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THE WORLD BANK

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President Wolfensohn - Briefings Books for Presidents Meetings - Meeting Materials
Courtesy Call - Ambassador Mickey Kantor - December 15, 1997

Courtesy Call: Ambassador Mickey Kantor

Monday, December 15, 1997

12:30 - 12:45 p.m.

JDW Office

Archive Management for the President's Office

Document Log

Reference # : Archive-01856

12/15/97

Edit

Print

A. CLASSIFICATION

☒	Meeting Material
☐	Trips
☐	Speeches

☐	Annual Meetings
☐	Corporate Management
☐	Communications with Staff

☐	Phone Logs
☐	Calendar
☐	Press Clippings/Photos

☐	JDW Transcripts
☐	Social Events
☐	Other

B. SUBJECT: COURTESY CALL: AMBASSADOR MICKEY KANTOR (N)//
TIME: 12:30 - 12:45 P.M. // VENUE: MC 12-750 (OFFICE) // CONTACT:
JACQUELINE CUNDIFF @ 778-0163 // FAX: 955-6458 // WB CONTACT:
SABINE @ 31110 // IN ATTENDANCE: JDW
EXTERNAL ATTENDEES: MICKEY KANTOR, IGNACIO DE BENITO,
DIRECTOR-GENERAL, TELEFONICA INTERNACIONAL, GASPAR ARINO,
MEMBER OF BOARD, TELEFONICA DE ESPANA / MANAGING PARTNER,
ASESORES JURIDICOS AGRUPADOS, S.L. (MADRID), BARRY MACHLIN,
ATTORNEY, MAYER, BROWN AND PLATT, NOTE: AMB. KANTOR WANTED
TO INTRODUCE MR. BENITO OF TELEFONICA TO JDW, 11/20 JDW AGREED
TO MTG PER DEANA // 12/01 CFMD VIA FAX, EXC: JDW // LFG (11/20)
Brief includes:
--- Briefing Note to JDW from Assaad J. Jabre
--- Grupo Telefonica Annual Report 1996
--- Ignacio de Benito's Bio
--- Gaspar Ariño Ortiz's Bio
--- Barry N. Machlin's Bio

DATE: 12/15/97

C. VPU

Corporate

☐	CTR
☐	EXT
☐	LEG
☐	MPS
☐	OED
☐	SEC/Board
☐	TRE

Regional

☐	AFR
☐	EAP
☐	ECA
☒	LAC
☐	MNA
☐	SAS

Central

☐	CFS
☐	DEC
☐	ESD
☐	FPD
☐	FPR
☐	HRO

Affiliates

☐	GEF
☐	ICSID
☒	IFC
☐	Inspection Panel
☐	Kennedy Center
☐	MIGA

D. EXTERNAL PARTNER

☐	IMF
☐	UN
☐	MDB/Other IO
☐	NGO
☒	Private Sector

☒	Part I
☐	Part II
☐	Other

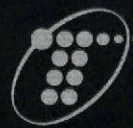
E. COMMENTS:

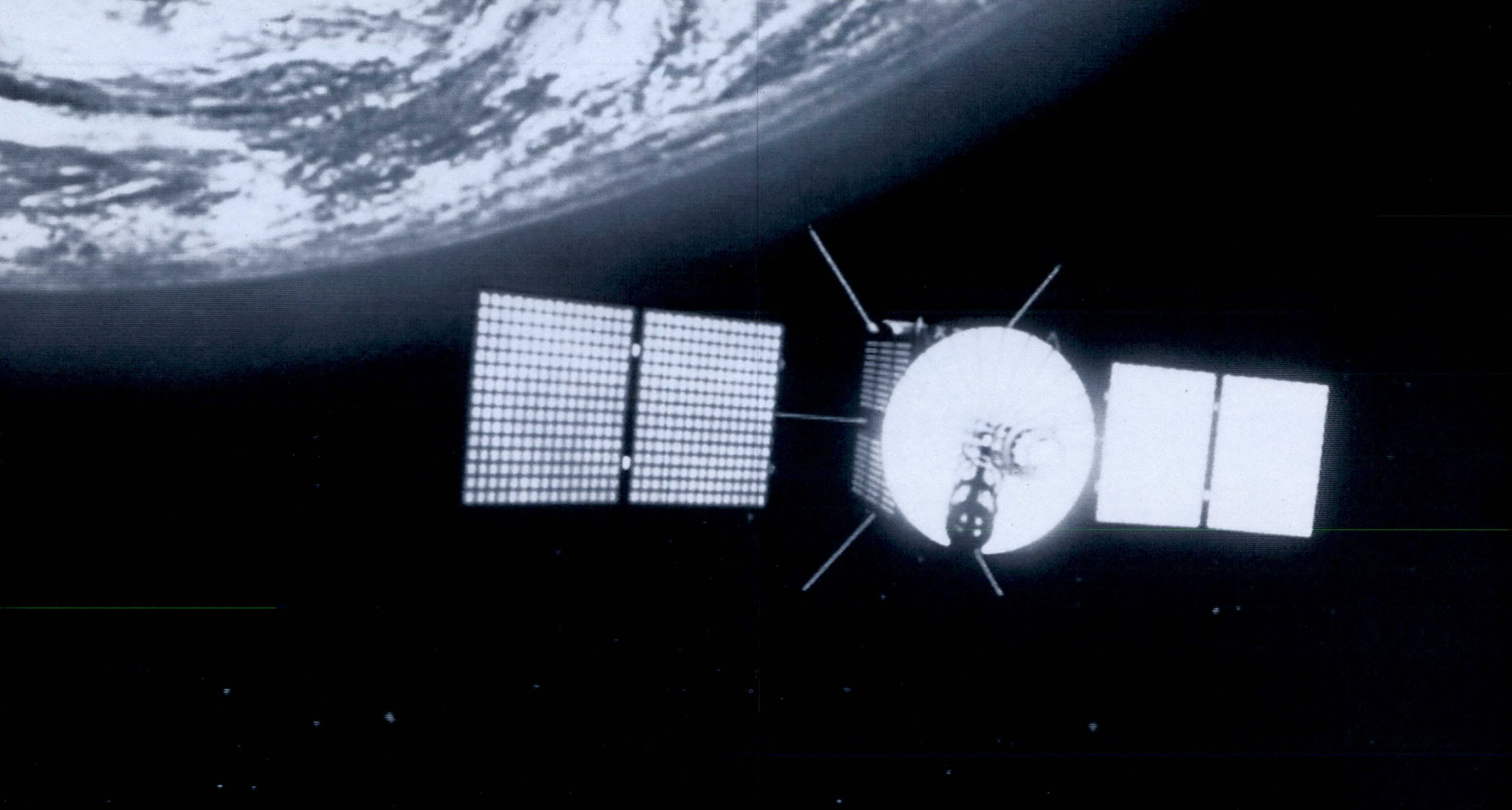
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Grupo Telefónica

