized. In making this assessment, our management considers the scheduled reversal of deferred tax liabilities, projected taxable profit 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 for all deductible temporary differences and for the carry-forward of unused tax credits and unused tax losses to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized. Our current and deferred income taxes 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 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.

Provisions

Provisions are recorded when, at the end of the period, we have a present obligation as a result of past events, whose settlement requires an outflow of resources that is considered probable and can be measured reliably. This obligation may be legal or constructive, arising from, but not limited to, regulation, contracts, common practice or public commitments, which have created a valid expectation for third parties that we will assume certain responsibilities. The

amount recorded is the best estimation performed by the management in respect of the expenditure that will be required to settle the obligations, considering all the information available at the closing date, including the advice of external experts, such as legal advisors or consultants.

If we are unable to reliably measure the obligation, no provision is recorded and information is then presented in the notes to the Consolidated Financial Statements.

Because of the inherent uncertainties in this estimation, actual expenditures may be different from the originally estimated amount recognized.

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Revenue recognition

Connection fees

Revenues from connection fees originated when customers connect to our network are deferred over the average expected length of the customer relationship.

The expected customer relationship period is estimated based on recent historical experience of customer churn rates. Significant changes in our estimations may result in differences in the amount and timing of revenues recognized.

Multiple-element arrangements

Arrangements involving the delivery of bundled products or services are assessed to determine whether it is necessary to separate the arrangement into individual component deliverables, each with its own revenue recognition criteria.

Revenue relating to the bundled contracts is allocated to the different deliverables identified, based on their relative fair values (i.e., the fair value of each individual component deliverables in relation to the total fair value of the bundled deliverables), considering that amounts contingent upon delivery of undelivered items are not allocated to delivered items. Given that the handsets and airtime are price-sensitive and volatile in a competitive marketplace, the determination of fair values in the mobile phone business is quite complex.

Additionally, a significant change in the facts and circumstances upon which we based our fair value estimates may have an impact on the allocation of revenues among the different deliverables identified and, consequently, on future revenues.

Exchange rate used to remeasure the financial statements of our Venezuelan subsidiaries

As of December 31, 2014, there are multiple exchange mechanisms and published exchange rates potentially available to remeasure BsF-denominated items and transactions in the financial statements of the Group's Venezuelan subsidiaries.

We review, on a regular basis, the economic conditions in Venezuela and the specific circumstances of our Venezuelan operations. Assessment of the exchange rate that better reflects the economics of Telefónica's business activities in Venezuela relies on several factors and is performed considering all the information available at the closing date, involving the use of estimates, where significant management judgment is required.

Because of the inherent uncertainties in the estimations required to determine the appropriate exchange rate for the conversion of BsF-denominated financial statements, actual cash flows denominated in such currency may differ from the amounts originally recognized on the basis of our estimations, as a result of changes in currency laws or changes in exchange mechanisms or published exchange rates that may have a material impact on the conversion rate to be used for our Venezuelan subsidiaries' financial statements, affecting the net monetary position of assets (liabilities) denominated in BsF.

Operating Environment

Our results of operations are dependent, to a large extent, on the level of demand for our services in the countries in which we operate. Demand for services in those countries is affected by the performance of their respective economies, particularly household private consumption, but also gross domestic product, or GDP, inflation, or CPI,

external accounts and unemployment rates.

During 2014, global activity picked up and recent developments suggest that this process may consolidate along 2015. The European Union is showing signs of turning the corner from recession to recovery due to the improvement of internal demand, especially in Spain and in the United Kingdom.

In Latin America, economic growth in 2015 is expected to be higher than in 2014, although the growth rates are expected to be significantly lower than those achieved before the recession. Moreover, commodity prices, especially oil, are expected to pose downward risks to the external accounts balances and to activity growth in the region. Additionally, a faster monetary normalization in the United States could have an impact on inward external flows, making financing conditions in Latin American countries more stringent, which would affect household private consumption negatively.

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Operating environment by country

Spain

In 2014, Spanish GDP expanded by 1.2% (according to Consensus Economics Forecast (“CFe”), an independent research firm), compared with a positive average annual growth rate of 3.6% in the period 1998 through 2008 and a contraction on average of 1.3% in 2009-2013.

This performance was explained by a positive evolution of internal demand, with household consumption increasing 2.0% according to CFe in 2014 compared with a negative annual rate of -2.0% during 2009-13 and compared with average growth of 3.6% during the period 1998 through 2008.

Investment grew at an annual rate of 0.8% (CFe) during 2014, after a 8.2% decline on average in 2009-13, compared with average annual growth of 5.6% during the period 1998 through 2008. Inflation was -1.0% in 2014, compared with 0.3% and 3.0% in 2013 and 2012, respectively.

The current account surplus for 2014 was 0.4% of GDP (CFe), compared with 1.5% of GDP in 2013 and -3.1% on average in 2009 through 2012.

The unemployment rate reached 24.6% at the end of 2014, higher than the average rate of 21.2% in 2009-12, but less than the 26.1% reached in 2013.

United Kingdom

In 2014, the British economy, measured in terms of GDP, grew by 3.0% compared with a growth rate of 1.7% in 2013 and 0.7% in 2012.

Fixed capital investment increased by 8.1% in 2014, compared with an increase of 3.2% in 2013. Private consumption grew by 2.4%, compared with a growth rate of 1.6% and 1.1% in 2013 and 2012, respectively.

The CPI increased by 0.5% in 2014, compared with 2.0% in 2013 and 2.7% in 2012. It is the lowest CPI figure since August 2000.

The positive performance of economic growth has had a favorable impact on the unemployment rate, which reached 6.2% in 2014 (CFe) on average, compared with an average annual rate of 7.6% in 2013 and 8.0% in 2012.

Germany

In 2014, the German economy grew 1.4%, after growing 0.1% in 2013 and 0.4% in 2012.

The economic growth recovery in 2014 was mainly due to a positive contribution of the internal demand, which offset the negative contribution of the external sector to GDP growth (exports increased just 3.5% while imports grew 4.5%, CFe).

In December 2014 the CPI rate reached 0.2% year-on-year (compared with 1.4% in 2013 and 2.0% in 2012), and the unemployment rate stood at 6.4%, compared with 6.9% in 2013 and 6.8% in 2012.

Brazil

Brazilian GDP increased approximately 0.2% in 2014 (CFe), following increases of 2.5% in 2013 and 1.0% in 2012, according to the Brazilian Geography and Statistics Institute. Investments contracted by approximately 6.4% in 2014, after an increase of 5.2% in 2013. Household consumption growth decelerated to approximately 1.5% in 2014, from 2.6% in 2013.

Inflation, as measured by the CPI, increased by 6.4% in 2014 (above the inflation target established by the Brazilian Central Bank of 4.5%, but within its range of tolerance), compared to 5.9% in 2013 and 5.8% in 2012. Due to increasing inflation, the basic interest rate, the Special Clearance and Escrow System rate (Selic rate), was raised from 10% at the end of 2013 to 11.75% at the end of 2014.

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The current account deficit reached 90.9 billion U.S. dollars in 2014, compared to 81.4 billion U.S. dollars in 2013 and 54.2 billion U.S. dollars in 2012. The deficit observed in 2014 was partially financed by capital inflows, such as foreign direct investments, of 62.4 billion U.S. dollars, and portfolio investments, of 26.5 billion U.S. dollars. International reserves decreased by 1.7 billion U.S. dollars in 2014, to a level of 374.1 billion U.S. dollars.

With the worsening of most domestic economic data, especially those regarding government accounts, the country risk increased. The J.P. Morgan Emerging Markets Bond Index Plus (EMBI + Brazil) reached 259 basis points at the end of 2014, down from 224 basis points at the end of 2013 and 142 basis points at the end of 2012.

The Brazilian real continued to depreciate in 2014. The Brazilian real depreciated against the U.S. dollar by 13.4% in 2014, reaching an exchange rate of 2.66 reais per 1 U.S. dollar on December 31, 2014, compared to 2.34 reais per 1 U.S. dollar on December 31, 2013 and to 2.04 reais per 1 U.S. dollar on December 31, 2012.

Mexico

Mexico's real GDP increased by an estimated 2.3% in 2014 (CFe), compared with a 1.7% and 3.7% growth in 2013 and 2012, respectively.

Inflation, as measured by the CPI, was 4.1% year-on-year in December 2014 compared with 4.0% in December 2013, above the Mexican Central Bank's target of 3% and also outside its tolerance range of 2% to 4%.

During 2014, aggregate demand in Mexico has continued to show the stabilizing trend that began in 2010, following the harsh economic downturn suffered in 2009. Exports increased by more than 5.5%, private consumption increased by almost 2.2% and investment increased by 2.0% compared with 2013.

The current account balance posted a deficit of 25.2 billion U.S. dollars in 2014 –according to CFe- compared with 26.5 billion U.S. dollars in 2013 (1.9% and 2.1% of GDP, respectively).