ANNUAL REPORT 1996

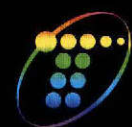




ANNUAL REPORT 1996

Grupo Telefónica

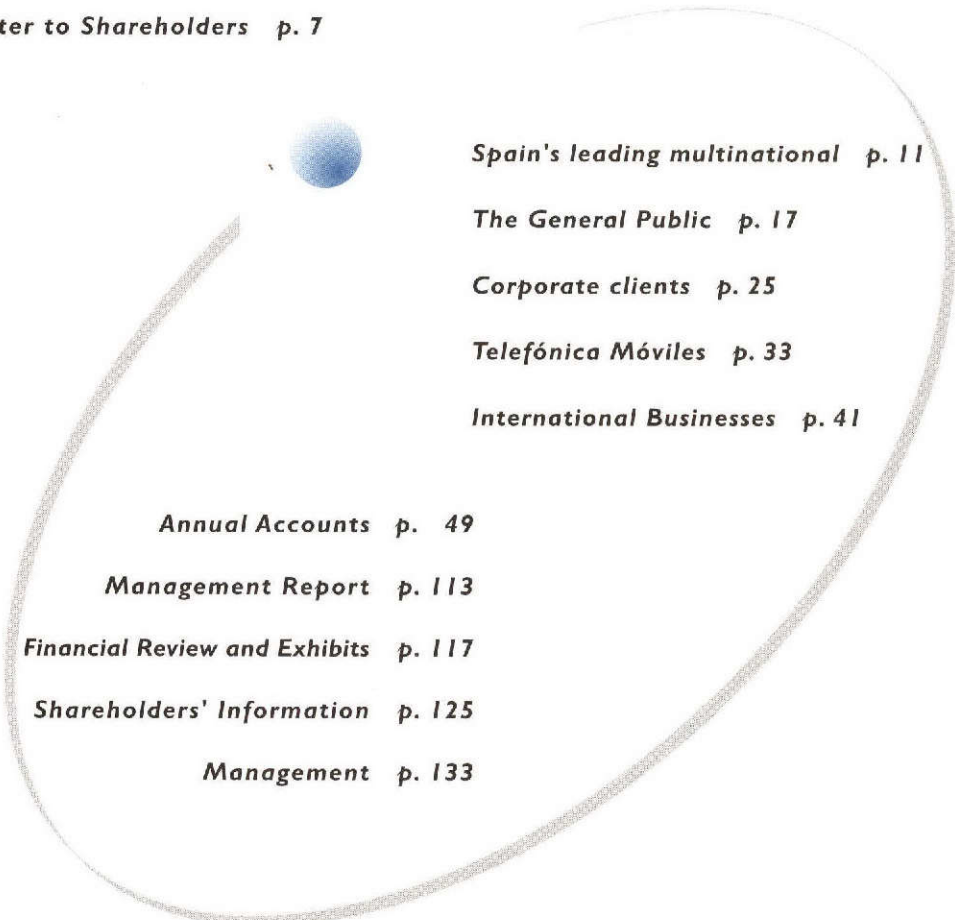
ANNUAL REPORT 1996





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TELEFONICA GROUP: HIGHLIGHTS

	1992	1993	1994	1995	1996
Lines in service (thousands)	19,328.8	20,614.4	22,683.0	24,247.3	26,477.1
Basic telephony *	13,792.2	14,253.5	14,685.4	15,095.4	15,412.8
IBERCOM *	460.6	548.3	622.2	651.3	691.3
ISDN *	—	0.6	5.4	28.0	96.0
Abroad **	5,076.0	5,812.0	7,370.0	8,472.6	10,277.0
Cellular subscribers	232,300	419,543	726,242	1,375,519	3,329,398
MoviLine (analog) *	180,296	257,261	411,930	892,187	1,307,929
MoviStar (GSM) *	—	—	—	36,768	1,037,716
Abroad **	52,004	162,282	314,312	446,564	983,753
Cable TV subscribers	—	—	55,861	774,989	1,149,260
In Spain	—	—	—	—	—
Abroad **	—	—	55,861	774,989	1,149,260
Employees ***	83,802	84,056	103,938	99,203	92,148
Revenue from operations (million pesetas)	1,208,938	1,297,437	1,578,850	1,740,557	2,006,058
Debt ratio (%)	58.4	57.6	54.5	51.6	47.5
Capital expenditure (million pesetas) ****	469,942	445,274	810,655	663,851	867,197
Cash flow (million pesetas)	465,250	502,882	644,750	750,357	811,235
Net income (million pesetas.)	80,761	96,367	112,608	133,214	160,282

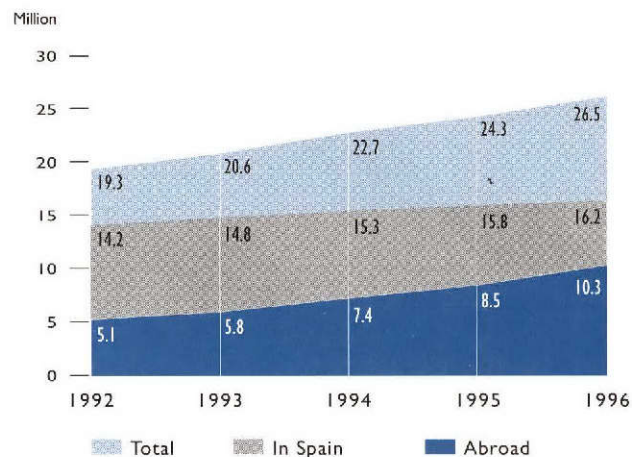
* Figures for Spain.

** Lines in service include those of TASA, CTC, Telefónica del Perú, CANTV and CRT. Cellular subscribers also include those of Cotelco and Telefonica Romania. Cable TV customers correspond to CTC, Telefónica del Perú and Multicanal.

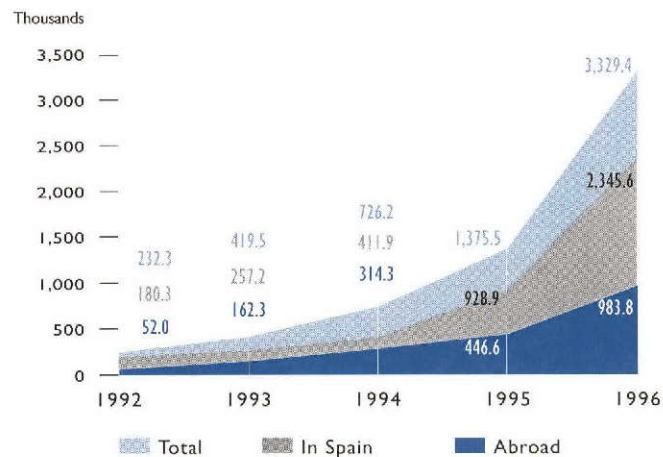
*** Average number for the year. At year-end 1995 and 1996 the workforce totalled 96,746 and 91,457 employees, respectively.

**** Tangible, intangible and financial.

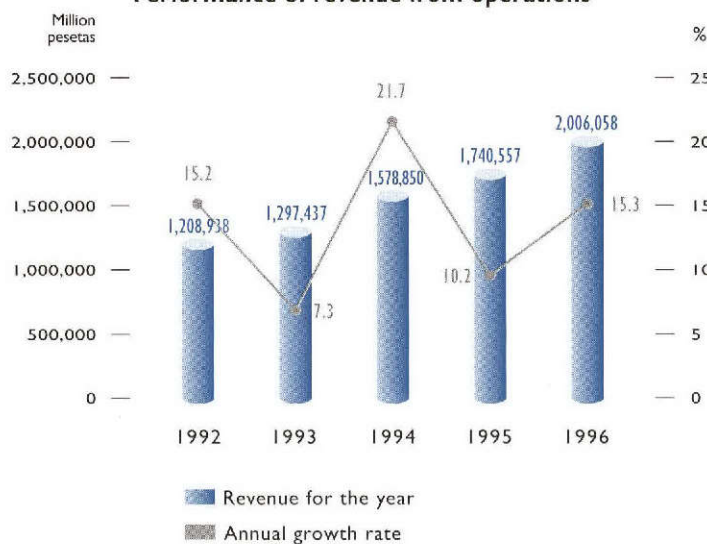
Performance of lines in service



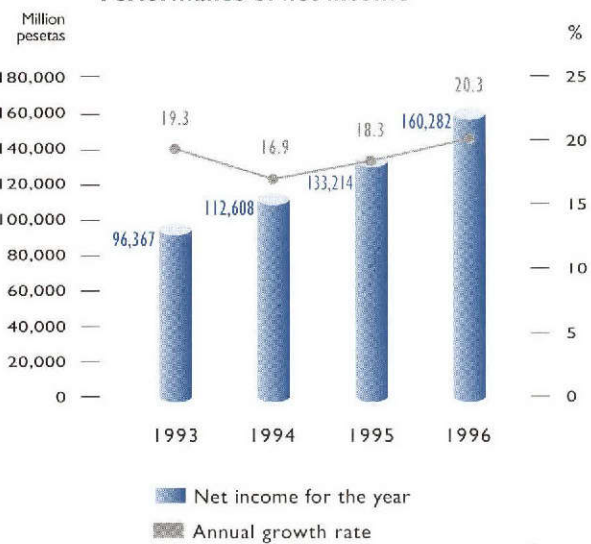
Performance of cellular subscribers



Performance of revenue from operations



Performance of net income





Letter to Shareholders

Dear Shareholder,

DURING THESE INITIAL MONTHS AS Chairman of Telefónica, I consider myself a privileged participant in the final stages of a long and productive period, during which we served the public under the aegis of the Spanish State. We now open a promising new era, in which Telefónica will continue to guarantee service to Spain and to its customers within a liberalized market and a highly competitive environment.

The Public Offering of the balance of State's participation was highly successful. Telefónica now ranks among the European companies with the largest number of shareholders, with roughly one in every eight Spanish families holding our shares. In this way, we have not only strengthened our shareholder base, but also given many Spaniards a heightened sense of personal commitment to the development of the economy.

Telefónica, Spain's leading multinational company, must be managed with the same high standards set by the largest and most successful corporations worldwide. To this end, our Board of Directors has passed a set of internal rules governing the Board's function. The Board has also welcomed new independent Directors, who do not form part of our management structure, in a measure designed to foster greater transparency, impartiality and professionalism in the Board's dealings, and to guarantee that the interests of all Telefónica shareholders are adequately defended.

I should also point out that the new internal governance rulings provide for the creation of supervisory commissions for Audit and Control, Personnel and Remuneration, and International Strategy functions. In this way, Board Members assume an active role in the management and control of the Company.



When you, the Shareholders, approve the new Board of Directors at the General Shareholders' Meeting, you will be acknowledging the professional credentials and prestige of these new independent Members. They will sit on the Board with Directors representing the majority shareholders and with Telefónica executives who so ably support me in the day-to-day management of the Company.

These measures aim at contributing to increased value for the shareholders in a fully-privatized Telefónica. Value will be generated by increased share price and dividend yield while offering a stable and reliable investment.

We can only reach this goal by offering our customers top-quality service, a commitment to be made by everyone who works at Telefónica.

With a customer base exceeding 23 million, Telefónica holds a position of unrivalled leadership in Spanish-speaking markets. During 1996, Telefónica reported a net profit of 160,282 million pesetas, representing a 20.3 % gain over the previous year. In parallel, our share price showed a positive upward swing and was quoted at 3,365 pesetas on February 18, the day after final privatization of the Company. This figure represented a 370-peseta increase over the price at the close of trading on December 20, date of the Government's formal announcement of the Public Offering.

We intend to make Telefónica become increasingly global, competitive, efficient and profitable, thus ensuring enhanced profits for our shareholders.

Our strategic objective, "*Telefónica, a global operator*", sets forth very positively our determination vis-à-vis a newly competitive telecommunications environment. As undisputed leader of Spanish-speaking markets, Telefónica is solidly positioned to face the challenge posed by the progressive liberalization of the telecommunications sector. We view the creation of regulatory authorities as a positive move to ensure a fair and equitable competitive environment which safeguards consumer interests. Our ability to compete has been put

to the test and we are convinced of our ability to meet client needs in a broader marketplace.

This new dynamism is fully compatible with our tradition of public service, a vocation which has strong roots in Telefónica's corporate culture. It takes the form of constant attention to client needs and demands, and our contribution to the economic development and technological advance of our country.

Finally, in this first appearance as Chairman before the General Shareholders Meeting, I do want to extend a warm welcome to all of our shareholders, both those of long-standing and those who are joining to us now for the first time. You may rest assured that together we shall reach the objective of consolidating Telefónica's unrivalled leadership in Spanish-speaking markets, while bringing the Company to the first rank of worldwide telecommunications operators.

A handwritten signature in blue ink, reading "Juan Villalonga". The signature is fluid and cursive, with a long vertical stroke on the left side of the name.

Juan Villalonga Navarro

CHAIRMAN AND CEO OF TELEFÓNICA



Spain's leading multinational

1996 has witnessed the consolidation of the Telefónica Group's leading position within the newly-created global telecommunications market. The policy of expansion into new markets, developed over the past few years, has achieved a business volume that has made Telefónica Spain's foremost multinational.

At the same time, and in line with the liberalization policies being introduced in the sector, at both a European and world level, these have resulted in a separation between regulatory organisms and operators, and a general trend towards privatization has been reflected by leading operators. With this in mind, the Spanish government decided to totally privatize Telefónica de España's share capital at the beginning of 1997. All the tranches of the Public Offering, launched at the beginning of 1997, have been highly successful, registering more than one million new investors, attracted by the excellent performance of our shares: at the end of October 1995 our share price stood at 1,615 pesetas, whereas, at the end of 1996, when the new Public Offering

was announced, our share price had soared to over 3,000 pesetas, 79% growth in less than a year; and almost double the growth reflected by the Spanish stock market. Demand exceeded 5.45 times the 196 million state-owned shares on offer.

1996 was also a year of profound restructuring, taking advantage of the experience and capacity gleaned in the more than seventy years that Telefónica has operated in the telecommunications marketplace with one clear objective: to provide our shareholders with a high degree of profitability on an investment that not only offers yield, but also inspires a sense of security and continuity. In order to achieve this, clear market orientation and customer satisfaction are vital, along with the confirmation of our capacity to face the challenges posed by the competition.

With this objective in mind, the Telefónica Group's business strategy is based on the firm commitment to maintain our leading position in all the telecommunications markets, especially those of Latin America; the



consolidating of our ever-increasing presence internationally and the maximizing of the Group's potential and synergies. Telefónica is moulding itself into a global telecommunications operator with the capacity to provide the wide range of services demanded by our customers, in markets that often cross our national frontiers.

The new organization

A key point in this process is the reorganization of the Group's business units, which was carried out at the end of 1996, based on the clear defining of our customers and the segmenting of our markets in order to consistently offer «made-to-measure» services. This new structure allows us to provide a highly competitive range of services, therefore taking advantage of the potential that each market has to offer:

The Telefónica Group's customers form five large groups: corporate clients, the general public, mobile telephony users, our Latin American customers and the customers in those countries in which we intend to operate or already have

interests. With this in mind, five Business Units have been created, each of which focuses on its respective market. These Units are the following: Retail Clients, Corporate clients, Telefónica Móviles, Telefónica Internacional, and International.