On December 31, 2014, the exchange rate relative to the U.S. dollar was 14.83 Mexican pesos to the U.S. dollar (13.08 and 12.87 on December 31, 2013 and 2012 respectively).

Venezuela

Venezuela is officially in an economic crisis, as GDP during the first three quarters of 2014 decreased on average by 4%, after a positive growth of 1.3% in 2013 and 5.6% in 2012. The oil sector expanded slightly by 0.3% and the non-oil sector fell by 3.8%. Nonetheless there were some sectors that showed growth in this period. For instance, banking and insurance (13.2%), communications (4.1%) and government services (1.7%).

Consumption fell 2.5% year-on-year on average in the first three quarters of 2014 (compared to an increase of 4.4% in 2013 and 6.9% in 2012). Despite the higher inflation, public consumption grew only by 0.8% (compared to growth of 3.3% in 2013 and 6.3% in 2012) while the private sector contracted by 3.3% (compared to a positive growth of 4.7% in 2013 and 7.0% in 2012) and investments declined by 17.9% (compared to a decrease of -9.0% in 2013 and a positive growth of 23.3% in 2012).

Additionally exports declined by 9.5% (compared to a decrease of -8.6% in 2013 and positive growth of 4.9% in 2012), and imports contracted by 19.0% (compared to a decrease of 10.6% in 2013 and positive growth of 26.8% in 2012). During 2014, exports were negatively impacted by the downfall of oil prices and oil production, but imports decreased to a larger extent due to the economic crisis that the country is facing. As a result, the current account

surplus was higher in 2014 than in 2013, reaching 9.9 billion U.S. dollars in the first nine months of 2014, compared with 4.9 billion U.S. dollars in the first nine months of 2013.

Also, the capital account deficit reached 7.5 billion U.S. dollars in the first nine months of 2014, compared with a deficit of 5.9 billion U.S. dollars in the same period of 2013. This performance diminished the Venezuelan Central Bank's stock of international reserves to 22.06 billion U.S. dollars at the end of September 2014 compared with 21.48 billion U.S. dollars at the end of December 2013.

In terms of inflation, the national CPI reached 63.6% year-on-year in November 2014 (compared to 56.2% year-on-year in December 2013 and 20.1% year-on-year in December 2012). Venezuela still has the highest inflation rate in Latin America.

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The unemployment rate reached 5.9% as of November of 2014, compared to 5.6% at the end of 2013 and 5.9% at the end of 2012.

Chile

Chilean GDP expanded moderately at an estimated rate of 1.9% (CFe), the lowest since the recession of 2009 and 3.4 percent points under the average annual growth rate for the 2010-2013 period (5.3%). Private consumption slowed down and grew by an estimated 1.8% compared with 5.6% in 2013 and 6.0% in 2012. Investment, in turn, is estimated to have contracted for the first time since 2009. As most emerging economies, Chile faced headwinds from the international financial markets tightening, the decreasing commodity prices (especially copper prices) and the emerging/advanced capital flows reallocation. Domestically, a persistent slack of confidence and decreasing expectations also weighed negatively on expenditure decisions.

The labor market was substantially resilient to the economic underperformance and the unemployment rate increased from an average of 6.0% in 2013 to 6.5% in 2014 -CFe- (among the lowest unemployment rates in the last decade). Nominal wages rose at increasing rates during the year; in part, to compensate the loss in purchasing power due to the higher inflation.

Inflation, measured by CPI, reached 4.6% in 2014 compared with 3.0% in 2013 and 1.5% in 2012. Inflation gained momentum as the local currency depreciated at a faster pace, as supply shocks temporally hit prices of certain food items and as additional or higher specific taxes rates were applied to alcoholic beverages, cigarettes, sodas and new cars, among other items. While the fall in international oil prices decreased inflation pressures in the last part of the year, general and core inflation closed 2014 well above the Central Bank's monetary policy target range (between 2% and 4%).

The Chilean Central Bank reduced its interest key rate 25 basis points six times during the year in response to less dynamic economic activity and falling expectations. The Monetary Policy Rate closed at 3.00% in 2014. The fiscal deficit reached 1.5% of GDP, compared to a deficit of 0.6% in 2013 and a surplus of 0.6% in 2012. The trade balance surplus increased from 2.2 billion U.S. dollars in 2013 to 8.6 billion U.S. dollars in 2014 due to a fall in imports caused by the economy's slowdown.

At the end of 2014, the nominal exchange rate was 607.4 Chilean Pesos per U.S. dollar, reflecting a year-over-year Chilean Peso depreciation of 16.0%. The exchange rate performance in 2014 was mainly explained by the opposing policy decisions adopted in the United States and Chile, with the former being expected to raise interest rates in the short term and the latter loosening its monetary policy stance. The decrease in copper prices also contributed to the Chilean Peso depreciation, although the impact of copper prices was less significant than in other times.

In 2014 a tax reform which aims to increase annual taxation by 3 percent points of GDP was approved. These additional resources will be used mainly to finance the upcoming educational reform (1.5% of GDP), to improve the scope of current social policies (0.5% of GDP) and to close the structural fiscal gap (1% of GDP). The reform introduces substantial changes to the Chilean tax system, including two alternative methods for computing shareholder-level income taxation, additional corporate tax rate increases, important amendments to the thin capitalization rules, and other substantial modifications.

Argentina

Argentina's GDP decreased by an estimated 1.1% in 2014 (CFe). This data is much lower than the average annual growth rates of approximately 8.5% achieved from 2003 through 2008, and 5.3% from 2009 to 2012.

The Argentine peso depreciated 29.8% relative to the U.S. dollar, closing at 8.46 Argentine pesos per U.S. dollar at the end of 2014 compared with 6.51 Argentine pesos per U.S. dollar at the end of 2013 and 4.91 Argentine pesos per U.S. dollar at the end of 2012.

The official CPI increased 23.9% in 2014 (compared with 11.0% in 2013 and 10.8 % in 2012).

The expected current account deficit of 5.2 billion U.S. dollars in 2014 is the highest deficit in the last decade. The trade balance contributed significantly to this result, even when exports decreased less than imports during the year (7.3 % and 8.3% respectively).

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Economic conditions affected the unemployment rate negatively, which increased to 7.7% in 2014 from 7.1% in 2013 and 7.2% in 2012.

Colombia

During 2014, the economy showed strong growth which remained supported by private consumption and good performance of investments (with the recovery of construction and better dynamism of civil construction works). However, exports showed a slight slowdown as a result of lower external demand and some supply shocks, and industrial production remained weak throughout the year. GDP is estimated to have grown nearly 4.9% (CFe) in 2014 (compared with 4.7% in 2013).

Employment during 2014 showed a significant recovery. The unemployment rate averaged 9.0% in 2014 compared with 9.7%, 10.4% and 10.8% in 2013, 2012 and 2011, respectively.

According to CFe, the balance of payments registered a current account deficit of 16.3 billion U.S. dollars, 4.2% of GDP, compared with 3.2% of GDP in 2013, and 3.1% of GDP in 2012.

Amid expectations of withdrawal of monetary stimulus by the Federal Reserve in the United States and a continuous and sharply decrease in oil prices, the Colombian peso depreciated 23.0% during 2014 against the U.S. dollar (closing the year at 2,455.3 Colombian pesos per one U.S. dollar).

The inflation rate was 3.7% year-on-year at the end of 2013, compared with 1.9% and 2.4% at the end of 2013 and 2012, respectively.

Peru

After four years of strong GDP growth (5.8% in 2013, 6.0% in 2012, 6.5% in 2011 and 8.5% in 2010), the Peruvian economy posted a sharp slowdown to a growth of 2.9% in 2014 (CFe). The main drivers of the slowdown were weak investment (both private and public) and exports (lower ore grades in key mines). Investment and exports are expected to post a contraction in 2014. On the other hand, strong private consumption was the main contributor to growth. El Niño-like climate anomalies during 2014 hurt output from fishing and agriculture, which, combined with the weakness in mining, turned into a contraction of primary GDP, while services and commerce sustained a strong pace of growth.

Consumer prices, as measured by the CPI, increased by 3.2% in 2014, slightly over the range of the Peruvian Central Bank's target (between 1% and 3%), compared with 2.9% in 2013 and 2.6% in 2012. Inflation gained momentum affected by climate changes and currency depreciation.

The Peruvian Central Bank cut its interest key rate by 50 basis points to 3.5%, and the reserve requirement deposits rate, from 15% to 9.5%, showing an explicit easing bias.

Due to a positive fiscal impulse, the government budget is likely to post a small deficit for 2014, compared with a fiscal surplus of 0.9% in 2013 and around 2.0% in 2012.

In the foreign exchange market, the Peruvian Nuevo Sol weakened 6.4 % against the U.S. dollar in 2014, reaching 2.98 Peruvian Nuevo Sol per U.S. dollar at the end of the year, compared with a depreciation of 9.6% in 2013 and an appreciation of 5.4% against the U.S. dollar in 2012. The large commercial deficit and slower financial capital inflows lead to a reduction of international net reserves, reaching 62.3 billion U.S. dollars compared to 65.7 billion U.S.

dollars in 2013 and 64.0 billion U.S. dollars in 2012.