Each Unit is entirely responsible for its own area, from the designing of the products to be marketed, to the setting of prices and the drawing up of publicity campaigns or the control of their distribution lines.

This autonomous management of each business line is complemented by the existence of the Corporate Centre which oversees the Group's business orientation at all times, with a view to fostering the Group's synergies. There are also two Common Resources Units (Infrastructures and Resources) which are responsible for providing their services to the previously mentioned Units.

The entire organization is managed by the Management Committee which is the decision-making body and draws up

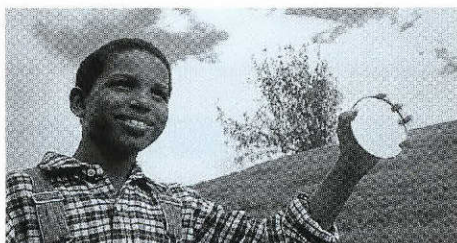
Telefónica Group's Management Committee



the proposals to be made to the Executive Committee and the Board of Directors. The Management Committee is made up of the Chairman, and those responsible for the Corporate Core, the Business Units and the Common Resources Units.

The Board of Directors has taken a more active role in the management and control of the Company, guaranteeing the financial markets a high

degree of transparency. New independent members have joined the Board, all of whom are outstanding professionals with vast experience, not only in the business world but also in legal matters.



Our priorities ... and their goals

Coinciding with the remodelling of our organization, the Telefónica Group laid down a series of priorities aimed at expanding and innovating the telecommunications business in the countries where the Group has a strong foothold, at the same time as consolidating the Group's position as the unquestionable leader in the mobile business and, making Telefónica a company with worldwide presence in its own right, or through the forming of alliances and the optimizing of the portfolios of our subsidiaries.

This remodelling task is being confronted using sound policies regarding the undertaking of ambitious projects to improve the selecting of



assets and investments, and increased productivity levels.

The consolidating of our leadership in mobile telephony

Mobile services have come to play a vital role in any telecommunications company; mobile telephony has become a huge communications system, not only used by individuals, but also as the communication among computers, and the Telefónica Group therefore intends to consolidate its leadership not only in Spain, but also in international markets.

The development of businesses outside Spain

At a moment in which the growth possibilities within Spain (at least regarding our traditional businesses) are going to be influenced by the action to be taken by the competition, it is crucial that all potential opportunities for new businesses must be taken advantage of. Therefore, one of our main priorities is that of confirming our leadership in the Latin American markets; another is that of accessing new markets.

Communication
is making the World smaller
and our Company bigger

Regarding the Latin American markets, three lines of action have been drawn up: maximum advantage must be taken of the current high growth potential offered by these countries; the panamerican project must be exploited to the full, as this is going to offer companies a made-to-measure communications services operator; and, finally, we must storm the Spanish-speaking North American market, as this is made up of approximately 30 million inhabitants. We would like to take this opportunity to remind you that Telefónica Larga Distancia de Puerto Rico has been authorized to offer domestic traffic throughout the whole of the United States.

In relation to our other markets, we have recently begun to investigate the business possibilities in North Africa and Asia. Contact has already been established with the Moroccan operator which is forecast to be privatized in 1997, and throughout the year visits will be made to other countries in the area. Concerning Asia, we intend to access its markets through the forming of alliances, as we did in Latin America.



Optimizing the value of other subsidiaries

The Group also has other companies with significant value and high development potential, namely: Telyco, Cabitel, Telefónica Publicidad e Información, the Telefónica Sistemas Group, Telefónica Transmision de Datos, and Telefónica Multimedia.

We will expand on the evolution of our different business units on subsequent pages.



Retail Clients

This market segment, with 12.5 million customers, represents one of the principal Business Units within the Telefónica Group's recent restructuring. This Unit has two main targets which are, to increase the profitability of our services and new businesses, and to raise margins. In order to achieve this we have introduced a series of marketing channels into the market by which the customer has become the focal point of our business. One example of this policy is that throughout 1996 seventy new products and services were introduced.

Solutions incorporated into the basic telephone service

Over 1996, the degree of digitalization of the access plant, with 16.3 million lines, increased significantly to reach 67.4%. This has enabled us to enhance the range of services on offer to include such services as Itemized Billing, which is available to 14.1 million lines. Throughout 1996, this charge-free service grew by 29.5%, also offering the customer itemized billing of metropolitan calls on request. At the

same time, we completed the studies necessary to be able to provide the customer with more informative billing, in line with his/her needs.

Telephone usage

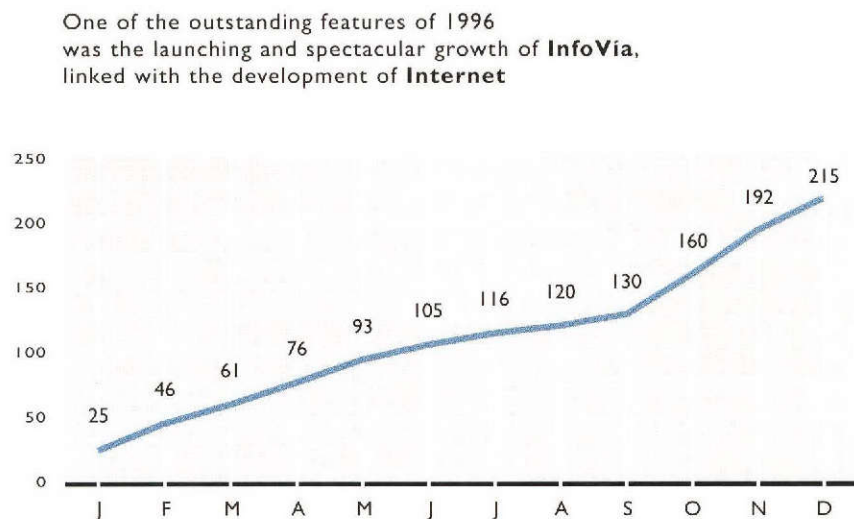
Usage per line rose more than 9% throughout 1996, with the performance registered by fixed-mobile traffic being particularly outstanding, having grown by 100%.

Regarding the attention to demand for lines, the waiting period stood at an average of three days, compared with four the previous year.

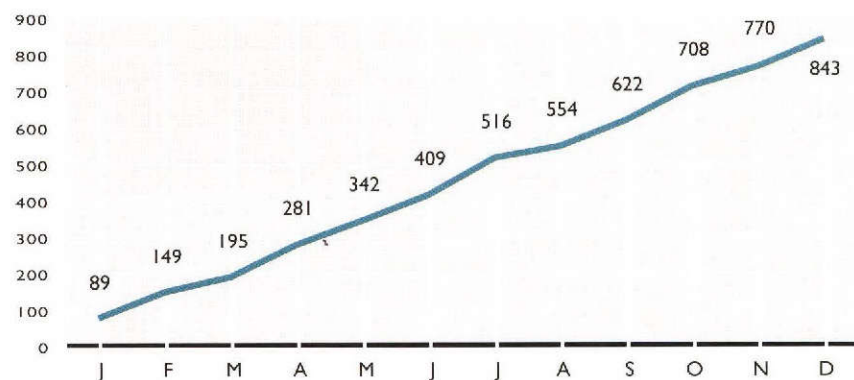
Star services

In 1996 a huge publicity effort was made, launching campaigns on all the media channels, television, radio and newspapers, and through new commercial platforms and direct marketing. These campaigns aimed to increase the usage and penetration among the general public of such services as: Call Waiting, Call Forward, etc. At December 1996, the number of

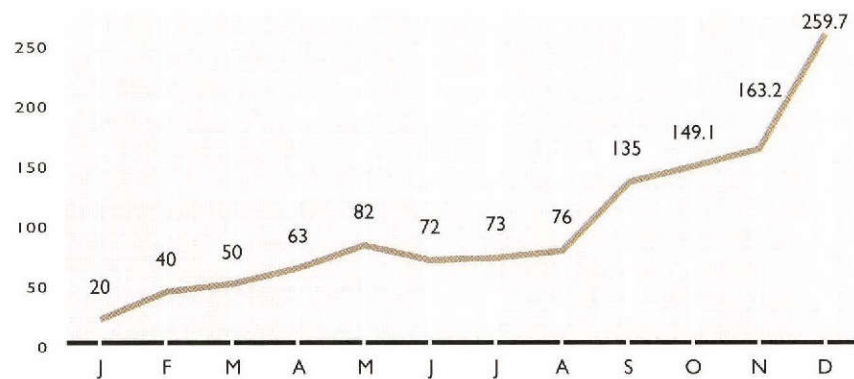
Number of lines
(Thou.)



Information provider centres



Calls - daily average
(Thou.) (*)



* Since June, calls of less than 30 seconds are not accounted

lines using these new services had risen 40%, to total 1,151,771.

The Telefónica Group's continuous effort to increase its direct relationship with the customer was also reflected in the national launching of the Answering Service, the «star» of the supplementary services. This service allows the customer to retrieve unanswered telephone calls or calls received while the line is engaged, without the need to install any additional equipment.

The convenience and user-friendly handling of this service, combined with the fact that the customer retrieves the calls free-of-charge from his/her home, and that the service is provided in the varying local languages of Spain, has made this service extremely popular, so much so that at year-end 1996, the number of telephone lines provided with this service totalled 4,041,256.

InfoVía/Internet

In response to the market's demands for electronic information, the InfoVía

service was launched at the beginning of 1996. This service offers Telefónica customers owning a PC to access all the service and information providers throughout Internet. In the course of the year, InfoVía became a universal information access channel to information highways both within Spain and abroad, and has come to represent Internet's principal expansion vehicle in Spain.

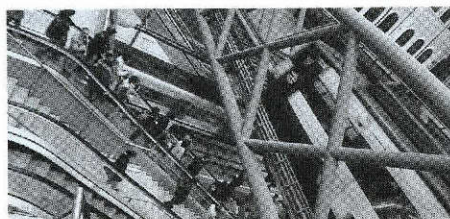
Over the twelve-month period, the effort made to extend this «star» service paid off, as the following record figures were achieved: 843 information service providers, 215,000 lines used to access the InfoVía service, and 36 million calls registered, resulting in a total of 10 million connection hours. Telefónica is also pioneering the export of this service to those Latin American countries in which it is already an established telecommunications operator.

InfoVía is also the gateway to Virtual TeleSpacio, through whose surfing system the shop may be accessed and purchases made, using a PC.



Service catalogue aimed at increasing profitability

Throughout 1996, more than one million telephone sets were sold, ranging from basic telephones with specific supplementary facilities to those that embody an answering machine or both an answering machine and fax, and particularly the most popular models such as cordless telephones.



Continuous customer service and sales

Our new Telemarketing system and our Customer Care Telephone Service (for which Telemanagement and Telesales 004 are responsible) aim to attend to our customers 24-hours a day, 365-days a year. At year-end 1996, over 80% of our customers were already receiving 24-hour attention, and more than 12.6 million calls had been attended to, therefore confirming this service to be Telefónica's most active sales channel, having generated more than 40% of the sales registered.

Distribution network through TeleSpacio

This distribution system, which has been in existence since May 1996, permits a personal approach to our customers and allows us to continuously adapt to their needs.

The four shops now attending to our customers (two in Madrid and two in Barcelona) are unique premises where, not only can our customers purchase our products and services, but he/she will also be provided with information on over 200 Telefónica products and services. Every one of these shops is equipped with a state-of-the-art telecommunications infrastructure that offers seven interactive audio-visual systems with a duration of more than four hours: access in real time to different services (Infovia, Internet, Teleline, Videoconferencing,...), a pilot channel of video-on-demand, screens offering digital satellite TV, and the most advanced broadband technology under development.

TeleSpacio, representing the most «visual» section of our new commercial network, will soon bring us closer to our customers through an extensive network of shops - both Telefónica-owned and through franchise agreements - and a distribution network which will include department stores, commercial malls and small retail outlets.

**Millions of people in 18 countries
speak, do business and communicate
via Telefónica**

**Personal attention to
our customers**

This customer approach policy also includes a sales channel of extreme importance which uses two direct marketing tools, these being Telesales and Personal Attention, accessed through the freephone number 900 123 004 managed by Estratel. This subsidiary has one of the most advanced technological platforms, enabling it to offer a wide range of products and services, at the same time as guaranteeing their quality and competitiveness. In 1996, its market share stood at 23.2%, compared with 14.8% the previous year.

Another key channel within the distribution network is that of the Telefónica subsidiary Telyco, which has more than 1,500 sales and customer care points throughout the country, where the customer is provided with a complete range of services. In 1996 it registered turnover totalling 55,000 million pesetas, and its logistic activity has become particularly significant in providing the customer an integral

service. These services aim to achieve maximum customer loyalty.

Continuous customer care

Customer care forms an essential part of the Telefónica Group's policy to improve quality. With this in mind, in 1996, our Operator and Inquiry Services reflected considerable improvements. The rate of attention to calls - more than 218 million calls were received - reached 95.1%, almost 6 percentage points higher than the previous year. This service uses highly professional operating resources, therefore reflecting significantly improved productivity. As a result of this strategy, all the Spanish provinces received the AENOR quality rating of ISO 9000.

Tariff cuts

Telefónica continued its strategy regarding international communications, through the cutting of the prices of all its communication services and, also, offering high volume customers special discounts. In July, an average 13.3% price



cut was introduced, which, combined with the cuts that took place at the end of 1995, resulted in a overall decrease in international tariffs of around 25% in under a year. Telefónica has announced that in 1997 further cuts will be introduced in international and long distance tariffs, along with a price-freeze in metropolitan calls.

**Telefónica Publicidad
e Información**

Within the General Public business unit, mention must be made of the 26% penetration level in potential market achieved by Telefónica Publicidad e Información (TPI), through its principal



product, Yellow Pages, as this penetration level is on a par with the European average. With an eye to the future, this company has already begun to renovate the technology of its information systems and therefore plays a vital role in the new information highways. Proof of this was the prize received from the North American Association of Yellow Pages Editors at its IXth yearly convention for TPI's multimedia web site in Internet.