Country risk, measured by the J.P. Morgan Emerging Markets Bond Index (EMBIG Peru), rose 20 basis points to 162 basis points, in 2014. Long-term sovereign debt is currently investment grade rated by Fitch, Standard and Poor's and Moody's rating agencies.

Exchange Rate Fluctuations

We publish our Consolidated Financial Statements in euros. Because a substantial portion of our assets, liabilities, revenues and expenses are denominated in currencies other than the euro, we are exposed to fluctuations in the values of these currencies against the euro. Currency fluctuations have had and may continue to have a material impact on our financial condition, results of operations and cash flows.

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We estimate that in 2014 variations in currencies and hyperinflation in Venezuela decreased our cash flows and cash balance by approximately 1,616 million euros and decreased our consolidated revenues by approximately 12.1%. Currency fluctuations can also have a significant impact on our statement of financial position, particularly equity attributable to equity holders of the parent, when translating the financial statements of subsidiaries located outside the Eurozone into euro. For example, in 2014 equity attributable to equity holders of the parent decreased by 2,857 million euros due to the translation of the financial statements of our foreign subsidiaries, principally due to the depreciation of the Venezuelan bolívar fuerte and the Argentine peso, partially offset by the appreciation of the pound sterling relative to the euro.

We estimate that in 2013 variations in currencies and hyperinflation in Venezuela decreased our cash flows and cash balance by approximately 1,468 million euros and decreased our consolidated revenues by approximately 7.5%. In 2013 equity attributable to equity holders of the parent decreased by 5,691 million euros due to the translation of the financial statements of our foreign subsidiaries, principally due to the depreciation of the Brazilian real, the Venezuelan bolívar fuerte and the Argentine peso, relative to the euro.

We estimate that in 2012 variations in currencies and hyperinflation in Venezuela decreased our cash flows and cash balance by approximately 382 million euros and increased our consolidated revenues by approximately 0.1%. In 2012 equity attributable to equity holders of the parent decreased by 1,278 million euros due to the translation of the financial statements of our foreign subsidiaries, principally due to the depreciation of the Brazilian real relative to the euro.

The exchange rate of 6.3 bolivars per U.S. dollar was used in the translation of the financial information of Venezuelan subsidiaries for the whole year 2013.

During 2014, by virtue of certain Exchange Agreements the allocations conducted through the Complementary System for Administration of Foreign Currency (SICAD I), to which Telefónica Venezuela had access for imports, were expanded and, in addition, a new exchange mechanism with a more widespread use was put in place, called SICAD II.

The exchange rates resulting in the last allocations of SICAD I and SICAD II before December 31, 2014 were 12.0 and 49.988 bolívares per U.S. dollar, respectively.

In the absence of auctions since mid-October 2014, and the lack of expectations of new auctions close to 2014 year-end, in a macroeconomic context aggravated by the fall of the oil price, the Company has decided to take as a reference the rate resulting in the allocations conducted through SICAD II for translating the financial statements of the Venezuelan subsidiaries. The Company considers that it is the most representative among the available official exchange rates at 2014 year-end for the monetary translation of the accounting figures of transactions, cash flows and balances.

The main impacts of using this new exchange rate in the Telefónica Group's consolidated financial statements as of December 31, 2014 were as follows:

- A decrease in equity, within the caption "Translation differences", of approximately 2,950 million euros (see Note 12.f of the Consolidated Financial Statements) as a combined result of the translation to euros at the new exchange rate partially offset by the impact in equity of the inflation adjustment for the period.
- As part of the decrease mentioned in the preceding paragraph, the value in euros of the net financial assets denominated in bolívares decreased by approximately 2,700 million euros, as per the balance as of December 31,

2014.

- The results from the Telefónica's subsidiaries in Venezuela have been translated at the new exchange rate. This implied a reduction in operating income before depreciation and amortization (OIBDA) and profit for the year of, approximately, 1,730 and 660 million euros, respectively.

The table below sets forth the average exchange rates against the euro of the U.S. dollar and the key currencies that impacted our consolidated results of operations for the periods indicated. Positive percentage changes represent a decline in the value of the applicable currency relative to the euro, and negative percentage changes represent increases in the value of the applicable currency relative to the euro.

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	2012(1)	2013(1)	2014(1)	% change 2012 to 2013	% change 2013 to 2014
	Average	Average	Average	Average	Average
Pound Sterling	0.81	0.85	0.81	4.94%	(4.71)%
U.S. Dollar	1.29	1.33	1.33	3.10%	–
Brazilian Real	2.50	2.85	3.12	14.00%	9.47%
Argentine Peso	5.84	7.23	10.75	23.80%	48.69%
Peruvian Nuevo Sol	3.39	3.58	3.77	5.60%	5.31%
Chilean Peso	624.59	656.25	756.71	5.07%	15.31%
Mexican Peso	16.90	16.93	17.65	0.18%	4.25%
Venezuelan Bolívar Fuerte (2)	5.67	8.69	60.69	53.26%	n.m.
Czech Crown	25.14	25.99	27.53	3.38%	5.93%
Colombian Peso	2,308.54	2,478.69	2,650.03	7.37%	6.91%
Guatemalan Quetzal	10.06	10.43	10.25	3.68%	(1.73)%

Source: Central treasury bank of the respective countries.

(1) These exchange rates are used to convert the income statements of our subsidiaries from local currency to euro.

(2) As Venezuela is considered a hyperinflationary country, the income statement from operations in Venezuela is accounted pursuant to the closing exchange rate of bolívar fuerte to euro.

We describe certain risks relating to exchange rate fluctuations in “Item 3. Key Information—Risk Factors,” and we describe our policy with respect to limiting our exposure to short-term fluctuations in exchange rates under “Item 11. Quantitative and Qualitative Disclosures About Market Risk.”

Group Results of Operations

Please see “Item 4. Information on the Company — Business Overview — Group Results of Operations.”

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B. Liquidity and Capital Resources

Cash Flow Analysis

The table below sets forth consolidated cash flow information for the periods indicated. Positive figures refer to cash inflows and those in parenthesis refer to cash outflows.

(millions of euros)	2012	2013	2014
Net cash from operating activities	15,213	14,344	12,193
Net cash used in investing activities	(7,877)	(9,900)	(9,968)
Net cash used in financing activities	(1,243)	(2,685)	(4,041)

For a discussion of our cash flows for the years ended December 31, 2012, 2013 and 2014, please see Note 20 to our Consolidated Financial Statements.

Anticipated Uses of Funds

Our principal liquidity and capital resource requirements consist of the following:

- costs and expenses relating to the operation of our business;
- debt service requirements relating to our existing and future debt;
- capital expenditures for existing and new operations;
- acquisitions of new licenses or other operators or companies engaged in complementary or related businesses; and
- dividend, other shareholder remuneration, and pre-retirement payments.

In 2015, we expect to continue transforming our networks, evolving them towards all-IP hyper-connected networks, by investing in FTTx in key markets, and by expanding our mobile networks with LTE in most of our operations, and also with 3G. We also expect to continue investing in IT as a critical factor in our transformation. We will continue to invest in TV and digital sources to take advantage of the opportunities in the digital markets. And we may also use funds to acquire new licenses engaged in complementary or related businesses in the digital world.

We also have liquidity requirements related to the costs and expenses relating to the operation of our business, financial investments, our payment of dividends, shareholder remuneration and pre-retirement payment commitments. In 2014 cash expenditures consisted principally of: 3,382 million euros in connection with shareholder remuneration (in connection with payment of dividends on Telefónica shares and the acquisition of Telefónica treasury shares), 1,346 million euros principally in connection with net financial investments and 789 million euros in connection with commitments under pre-retirement plans.

We also have liquidity requirements related to debt service requirements in connection with our existing and future debt. At December 31, 2014, we had gross financial debt of 59,782 million euros compared with 60,699 million euros at December 31, 2013. For the amortization schedule of our consolidated gross financial debt at December 31, 2014 and a further description of financing activity in 2014, see “—Anticipated Sources of Liquidity” below. Our net financial debt decreased to 45,087 million euros at December 31, 2014, compared with 45,381 million euros at December 31, 2013 (excluding the implicit devaluation of the Venezuelan bolívar our net financial debt would have decreased by

2,635 million euros). The decrease in net financial debt was mainly explained by our 2014 cash flow generation before spectrum payments of 4,748 million euros, the issue of equity instruments for a total amount of 4,699 million euros of Telefónica Deutschland (including the portion subscribed by Telefónica Deutschland's minority shareholders in the capital increase) and proceeds of 3,981 million euros from disposals (relating to the sale of Telefónica Czech Republic and a 2.5% stake in China Unicom). In contrast, factors contributing to increased debt in 2014 include net financial investments (4,949 million

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euros), 3,382 million euros as remuneration of equity instruments (including the purchase of treasury stock), spectrum payments (932 million euros), the payment of labor commitments mainly associated with early retirements (789 million euros) and other factors that increased debt by 741 million euros. For a reconciliation of net financial debt to gross financial debt (the sum of current and non-current interest-bearing liabilities), see “—Presentation of Financial Information—Non-GAAP financial information—Net financial debt and net debt”.