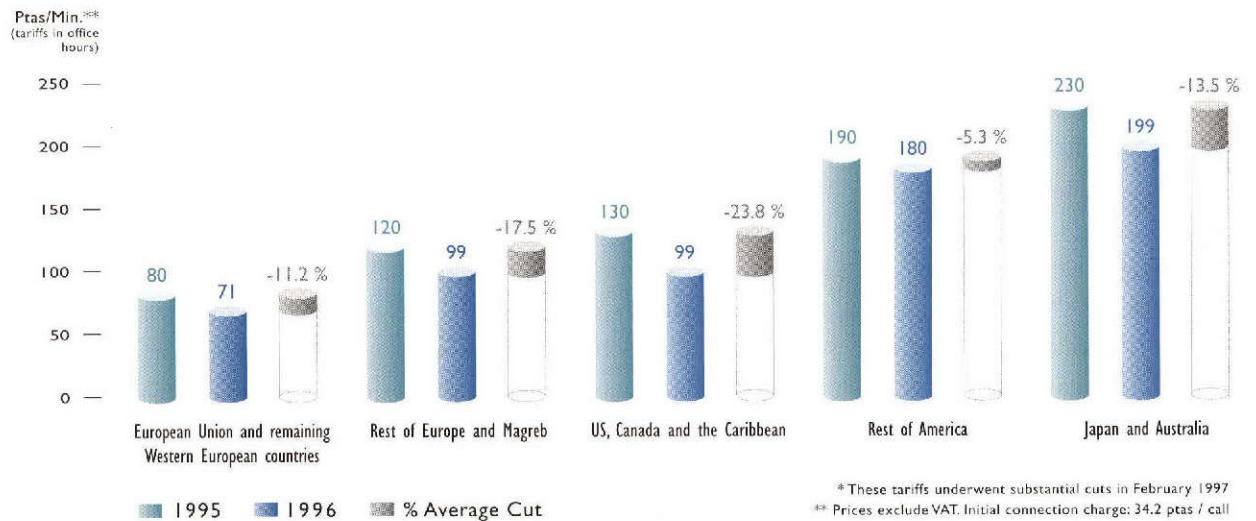
The 15.2% increase in revenue and the 8% rise in customers over 1996, are a

reflection of the consolidation of this company's leadership in all its business lines, not only Yellow Pages, but also direct marketing, telephone marketing - carried out by Estratel- and multimedia products that have developed to such an extent that they are becoming increasingly user-friendly, in response to a dynamic market. Their contribution to customer segmentation is therefore a vital ingredient in the General Public business.

TPI's strategy for the next few years is based on the evolution and

New international tariffs

In force since July 1996*





development of its existing products, providing the value added that the market demands, combined with the introduction of new services developed from the information highways and the commitment to the international expansion of its business lines. With this aim, new Yellow Pages projects for InfoVía and Internet have begun, which will be included in the Telefónica Group's other services such as Infomail and electronic shopping.

Cabitel

Within the framework of liberalized public telephony, Cabitel has continued its expansion to reach 58,234 outdoor public telephones throughout Spain, and 23,685 indoor public telephones. Likewise, the effort made in the development of prepaid telephone cards should also be underlined, as this has become the most highly used electronic system, having grown 20.1%, measured by the nominal value of the cards sold. At year-end 1996, this company's turnover had risen 20.2% to total more than 40,960 million pesetas.

Digital television

Telefónica has entered the digital television market as a step towards the launching of an extensive range of interactive multimedia products. In order to manage this business, Telefónica has pioneered the establishing of the company Distribuidora de Televisión Digital (DTD), in which participations are also held by other television broadcasting companies namely, Radiotelevisión Española, Televisa (Mexico), Canal 9, Televisión de Galicia, Telemadrid, Cadena COPE and the publishing groups Grupo Recoletos, Unidad Editorial, Crónicas P. Leonesas, Las Provincias and Epoca. In December 1996, this new company began pilot broadcasting through the satellite Hispasat that offers high quality coverage throughout Spain, part of

Europe and Latin America. The share capital can be increased through the participation of other multinational communications groups.



Corporate Clients

Throughout 1996, the area of the Telefónica Group's Corporate Clients continued to adapt to its new competitive environment, improving quality and developing a policy to satisfy, still further, our customers' product and service needs.

Commercial strategy

The challenge that the Telefónica Group faces is that of satisfying our customers' ever-increasing demands. In order to achieve this, the Company has launched a commercial strategy which focuses on the introduction of market oriented business lines and the achieving of customer loyalty through the implementation of such steps as:

- The development and launching of «made-to-measure» solutions.
- Improved after-sales services.
- Improved management of one-stop-shopping.
- Personal attention.

Corporate clients

Telefónica's growing range of products and services on offer, and its commitment to providing global solutions have been possible thanks to the high stimulus channelled into our commercial network. The Telefónica Group is more than aware of our competitors high degree of activity in this business segment, something that has not prevented us from increasing the revenue derived from this sector by 28.36% and has confirmed our desire to lead the telecommunications market.

Regarding our Corporate Services, the Ibercom service extended its market scope to assist our customers in such areas as: management, configuration, administration, computation control, alarms, graphical presentation of the telephone network's topology, statistic reports and local electronic voice mail servers.

The Intelligent Network continued to reflect growth, both in its number of customers and its range of services on



offer, having introduced the Tele-voting service which is controlled by the customer himself from his PC, and the enhancement of statistic information in order to improve customer attention.

Leased circuits have increased their speeds, therefore raising the digital transmission capacity.

Concerning Data Communications Services, not only have we confirmed our position in the marketplace with such services as those offered by our networks, Iberpac, Iberpac Plus and the Red Uno, but we have also consolidated

the Frame-Relay service providing our customers with high speed transmission of above 256 Kbps. Services such as Data&Voz have also been developed to integrate voice and data over Frame-Relay, along with the Datafono Redelta service and that of Telealarmas Redelta which provide companies with Data Over Voice technology and high-security networks.

In order to promote the usage of the ISDN network, access to InfoVía was completed and new digital telephones and network terminals were launched. The package «Novacom Básico» was also launched, which is vital for connection to the ISDN network and, along the same lines, the package solutions «Novacom Reto» and «Novacom Office» which offer integrated communications solutions to companies. These were not the only new services. Multimedia Videoconferencing was also introduced, which permits the customer to use his/her PC to exchange data, voice and image, and to access such services as Teleemployment and Telemedicine, among others.

The infrastructure necessary for the Autonomous Regions to access the Emergency Service was also introduced. This service provides emergency attendance throughout the whole of the European Union through the dialling of the number 112, wherever the person may be.

**Solutions for small
and medium-sized
companies
(PYMES)
and professionals**

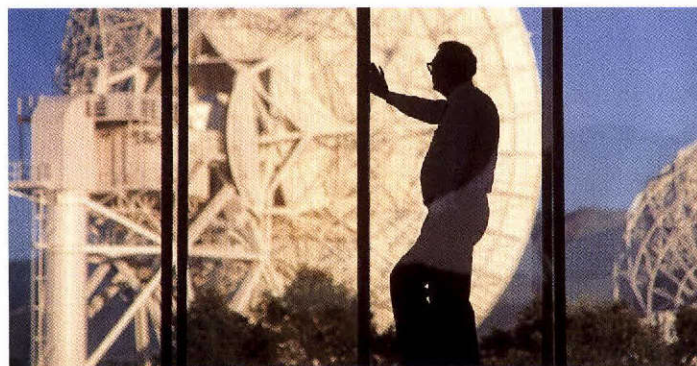
If we take into consideration the number of companies in this segment, combined with their turnover, it can be easily deduced that this represents an expanding market. Telefónica has drawn up a strategy that besides making customer care a priority, has also taken the following steps:

— Business Offices which offer our customers one-stop-shopping, along with direct marketing and customer visits. At the end of 1996, there were 28 of these offices in Spain's major towns and cities.



— Alternative channels for the marketing of Telefónica products and services to PYMES, with 56 registered consultants offering our products and/or services.

— More than 100 seminars, with both an informative and educational focus,



promoting the Telefónica Group's products and services.

The Telefónica Group leads Spain's technological changes

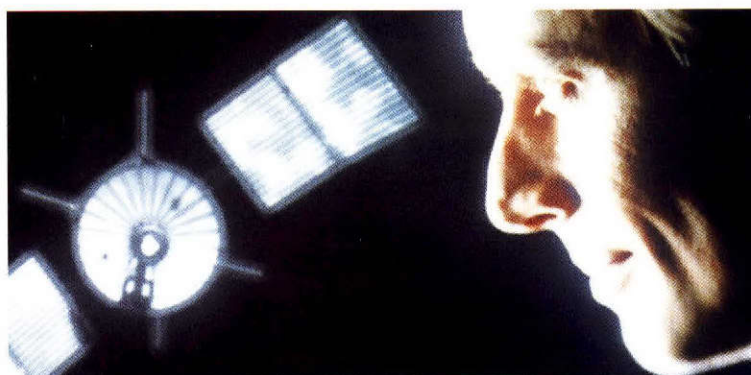
The new advances being made in telecommunications technology result in the introduction of new products and services in the market, thus allowing the Telefónica Group to further improve its attention to the millions of customers that place their trust in us, enabling us to offer them more adequate solutions to their specific needs.



Telefónica I+D has continued to provide all the Group companies with the most varied array of technological solutions to fulfill the customer's needs, at the same time as taking an active role in the European Union's research programmes and attending the most significant international and national events taking place in the sector. It should be underlined that since 1996, Telefónica I+D has presided over the R&D Committee within the Unisource Alliance.

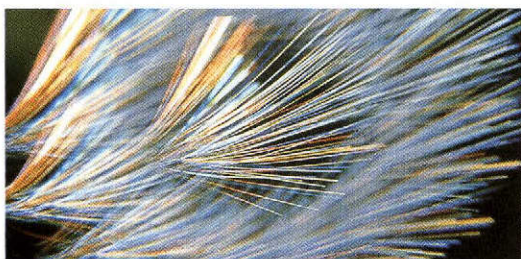
The Telefónica Sistemas Group

Within the objective of enhancing the products and services on offer to our corporate customers, the Telefónica Sistemas Group has concentrated on providing the answer to the demand for high value added services. This has been achieved in close collaboration with all the Telefónica Group's operators, particularly in Portugal, Chile, Argentina and Peru. Since 1993, Telefónica Sistemas has headed a group of companies that operate the infrastructure for public networks, communications services and networks via satellite and systems engineering, to name but a few of our activities. This group is made up of production units that can be called «project factories» as they develop specific projects such as corporate networks, Intranet applications, professional services, applications for mobile services, multimedia, etc. The technology they offer is aimed at telecommunications operators, public administrations, defence, banking, security, transport, distribution, construction, small and



medium-sized companies and the general public. This active presence in the principal business sectors is further strengthened by the participation of the Telefónica Group in the leading markets, permitting alliances with the leaders of each sector.

The Telefónica Sistemas Group is made up of the following subsidiaries: Telefónica Servicios Avanzados de Información, Telefónica Sistemas de Satélites, Telefónica Sistemas Ingeniería de Productos, Telefónica Sistemas Ingeniería de Productos Seguridad, Telefónica Gestión de Sistemas y Telefónica Sistemas de Información Geográfica.



The creation and updating of the network

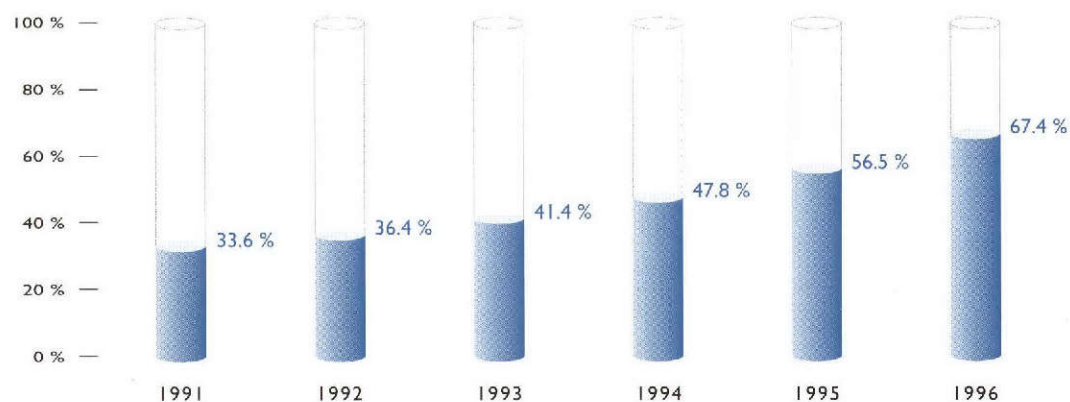
In response to the demand for new services, both by the general public and companies, Telefónica increased its effort to modernize the network, achieving the installation of 2.25 million digital metropolitan lines, 20.5% more than the previous year. Digitalization of the access plant reached 67.4%, while the whole of the transit plant is now digital.

At the same time, the transit network was totally modernized, increasing the

number of trunks in service which permit the carrying of integrated telecommunications services traffic to all the exchanges within the aforementioned network.

We also continued the modernization of our analogue exchanges, initiated in 1995 which, over the year affected more than one million lines in 78 exchanges. This, combined with the increase in digitalization, allowed us to offer itemized billing to 14.1 million basic telephony lines of which 12.7 correspond to the basic telephony

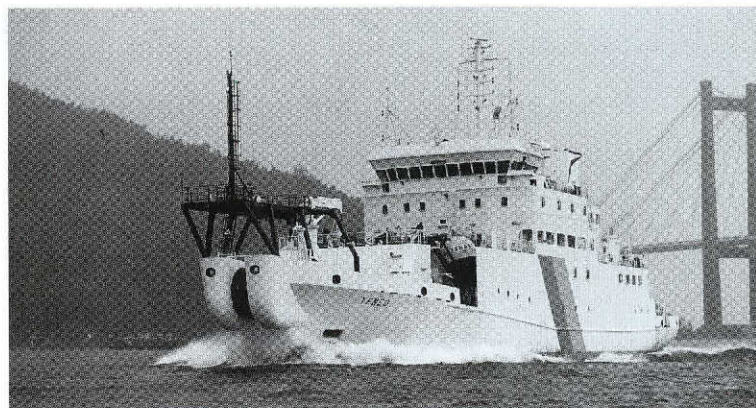
Network digitalization



network (9.4 million lines in 1995) and 1.4 million to ISDN, Ibercom and Rural Telephony through Cellular Access lines. Throughout 1996, the figure of one million kilometres of land fibre optic cable was surpassed since the initiation of the laying of this high technology cable, capable of carrying all types of services.

Finally, over the year, an important step was taken in the development of the multiservice basic network, with the completion of the new network structure with one single transit level, based on double exchange nodes which offer communications with a higher degree of quality and reliability.