For a discussion of our liquidity risk management policy, see Note 16 to our Consolidated Financial Statements.

Anticipated Sources of Liquidity

Cash flows from operations are our primary source of cash funding for existing operations, capital expenditures, interest obligations and principal payments. We also rely on external borrowings, including a variety of short- and medium-term financial instruments, principally bonds and debentures, undated deeply subordinated securities and borrowings from financial institutions. Cash and cash equivalents are mainly held in euros and euro-denominated instruments. 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.

Financing

The following table shows the amortization schedule of our consolidated gross financial debt at December 31, 2014 as stated in euro. We may have exchange rate financial derivatives as instruments assigned to the underlying debt instruments. In 2014, the average cost of net debt, which we measure as net financial expense divided by our average net debt which, adjusted for exchange rate differences, was 5.40%. The table below includes the fair value of those derivatives classified as financial liabilities (negative mark-to-market) under IFRS (401 million euros classified as a current financial liability and 3,231 million euros as a non-current financial liability). The table does not include the fair value of derivatives classified as financial assets (positive mark-to-market) under IFRS (813 million euros classified as current financial assets and 5,499 million euros as non-current financial assets). For description of the liquidity risk we face, see Note 16 to our Consolidated Financial Statements, and for a description of our financial liabilities, see Note 13 to our Consolidated Financial Statements.

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Millions of euros

Maturity	Current			Non-current		Subsequent Non-current		Total
	2015	2016	2017	2018	2019	years	total	
Debentures and bonds	4,601	6,722	6,392	4,834	3,465	18,214	39,627	44,228
Promissory notes & commercial paper	502	-	-	-	-	-	-	502
Other marketable debt securities	-	-	-	-	-	-	-	-
Total Issues	5,103	6,722	6,392	4,834	3,465	18,214	39,627	44,730
Loans and other payables	3,590	1,533	3,205	761	849	1,482	7,830	11,420
Other financial liabilities	401	152	347	477	357	1,898	3,231	3,632
TOTAL	9,094	8,407	9,944	6,072	4,671	21,594	50,688	59,782

Notes:

- Estimated future interest payments as of December 31, 2014 on our interest-bearing debt (not included above) are as follows: 2,215 million euros in 2015, 1,960 million euros in 2016, 1,671 million euros in 2017, 1,279 million euros in 2018, 1,077 million euros in 2019 and 6,586 million euros in subsequent years. With respect to floating rate debt, we estimate future interest payments as the forward rates derived from yield curves quoted for the different currencies on December 31, 2014.

During 2014, we obtained external financing in the form of borrowings of approximately 14,740 million euros. The financing activity in 2014 was mainly focused on completing the financing for the acquisition of E-Plus (via the issue of a 1,500 million euro bond mandatorily convertible into Telefónica shares and the execution of a capital increase by Telefónica Deutschland), strengthening the liquidity position, actively managing the cost of debt and smoothing the debt maturity profile for the following years. Therefore, as of December 31, 2014, we believe we maintain an adequate liquidity position to accommodate 2015 and 2016 debt maturities.

For a description of our financing, see Note 13 to our Consolidated Financial Statements.

In 2015, through the date of this Annual Report, our debt issuances and principal financing arrangements consisted of:

- On February 19, 2015, Telefónica, S.A. signed a 2,500 million euros syndicated credit facility maturing in 2020 with two twelve month extension options requiring mutual agreement of the parties (which could extend the maturity to as late as 2022). This agreement entered into effect on February 26, 2015 and allowed us to cancel in advance the syndicated loan facility of Telefónica Europe, B.V. dated on March 2, 2012 with two tranches of 756 million euros and 1,469 million pounds sterling originally scheduled to mature in 2017. On the same date, Telefónica S.A. signed an amendment to its 3,000 million euros syndicated credit facility arranged on February 18, 2014 and maturing in 2019 in which the parties mutually agreed two twelve month extension options (which could extend the maturity to as late as 2021).

Our borrowing requirements are not significantly affected by seasonal trends.

Availability of funds

At December 31, 2014, Telefónica has funds available amounting to 19,414 million euros, which includes: undrawn lines of credit for an amount of 11,545 million euros (10,618 million euros maturing in more than 12 months); cash and cash equivalent and current financial assets other than those in Venezuela (367 million euros) and Telefónica's participation in Telco's bond (principal amount of 1,225 million euros) totalling 7,869 million euros.

For a description of our liquidity and undrawn lines of credit available at December 31, 2014, see Notes 12 and 13 to our Consolidated Financial Statements, and for a discussion of our liquidity risk management and our capital management, see Note 16 to our Consolidated Financial Statements.

Telefónica, S.A. is the parent company of the Telefónica Group and receives funding from its subsidiaries in the form of dividends and loans. Consequently, restrictions on the ability of the Group's subsidiaries to transfer funds to Telefónica, S.A. in the form of cash dividends, loans or advances, capital repatriation and other forms would negatively affect our liquidity and thus our business.

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Certain Latin American economies, such as Argentina and Venezuela, have experienced shortages in foreign currency reserves and their respective governments have adopted restrictions on the ability to transfer funds out of the country and convert local currencies into U.S. dollars. This may limit our ability to repatriate funds out of certain subsidiaries from such countries. However, regarding repatriation of funds to Spain, in 2014 we have received 1,118 million euros from our Latin American subsidiaries, of which 961 million euros was from dividends and 157 million euros was from other items.

Credit Ratings

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 financial markets. However, negative conditions in the financial markets or a downgrade of any of the ratings of our debt or the Kingdom of Spain's debt by any of Fitch, Moody's and/or Standard & Poor's may increase the cost of our future borrowings 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 general macroeconomic and political conditions (including sovereign credit rating prospects), the performance of our businesses in countries where we operate, our financial and shareholder remuneration policy, our M&A policy, our ability to integrate acquired companies and our ability to refinance debt.

In 2014, we have taken certain measures to protect our credit rating. These measures mainly include: an intensive and prudent financing activity together with a conservative liquidity policy, the implementation of a scrip dividend (instead of a cash only dividend) in November 2014, a portfolio rationalization through the total or partial sale of certain assets such as Telefónica Ireland, Telefónica Czech Republic and China Unicom, the issuance of financial instruments with high equity content to finance the E-Plus acquisition (such as bonds mandatorily convertible into Telefónica shares) and the issuance of undated deeply subordinated securities as a solvency protection measure to mitigate negative impacts on our consolidated financial statements deriving from unforeseen events such as the devaluation in Venezuela.

Intragroup Loans

We lend funds to our operating subsidiaries, directly or through holding companies that head our different lines of business. At December 31, 2014, we had loans outstanding totaling 7,433 million euros (9,806 million euros at December 31, 2013) to companies in the Telefónica Group (including subsidiaries located in Latin American countries). These funds are derived from retained cash flows, loans, bonds, issuances of undated deeply subordinated securities and other sources (such as asset disposals).

C. Research and Development, Patents and Licenses, etc.

Telefónica remains firmly committed to technological innovation as an essential tool for achieving competitive advantages, trying to anticipate market trends and differentiating its products. By introducing new technologies and developing new products and business processes, we seek to become a more effective, efficient and customer-oriented Group.

Telefónica has developed an open innovation model for the management of technological innovation to boost the application of technical research in the development of new commercial products and services. Telefónica focuses on certain applied research and development (R&D) priorities that are aligned with its strategy. Open innovation initiatives driving this model include the creation of a venture capital fund and involvement in business collaboration forums, among others. The model also promotes the use of knowledge developed at technology centers, universities and start-ups, among other sources, and encourages innovation in conjunction with other agents (e.g. customers,

universities, public administrations, suppliers, content providers and other companies), making them “technological partners.” Within this open innovation strategy, the Open Future program was reinforced during 2014. This program is designed to connect entrepreneurs, startups, investors and public and private organizations from all over the world with a view to fostering innovation and developing viable projects.

Telefónica believes it cannot rely solely on acquired technology to differentiate its products from those of its competitors and to improve its market positioning. It is also important to encourage R&D initiatives in an effort to achieve this differentiation and make inroads in other innovation activities. The Group’s R&D policy is geared towards:

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- developing new products and services in order to win market share;
- boosting customer loyalty;
- increasing revenue;
- enhancing innovation management;
- improving business practices;
- increasing the quality of infrastructure services to improve customer service and reduce costs;
- promoting global products;
- supporting open innovation; and
- creating value from the technology generated.

In 2014, the technological innovation projects undertaken focused on sustainable innovation, process efficiency, creation of new revenue streams, customer satisfaction, consolidation of operations in new markets and technological leadership.

Technical innovation activities are a key part of Telefónica's strategy of creating value through latest-generation network communications and services.

In 2014, projects were undertaken to promote greater access to information technology, new services focused on new internet business models, advanced user interfaces, TV distribution, multimedia content and other added-value services leveraging on the potential of the new infrastructures. These initiatives, among others, were undertaken based on our objective of rapidly identifying emerging technologies that could have a relevant impact on our businesses and pilot testing these technologies in new services, applications and platform prototypes.

Most of our R&D activities are carried out by Telefónica Investigación y Desarrollo, S.A.U. (Telefónica I+D), a wholly-owned subsidiary, which works mainly for the lines of business. In its operations, Telefónica I+D receives the assistance of other companies and universities. Telefónica I+D's mission is centered on enhancing the Company's competitive positioning by leveraging technological innovation and product development. Telefónica I+D undertakes experimental and applied research and new product development with the overriding goal of broadening the range of services offered and reducing operating costs.

Telefónica I+D's technological innovation activities focus on two big areas:

- Telefónica I+D's works on new networks, primarily in collaboration with Telefónica's Global Resources team. These activities are related to radio access technologies and fiber; network virtualization technologies, in line with the technology trend known as software defined networks (SDN); and network optimization and zero touch developments making networks more flexible and moldable and able to adapt dynamically to new digital consumer and service requirements.
- R&D activities to develop new products and services are conducted as part of the digital services strategy. These activities include the following:

- o Natural P2P communication of the future, using the Internet, Web 2.0 and smartphones.
- o Video and multimedia services (combining text, audio, images and video) offering a user experience in all connected devices.
- o Advanced solutions in emerging ITC businesses such as cloud computing, security, financial services or e-health.
- o M2M (machine-to-machine) service management associated with energy efficiency and mobility and with the Internet of Things and their adoption in the urban and industrial scenario, and as a service creation enabler.

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oMaking use of user communication profiles to exploit opportunities to operate different products and business models (marketing campaigns, target marketing, contextual services, churn reduction, cross-selling, etc.).

Telefónica I+D's also boasts scientific work groups with a more medium- to long-term focus and aims to look into opportunities relating to new networks and services and solutions to the technological challenges that arise.

In 2014, Telefónica in collaboration with the Chilean government launched a new R&D center in Chile, with focus on Internet of Things and Big Data, in the field of Smart Cities, Smart Industry and Smart Agro.

At December 31, 2014, Telefónica I+D had 652 employees (689 employees in 2013).

Total I+D expense in the Group for 2014 amounted to 1,111 million euros, up 6.2% from the 1,046 million euros incurred in 2013 (1,071 million euros in 2012). This expense represents 2.2%, 1.8% and 1.7% of the Group's consolidated revenue for 2014, 2013 and 2012, respectively. These figures were calculated using guidelines of the Organization for Economic Co-operation and Development (OECD).

During 2014, Telefónica filed 27 new patent applications, all of them registered through the Spanish Patent and Trademark Office (OEPM), of which 25 are European applications (EP) and 2 are International applications (PCT). Additionally 2 utility models were filed, also through OEPM.

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D. Trend Information

Telefónica is an integrated diversified telecommunications group that offers a wide range of services, mainly in Europe and Latin America. Its core business is the provision of fixed and mobile telephony, broadband, internet, data, Pay-TV and value-added services, among others. The Group's operations in 25 countries, managed through a regional organization geared towards certain businesses in global units, enable it to leverage the strong local positioning, as well as the advantages afforded by its scale.

As a multinational telecommunications company that operates in regulated markets, Telefónica is subject to different laws and regulations in each of the jurisdictions in which it provides services. Among other developments, Telefónica may face pressure from regulatory initiatives in some European countries regarding tariffs, the reform of rights of spectrum use and allocation, issues related to the quality of service, and the regulatory treatment of new broadband infrastructure deployments.

Telefónica faces intense competition in the vast majority of the markets where it operates in, and is therefore subject to the effects of actions taken by its competitors. The intensity of the competition may deepen which could have an impact on tariff structures, consumption, market share and commercial activity and negatively affect the number of customers, revenues and profitability.

However, Telefónica believes that it is in a strong competitive position in most of the markets where it operates, which it expects to help enable it to continue taking advantage of the growth opportunities that arise in these markets, such as by boosting both fixed and mobile broadband services and by furthering the development of services beyond connectivity, information technology services and related businesses.

In 2014, Telefónica took a further step towards its transformation into a leading digital telecommunications company, in a sector which we believe still offers excellent growth potential. Digital capacities were boosted, new products were developed, and new business models were set up. This was achieved as a result of a transformation drive implemented throughout the Company.

2013 marked a turning point with the launch of a multinational program, "Be More", focused on transformation and growth and the deleveraging of our business in Ireland, Czech Republic and 40% of Central America. This program aims to take advantage of our customer insight, the capture of future Business to Business (B2B) opportunities, further data monetization of our services and reinforcing our video business. In addition, we will seek to simplify our operating model and increase investments in fiber and LTE, transforming the IT in our operating business. In 2014, we made progress in the transformation process of Telefónica, simplifying the Company and building the bases for a new organization, simplifying operations, making provisions for a leaner staffing at a number of group operators and making key changes to our structure.

We believe that both the completion of the consolidation of our operations in Germany and the acquisition of GVT in Brazil (which is still pending approval by the regulator), which entail structural changes to the Company's positioning in two of its largest markets, points to, and strengthens, our capacity for future growth.

The pace of addition of high-value customers was stepped up in 2014, with more than 21 million new smartphones, 1.5 million new Pay-TV accesses and 927 new fiber accesses. We believe these figures indicate a growing generalization of usage-intensive data and content services.

Intense commercial activity in the area of high-value services was attributable mainly to greater investment, which allowed us to double the size of our FTTH network to 14.7 million premises passed, securing LTE coverage of 41% of

the outdoor population in the regions where we operate, thereby increasing the number of LTE base stations to more than 20 thousand in 2014 (2.2X compared to 2013).

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Telefónica Spain showed a change in trend due to the in-depth transformation process rolled out by the company to steady the pace of the year-on-year fall in revenue, with the assistance of intense commercial activity, especially in terms of fiber and Pay-TV. “Movistar Fusión” continued to grow steadily mainly as a result of the offering of the new bundled portfolio including TV in almost all our portfolio with a competitive price from 60 euros/month, which continued to attract customers to value-added offers.

Telefónica United Kingdom continued to work on the deployment of its LTE network, reaching 58% outdoor coverage at year-end, keeping the focus on offering a positive network experience and an exclusive content proposition to 4G customers. The operator is still migrating its high-value customers to LTE, with a view to boosting the network experience and customer satisfaction. Telefónica United Kingdom continues to deliver a good commercial performance with its "Refresh" offer, helping improve the market distribution dynamics towards more efficient channels.

On August 29, 2014 the Company was given the green light from the European Commission to purchase the E-Plus Group, and the transaction was completed on October 1, 2014. The E-Plus Group has been part of Telefónica Deutschland since that date. The new company is intent on becoming Germany's leading digital telecommunications company, and aims to secure synergies of more than 5 billion euros of present value, mainly produced by the network, customer service, overheads and new opportunities for generating income.

Telefónica Germany continued to perform well in 2014, mainly in the mobile contract segment, thanks to a strategy focusing on data monetization. This performance was achieved against a more competitive backdrop with growing demand for LTE offers and terminals. Year-on-year revenue stabilized, and mobile revenue rose again year-on-year.

As part of the transformation process, embarked by the Group, a significant provision was recorded for E-Plus in connection with the planned downsizing of its staffing, which aims to lay the foundations for future growth.

In Brazil, we consolidated the leadership in the higher-value mobile segments, maintaining our dominance of the market. The Company was awarded one of the three blocks of radioelectric spectrum for LTE auctioned in the 700 MHz band (2x10 MHz) on September 30, 2014, for the minimum reserve price of the block (approximately 619 million euros). This gave Telefónica Brazil the spectrum it needed to expand the 4G services in the medium and long term, and accelerate adoption of data (in 2014, data revenue accounted for 34.3% of the total).

In the fixed business, fiber deployment was key, with 14.7 million premises passed by December 2014, and the number of connected homes gradually rose to 1.8 million.

On September 19, 2014 the Company entered into an agreement with Vivendi to purchase GVT, with a view to creating an integrated operator with national coverage focused on higher-value customers to give a major boost to the Company's market positioning. The purchase is pending approval by the regulator.

Strong commercial activity by Telefónica Hispanoamérica, along with robust investment to improve service quality, continued to drive steady year-on-year growth of revenue and OIBDA, especially in Mexico, Colombia and Peru.

In summary, in the context of intense competition and regulatory pressure on pricing, Telefónica aims to continue strengthening its business model to make it more efficient and capture the synergies arising from the integrated approach of businesses, processes and technologies, while focusing even more on the client and staying ahead of trends in the new digital world.

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 statement of financial position at December 31, 2014 although they are described in the notes to our Consolidated Financial Statements. For summary of our off-balance sheet commitments, see Note 21(b) and Note 16 to our Consolidated Financial Statements.

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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 (including accrued interest payments) are as of December 31, 2014. For additional information, see our Consolidated Financial Statements.

Millions of euros	Total	Payments Due by Period			
		Less than 1 year	1-3 years	3-5 years	More than 5 years
Financial liabilities (1)(2)	59,782	9,094	18,351	10,743	21,594
Operating lease obligations (3)	10,197	1,643	2,669	2,068	3,817
Purchase and other contractual obligations(4)	9,037	4,295	2,071	961	1,710
Other liabilities (5)	3,828	574	3,254	—	—
Total	82,844	15,606	26,345	13,772	27,121

- (1)Capital (finance) lease obligations are not calculated separately and are instead included as part of our long-term debt obligations.
- (2)Estimated future interest payments as of December 31, 2014 on our interest-bearing debt (not included above) are as follows: 2,215 million euros in 2015, 1,960 million euros in 2016, 1,671 million euros in 2017, 1,279 million euros in 2018, 1,077 million euros in 2019 and 6,586 million euros in subsequent years. With respect to floating rate debt, we estimate future interest payments as the forward rates derived from yield curves quoted for the different currencies on December 31, 2014. This item includes the fair value of those derivatives classified as current financial liabilities (negative mark-to-market) under IFRS (401 million euros). It does not include the fair value of derivatives classified as financial assets (positive mark-to-market) under IFRS (813 million euros classified as current financial assets and 5,499 million euros as non-current financial assets). For a more detailed description of our financial derivative transactions, see Note 16 to our Consolidated Financial Statements. For details of the composition of this item, see “Liquidity and Capital Resources– Anticipated Sources of Liquidity”).
- (3)This item includes definitive payments (non-cancellable without penalty cost). Our operating lease obligations have in some cases extension options conditioned on the applicable law of each country. Accordingly, we have included only those amounts that represent the initial contract period. At December 31, 2014, the present value of future payments for operating leases was approximately 7,966 million euros (1,715 million euros in Telefónica Brazil, 1,640 million euros in Telefónica Hispanoamérica, 930 million euros in Telefónica Spain, 710 million euros in Telefónica United Kingdom, 2,837 million euros in Telefónica Germany and 134 million euros in other companies). For a more detailed information about payments due under this item, see Note 19 to our Consolidated Financial Statements.
- (4)This item includes definitive payments (non-cancellable without penalty cost) due for agreements to purchase goods (such as network equipment) and services.
- (5)“Other liabilities” include: (a) long-term obligations that require us to make cash payments, excluding financial debt obligations included in the table under “Financial Liabilities” above and (b) other provisions. Because of the nature of the risks covered by “Other liabilities” such as other provisions, it is not possible to determine a reliable schedule of potential payments, if any. For details of the composition of other provisions, see Note 15 to our Consolidated Financial Statements.

In addition, at December 31, 2014, we had short-term and long-term employee benefits provisions amounting to 574 million euros and 3,254 million euros, respectively (see Note 15 to our Consolidated Financial Statements).

For details of the composition of, and changes in, our debt, see “—Liquidity and Capital Resources—Anticipated Sources of Liquidity” and Note 13 to our Consolidated Financial Statements.

Item 6. Directors, Senior Management and Employees

A. Directors and Senior Management

During 2014, our Board of Directors met 14 times. At February 27, 2015, our Board of Directors had met three times during 2015. At February 27, 2015, our directors, their respective positions on our Board and the year they were appointed to such positions were as follows:

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Name	Age	First Appointed	Current Term Ends
Chairman			
Mr. César Alierta Izuel(1)	69	1997	2017
Vice-chairmen			
Mr. Isidro Fainé Casas(1)(2)	72	1994	2016
Mr. José María Abril Pérez (1)(3)(7)	62	2007	2018
Mr. Julio Linares López (5)(7)(8)	69	2005	2016
Members (vocales)			
Mr. José María Álvarez-Pallete López (1)	51	2006	2017
Mr. José Fernando de Almansa Moreno -Barreda(5)(6)(8)	66	2003	2018
Ms. Eva Castillo Sanz (6)(8)(10)	52	2008	2018
Mr. Carlos Colomer Casellas(1)(4)(7)(9)(10)	70	2001	2016
Mr. Peter Erskine(1)(7)(8)(9)	63	2006	2016
Mr. Santiago Fernández Valbuena	56	2012	2018
Mr. Alfonso Ferrari Herrero (1)(4)(5)(6)(8)(9)(10)	73	2001	2016
Mr. Luiz Fernando Furlán	68	2008	2018
Mr. Gonzalo Hinojosa Fernández de Angulo (1)(4)(5)(6)(8)(9)(10)	69	2002	2017
Mr. Pablo Isla Álvarez de Tejera(9)	51	2002	2017
Mr. Antonio Massanell Lavilla(2)(4)(5)(7)(10)	60	1995	2016
Mr. Ignacio Moreno Martínez (3)(4)(6)(10)	57	2011	2017
Mr. Francisco Javier de Paz Mancho (1)(5)(6)(10)	56	2007	2018
Mr. Chang Xiaobing (11)	57	2011	2016
(1)	Member of the Executive Commission of the Board of Directors.		
(2)	Nominated by Fundación Bancaria Caja de Ahorros y Pensiones de Barcelona (“La Caixa”).		
(3)	Nominated by Banco Bilbao Vizcaya Argentaria, S.A. (“BBVA”).		
(4)	Member of the Audit and Control Committee of the Board of Directors.		
(5)	Member of the Institutional Affairs Committee.		
(6)	Member of the Regulation Committee.		
(7)	Member of the Innovation Committee.		
(8)	Member of the Strategy Committee.		
(9)	Member of the Nominating, Compensation and Corporate Governance Committee.		
(10)	Member of the Service Quality and Customer Service Committee.		
(11)	Nominated by China Unicom (Hong Kong) Limited.		

Board Committees

At February 27, 2015, the committees of our Board of Directors and members thereof are as follows:

Executive Commission

Our Board of Directors has expressly delegated all of its authority and power to the Executive Commission except as prohibited by the Spanish Corporation Act, under our Articles of Association, or under our Board Regulations. This commission is made up of fewer directors and meets more frequently than our Board of Directors. The members of the Executive Commission are Mr. César Alierta Izuel, Mr. Isidro Fainé Casas, Mr. José María Abril Pérez, Mr. José María Álvarez-Pallete López, Mr. Carlos Colomer Casellas, Mr. Peter Erskine, Mr. Alfonso Ferrari Herrero, Mr. Gonzalo Hinojosa Fernández de Angulo, Mr. Francisco Javier de Paz Mancho and Mr. Ramiro Sánchez de Lerín García-Ovies, as secretary.

Audit and Control Committee

The Audit and Control Committee functions are regulated by our bylaws and our Board Regulations. The Audit and Control Committee has the primary objective of providing support to our Board of Directors in its supervisory and oversight functions, specifically having the following responsibilities:

- to report, through its chairman, to our shareholders at the general shareholders' meeting regarding matters raised therein by the shareholders relating to the functions and matters of competence of the committee;

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- to propose to our Board of Directors to submit to our general meeting of shareholders the appointment of our auditors referred to in Article 264 of the Spanish Corporation Act, as well as, when appropriate, the terms of their engagement, the scope of their professional assignment and the revocation, re-appointment or non-renewal of their appointment;
- to supervise the effectiveness of the Company's internal control system, the internal audit and the risk management systems as well as to discuss with our auditors any significant weaknesses in the internal control system detected during the audit;
 - to supervise the preparation and submission of regulated financial information;
- to establish and maintain the necessary relations with the auditors to receive, for review by the Committee, information on all matters that may put their independence at risk, and any other matters related to the process of auditing our accounts, as well as to receive information and maintain communication with our auditors as required by laws relating to the audit process and with respect to technical regulations on auditing. In any event, the Audit and Control Committee must receive annually written confirmation from our auditors of their independence vis-à-vis the entity or entities directly or indirectly related thereto, as well as information regarding additional services of any kind provided to such entities by our auditors, or by the persons or entities related thereto, pursuant to Law 19/1988, of July 12, on Auditing of Financial Statements; and
- to issue on an annual basis, prior to the issuance of the audit report, a report stating an opinion regarding the independence of our auditors. This report must in all cases include an opinion on the provision of the additional services referred to in the immediately preceding paragraph.

The Audit and Control Committee meets at least once per quarter and as many times as considered necessary. During 2014, the Audit and Control Committee met eleven times and, as of the date of this Annual Report, had met two times in 2015. The members of the Audit and Control Committee are Mr. Carlos Colomer Casellas (chairman), Mr. Gonzalo Hinojosa Fernández de Angulo, Mr. Antonio Massanell Lavilla, Mr. Alfonso Ferrari Herrero and Mr. Ignacio Moreno Martínez. Our Board of Directors has determined that Mr. Antonio Masanell Lavilla meets the requirements of an “audit committee financial expert” as such term is defined by the SEC.

Nominating, Compensation and Corporate Governance Committee

The Nominating, Compensation and Corporate Governance Committee is responsible for, among other things, reporting to our Board of Directors with respect to proposals for the appointment, re-election and removal of directors, members of the Executive Committee and the other committees of our Board of Directors and top members of our management and management of our subsidiaries. In addition, the Nominating, Compensation and Corporate Governance Committee is responsible for proposing to the Board of Directors, within the framework established in the bylaws, the compensation for the directors and reviewing it periodically to ensure that it is in keeping with the tasks performed by them, as provided in Article 35 of the Board Regulations, to propose to the Board of Directors, within the framework established in the bylaws, the extent and amount of the compensation, rights and remuneration of a financial nature, of the chairman, the executive directors and the senior executive officers of Telefónica, including the basic terms of their contracts, for purposes of contractual implementation thereof and to supervise compliance with the corporate governance rules in effect from time to time.

The members of the Nominating, Compensation and Corporate Governance Committee are Mr. Alfonso Ferrari Herrero (chairman), Mr. Carlos Colomer Casellas, Mr. Peter Erskine, Mr. Gonzalo Hinojosa Fernández de Angulo and Mr. Pablo Isla Álvarez de Tejera. During 2014, the Nominating, Compensation and Corporate Governance Committee

met eleven times, and as of the date of this Annual Report, it had met three times in 2015.

Regulation Committee

The Regulation Committee's main objective is to monitor the main regulatory matters which affect us. Another responsibility of the Regulation 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. Gonzalo Hinojosa Fernández de Angulo (chairman), Mr. José Fernando de Almansa Moreno-Barreda, Ms. Eva Castillo Sanz, Mr. Alfonso Ferrari Herrero, Mr. Ignacio Moreno Martínez and Mr. Francisco Javier de Paz Mancho.

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During 2014, the Regulation Committee met five times, and of the date of this Annual Report, it had met one time in 2015.

Service Quality and Customer Service Committee

The Service Quality and Customer Service Committee is responsible for monitoring and reviewing the standards of quality of the main services we provide. 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. Antonio Massanell Lavilla (chairman), Ms. Eva Castillo Sanz, Mr. Carlos Colomer Casellas, Mr. Alfonso Ferrari Herrero, Mr. Gonzalo Hinojosa Fernández de Angulo, Mr. Ignacio Moreno Martínez and Mr. Javier de Paz Mancho. During 2014 the Service Quality and Customer Service Committee met two times, and as of the date of this Annual Report, it had met one time in 2015.

Institutional Affairs Committee

The Institutional Affairs Committee is responsible for reviewing, reporting and proposing to the Board of Directors the principles that are to govern the Group's Sponsorship and Patronage Policy, to monitor such policy, and to individually approve sponsorships or patronages the amount or importance of which exceed the limit set by the Board and which require its approval. The Committee is responsible for promoting the development of the Telefónica Group's Corporate Reputation and Responsibility project and its institutional affairs. The members of the Institutional Affairs Committee are Mr. Julio Linares López (chairman), Mr. José Fernando de Almansa Moreno-Barreda, Mr. Alfonso Ferrari Herrero, Mr. Gonzalo Hinojosa Fernández de Angulo, Mr. Antonio Massanell Lavilla and Mr. Francisco Javier de Paz Mancho. During 2014, the Institutional Affairs Committee met six times, and as of the date of this Annual Report it had met two times in 2015.

Innovation Committee

The Innovation Committee is responsible for advising and assisting in all matters regarding innovation. Its main object is to examine, analyze and periodically monitor the Group's innovation projects, provide guidance and help ensure the implementation and development of innovation initiatives across the Group. The members of the Innovation Committee are Mr. Carlos Colomer Casellas (chairman), Mr. José María Abril Pérez, Mr. Antonio Massanell Lavilla, Mr. Julio Linares López and Mr. Peter Erskine. During 2014, the Innovation Committee met five times, and as of the date of this Annual Report, it had met two times in 2015.

Strategy Committee

Without prejudice to any other tasks that the Board of Directors may assign thereto, the primary duty of the Strategy Committee is to support the Board of Directors in the analysis and implementation of the global strategy policy of the Telefónica Group. The members of the Strategy Committee are Mr. Peter Erskine (chairman), Mr. José Fernando de Almansa Moreno-Barreda, Ms. Eva Castillo Sanz, Mr. Alfonso Ferrari Herrero, Mr. Julio Linares López and Mr. Gonzalo Hinojosa Fernández de Angulo. The Strategy Committee met five times during 2014, and as of the date of this Annual Report, had met two times in 2015.

Biographies of Directors

Mr. César 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, S.A. in Madrid, where he worked until 1985. Subsequently, he founded and served as Chairman of Beta Capital Sociedad de Valores, S.A.

which he combined as from 1991 with his post as Chairman of the Spanish Financial Analysts' Association (Instituto Español de Analistas Financieros). Between 1996 and 2000, he was Director and Chairman of Tabacalera, S.A. At that time Tabacalera, S.A. changed its name into Altadis, S.A. (following its merger with the French Group, Seita-Société Nationale D'Éxploration Industrielle des Tabacs et Allumettes) and he became Director and Chairman of Altadis, S.A. He has also been a member of the Board of Directors of the Madrid Stock Exchange (Bolsa de Madrid), Plus Ultra Compañía de Seguros y Reaseguros, S.A. and of Iberia, S.A. In January 1997, Mr. Alierta was appointed as a Director of Telefónica and on July 26, 2000, he was appointed as our Executive Chairman. Mr. Alierta is Director of China Unicom (Hong Kong) Limited since October 15, 2008, and of International Consolidated Airlines Group (IAG) since September 2010. Also, he is Trustee of Fundación Bancaria Caja de Ahorros y Pensión ("La Caixa"). Mr. Alierta has been a Director of Telecom Italia

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from November 8, 2007, to December 13, 2013. Mr. Alierta holds a Law degree from the University of Zaragoza and an MBA from Columbia University (New York) and is currently a member of the Columbia Business School Board of Overseers, and Chairman of the Social Board of the UNED (National Long Distance Spanish University).

Mr. Isidro Fainé Casas serves as Vice-Chairman of our Board of Directors. For over 40 years, Mr. Fainé has worked in several financial institutions, including amongst others: Banco Atlántico, S.A., (1964), Banco de Asunción (Paraguay) (1969), Banca Riva y García, S.A. (1973), Banca Jover, S.A. (1974), and Banco Unión, S.A. (1978). Mr. Fainé is currently Chairman of Fundación Bancaria Caja de Ahorros y Pensiones de Barcelona (“La Caixa”) of Caixa Bank, S.A., of Criteria Caixaholding, S.A., and of the Spanish Confederation of Savings Banks (CECA). He is also the Chairman of the Board of trustees of the Caixa d’ Estalvis I Pensiones de Barcelona “La Caixa” Banking Foundation; First Deputy Chairman of Abertis Infraestructuras, S.A. of Repsol YPF, S.A. of the European Savings Banks Group (ESGB) and Deputy Chairman of the World Savings Banks Institute (WSBI). Furthermore, he is a member of the Boards of Directors of Banco Portugués de Investimento, S.A. (BPI), of the Bank of East Asia and of Suez Environnement Company. He is currently the Chairman of the Spanish Confederation of Executives (CEDE), the Spanish Chapter of the Club of Rome and the Círculo Financiero. He is also a member of the Business Council for Competitiveness (CEC). Mr. Fainé holds a Doctorate degree in Economics, a Diploma in Senior Management from IESE Business School and an ISMP certificate in Business Administration from Harvard University. He is a member of the Royal Academy of Economics and Finance and of the Royal Academy of Doctorate Holders.

Mr. José María Abril Pérez serves as Vice-Chairman of our Board of Directors. From 1975 to 1982 he served as Financial Manager of Sociedad Anónima de Alimentación (SAAL). Since then, and until he joined the Banco Bilbao Vizcaya Argentaria Group (BBVA), he was Financial Manager of Sancel-Scott Ibérica, S.A. In 1985 he joined Banco Bilbao, S.A. as Managing Director of Investment Corporate Banking. From January to April 1993, he was appointed Executive Coordinator of Banco Español de Crédito, S.A. In 1998, he became General Manager of the Industrial Group of BBV. In 1999, he was appointed member of the Executive Committee of the BBV Group. He has also been a member of the Board of Directors of Repsol, S.A., Iberia, S.A., Corporación IBV, and Vice-Chairman of Bolsas y Mercados Españoles, S.A. In 2002 he became Managing Director of the Wholesale and Investment Banking Division and a member of the Executive Committee of Banco Bilbao Vizcaya Argentaria, S.A., and he is now in retirement. He holds a degree in Economics from the University of Deusto (Bilbao, Spain) and he has been professor of such University for nine years.

Mr. Julio Linares López serves as Vice-Chairman of our Board of Directors since September 2012 and had been our Chief Operating Officer from December 2007 to September 2012. He is also a member of the Advisory Committee of Telefónica Hispanoamérica and Telefónica España. In May 1970, he joined our Research and Development Center, where he held several positions until he was appointed head of our Technology Department in 1984. In April 1990, he was appointed General Manager of Telefónica Research and Development, S.A. In December 1994, he became Deputy General Manager of the Marketing and Services Development department in the commercial area and subsequently, Deputy General Manager for Corporate Marketing. In July 1997, he was appointed Chief Executive Officer of Telefónica Multimedia S.A. and Chairman of Telefónica Cable and Producciones Multitemáticas, S.A. in the Telefónica multimedia business. In May 1998 he was appointed General Manager of Strategy and Technology in Telefónica, S.A. In January 2000, he was appointed Executive Chairman of Telefónica de España, S.A., a position which he held until December 2005, when he was appointed our Managing Director for Coordination, Business Development and Synergies. Mr. Linares was a Director of Telecom Italia until December 13, 2013. He is currently member of the GSM Association Board and Executive Committee, and is Chairman of the Strategic Committee. He is a Trustee of the Mobile World Capital Barcelona Foundation, of the Telefónica Foundation and of the CEDE-Confederación Española de Directivos and Ejecutivos Foundation. He is also a member of the Association Management Board for Managerial Progress and of the Social Council of the Complutense University in Madrid. Mr. Linares holds a degree in Telecommunications Engineering from the Polytechnic University of Madrid (Universidad

Politécnica de Madrid).

Mr. José María Álvarez-Pallete López serves as a Director of our Board of Directors and, since September 2012 as our Chief Operating Officer. From September 11, 2011, to September 2012, he served as Chairman of Telefónica Europe. He began his career at Arthur Young Auditors in 1987. In 1988, he joined Benito & Monjardín/Kidder, Peabody & Co., where he held various positions in the research and corporate finance departments. In 1995, he joined Compañía Valenciana de Cementos Portland, S.A. (Cemex) as head of the Investor Relations and Analysis department. In 1996 he was promoted to Chief Financial Officer of Cemex Group in Spain, and in 1998, to Chief Administration and Financial Officer of Cemex in Indonesia, headquartered in Jakarta, and he was appointed member of the Board of Cemex Asia, Ltd. In February 1999 he joined the Telefónica Group as General Manager of Finance for Telefónica International, S.A. In September of the same year he was promoted to Chief Financial Officer of Telefónica. In July 2002, he was appointed

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Chairman and Chief Executive Officer of Telefónica Internacional, S.A., in July 2006 General Manager of Telefónica Latin America, and in March 2009, Chairman of Telefónica Latin America. Mr. Álvarez-Pallete holds a degree in Economics from the Complutense University in Madrid. He also studied Economics at the Université Libre de Belgique and holds an International Management Program from the Pan-American Institute of Executive Business Administration (IPADE) and a Diplome of Advanced Studies (DEA) from the department of financial economics and accounting of the Complutense University of Madrid.

Mr. José Fernando de Almansa Moreno-Barreda serves as a Director of our Board of Directors. In December 1974 he joined the Spanish Diplomatic Corps (Cuerpo Diplomático) and served from 1976 to 1992 as Secretary of the Spanish Embassy in Brussels, Cultural Counsellor of the Spanish Delegation to Mexico, Chief Director of the General Coordination Branch of Eastern Europe, Director of Atlantic Affairs in the General Directorate of Foreign Policy for Europe and Atlantic Affairs, Political Counsellor to the Spanish Permanent Representation to NATO in Brussels, Minister-Counsellor of the Spanish Embassy in the Soviet Union, General Secretary of the National Commission for the 5th Centennial of the Discovery of the Americas and Deputy General Director for Eastern Europe in the General Directorate of Foreign Policy for Europe. From 1993 to 2002, Mr. Fernando de Almansa was appointed Chief of the Royal Household by His Majesty King Juan Carlos I, and is currently personal advisor to His Majesty the King Juan Carlos I. He is also a Director of Telefónica Brasil S.A., and of Telefónica Móviles México, S.A. de C.V. and a Deputy Director of Grupo Financiero BBVA Bancomer, S.A. de C.V. and of BBVA Bancomer, S.A. He holds a law degree from the University of Deusto (Bilbao, Spain).

Ms. Eva Castillo Sanz serves as a Director of our Board of Directors. Ms. Castillo began her career at the Spanish broker Beta Capital Sociedad de Valores, S.A., where she worked for five years. After that, she worked for another five years for Goldman Sachs International in London in the International Equity Markets Department. In 1997, Ms. Castillo joined Merrill Lynch as head of Equity Markets for Spain and Portugal. In 1999, she was promoted to Country Manager for Spain and Portugal and in 2000 she became Chief Executive Officer of Merrill Lynch Capital Markets Spain. After that, Ms. Castillo was appointed Chief Operating Officer for EMEA Equity Markets. In October 2003, she was appointed head of Global Markets & Investment Banking in Spain and Portugal, as well as president of Merrill Lynch Spain. Until December 2009, she headed Global Wealth Management business operations in Europe, the Middle East and Africa, including Merrill Lynch Bank (Suisse) and the International Trust and Wealth Structuring business. She was a member of the Merrill Lynch EMEA Executive Committee, the Global Wealth Management Executive and Operating Committees. Ms. Castillo was Chairwoman of Telefónica Europe and a member of Telefónica's Executive Committee from September 2012 to February 2014. Currently, Ms. Castillo is the Chairperson of the Supervisory Board of Telefónica Deutschland Holding AG, member of the Board of Directors of Bankia, S.A., of Visa Europea and of the Telefónica Foundation. She is also a member of the Board of the Comillas-ICAI Foundation and member of the Board of Entreculturas Foundation. Ms. Castillo holds degrees in Business and Law (ICADE – E3) from the Universidad Pontificia de Comillas of Madrid.

Mr. Carlos Colomer Casellas serves as a Director of our Board of Directors. Mr. Colomer began his career in 1970 as Marketing Vice-Chairman of Henry Colomer, S.A. In 1980, he was appointed 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 Chairman of Revlon International and in 1990, he was appointed Executive Vice-President and Chief Operating Officer of Revlon Inc. in New York. In 2000, he was appointed Chairman and Chief Executive Officer of The Colomer Group. Currently, he is Chairman of Ahorro Bursátil, S.A. SICAV, Inversiones Mobiliarias Urquiola, S.A. SICAV, Haugron Holdings S.L, MDF Family Partners and Abertis Infraestructuras S.A. Mr. Colomer has a degree in Economics from the University of Barcelona and an MBA from IESE Business School.

Mr. Peter Erskine serves as a Director of our Board of Directors. He began his career in the field of marketing in Polycell and in Colgate Palmolive. He worked for several years at the Mars Group, serving as Vice-Chairman for

Europe of Mars Electronics. In 1990 he was appointed Vice-Chairman of Marketing and Sales of Unitel. From 1993 to 1998, he held a number of senior positions, including Director of British Telecom (BT) Mobile and President and Chief Executive Officer of Concert. In 1998 he became Managing Director of BT Cellnet. Subsequently, in 2001 he became Chief Executive Officer and a Director of the Board of Directors of Telefónica Europe, Plc. In 2006 he became Executive Chairman of Telefónica Europe, Plc (until December 31, 2007, after which he became a Non-Executive Director) and from July 2006 until December 2007 he served as General Manager of the business unit Telefónica Europe. In January 2009 he joined the Board of Ladbrokes Plc. as a Non-Executive Director, becoming Chairman in May 2009. Currently, he is also Chairman of the Advisory Board of Henley Management Centre, and a member of the Council of Reading University. In 1973, he received a degree in Psychology from Liverpool University.

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Mr. Santiago Fernández Valbuena is Chief Strategy Officer (CSO) and Chairman of Fonditel since February 2014. He is also a member of the Board of Telefónica S.A. and Deputy Chairman of Telefônica do Brasil. He has been Chairman & CEO of Telefónica Latin America (2011-2014), Chief Finance and Strategy Officer (2010-2011) and Chief Financial and Corporate Development Officer (2002-2010). Throughout this period he was also responsible (not continuously) for Procurement, IT, HR, Internal Audit and Subsidiaries (Atento, Endemol). From 1997 to 2002 he was CEO of Fonditel, the pension fund manager for Telefónica. Since 2008 he serves as Independent Director at Ferrovial S.A. and member of its Audit Committee. Before joining Telefónica he was Managing Director at Société Générale de Valores and Head of Equities at Beta Capital in Madrid. He holds a degree in Economics from the Complutense University of Madrid, a PhD and a Master's degree in Economics from Northeastern University in Boston. He has been a Professor of Applied Economics at Complutense University in Madrid and the Universidad de Murcia and has lectured at Instituto de Empresa (IE Business School) in Madrid.

Mr. Alfonso Ferrari Herrero serves as a Director of our Board of Directors. From 1968 to 1969 he was Assistant to the Financial Manager of Hidroeléctrica del Cantábrico, S.A. From 1969 to 1985, he worked in Banco Urquijo, S.A. holding several positions as Analyst, Manager of Industrial Inve