Regarding international networks, in December 1996, an agreement for the construction and maintenance of a Panamerican underwater cable was signed, along with the contract for the provision of this underwater cable. This cable will link Chile, Peru, Ecuador, Panama, Colombia, Venezuela, Aruba and St.Croix (the Virgin Islands) with an extension to the island of St.Thomas. Another significant item was the laying



of the Barcelona-Savona underwater cable by the cable-laying ships «Teneo», belonging to our subsidiary Temasa, and the Italian-owned «Teliri».



Telefónica Móviles

It would be difficult to find any other sector within the Spanish economy that over the past few years has witnessed such meteoric growth as mobile telephony did last year.

The figure of almost 3 million customers - 8 of every 100 Spaniards - reflects the qualitative leap that this country has taken in this market, ahead of many other European countries.

Four out of every five mobile telephony customers have opted for our services MoviLine or MoviStar. In consequence, in its first year of complete responsibility for all its operating activities and under competition, Telefónica Móviles has more than proven its position as the leading national operator. This leadership is not only reflected by the number of customers, but also by the higher standard of quality, the more varied price range and the greater number of services on offer, when compared with our competitors. This company's principal aims are to guarantee customer satisfaction, at the same time as enhancing shareholder value and

motivating its workforce by making sure that each employee plays an integral part in the business project. All these things combined have made Telefónica Móviles the unquestionable leader it is today.





At year-end 1996, Telefónica Móviles had doubled, for the second year running, its customer base which stood at 2,345,645, reflecting a 153% increase over 1995. Of this figure 1,307,929 subscribed to the MoviLine service, and 1,037,716 to MoviStar. In consequence, Telefónica Móviles now holds a market share of almost 80%, and what is of even greater

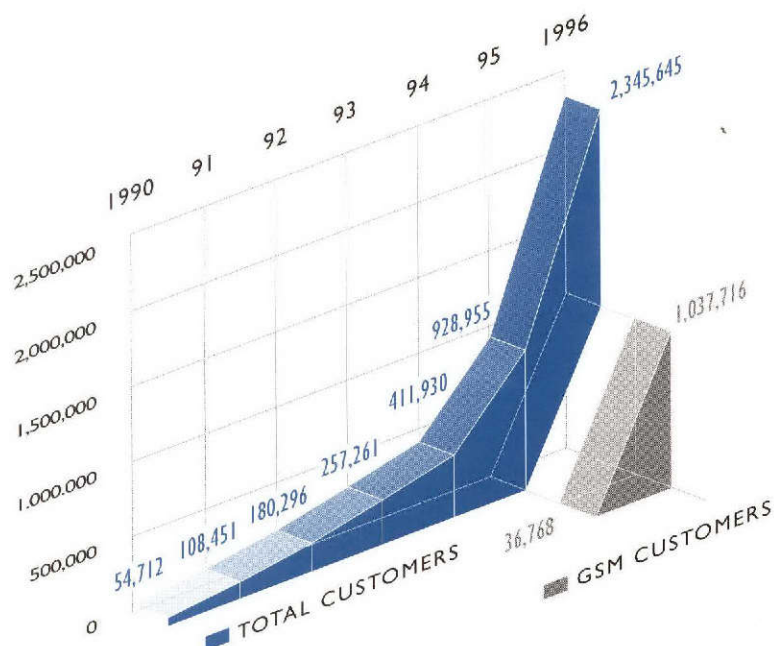
importance, has achieved a differential with its competitor of 1,700,000 customers, an 86% advance over the December 1995 differential.

Some of the milestones in this growth are the following: in January, MoviLine and MoviStar reached the joint figure of 1,000,000 customers which by November had become 2,000,000. Before the end of the year, MoviStar alone had achieved its first million customers, only 16 months after its launching.

Compared with leading European operators, Telefónica Móviles has registered the highest growth rate for the year and is second in its number of new customers, in absolute terms. Therefore, over the past three years the Company has gone from twelfth place to sixth in terms of customers.

This significant growth has been possible thanks to the stimulus that Telefónica Móviles has given the mobile market in Spain, through its extensive distribution network which, with more than 6,600 sales outlets, has enabled us to work

Telefónica Móviles' cellular customers



Consolidating our leadership in mobile communications

more closely with our customers and offer easier access to our services. Telefónica Móviles has gone to great lengths to promote its services and to surmount any barriers in the receiving of new customers, so in a year in which market positions were set, more than 37% of the company's revenue was channelled into marketing.

Service pioneers

Despite the fact that the Spanish market has achieved a certain degree of maturity, with forecast growth rates now becoming more moderate, the road ahead promises to be even harder than what has already been achieved, and, even though mobile telephony is now a part of many Spanish people's lives, its usage still tends to be limited to voice telephony for professionals and 15% of Spanish families. The ground to be covered presents a great challenge for Telefónica Móviles: the extending of the service to other communication areas such as data, text, etc, as the vehicle to increasing the productivity levels of our companies, at the same time as increasing penetration in the

residential market. With this in mind, Telefónica Móviles has launched its new services «factory», introducing an average of one new service per month and proving its capacity to provide the market with applications whose only boundaries will be those of the market's own capacity of absorption.

To name but a few of the new services launched last year: Corporate MoviStar, Multiassistance 2424, Reuters Financial Information, Telebanking, Fax Mail, MoviStar Photo, MoviStar X.28 and MoviStar Activa, the rechargeable prepaid card, which need no contract, nor monthly charges or bills. Telefónica Móviles has also increased the type of contracts it has on offer. In the spring of 1996, the Family Contract was introduced, which was followed by the Provincial MaxiSavings contract and the 3-Number MaxiSavings, which offer savings of up to 35% over the base price. These contracts permit Telefónica Móviles to offer the most extensive range of services and prices currently in the market and, without a doubt, the best attention to our customers' varying needs.



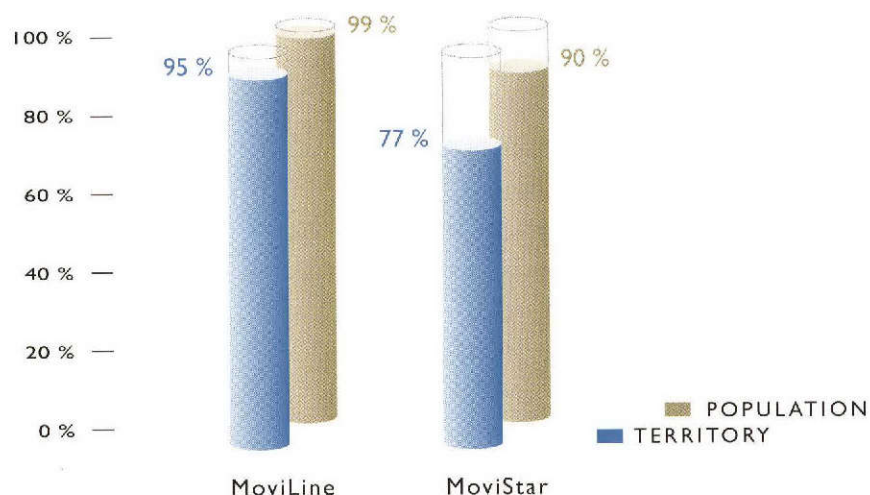
Quality is coverage

The back-up to these services and significant increase in customers is also of vital importance, and this has been reflected in the improvements made in the Telefónica Móviles networks, which last year alone carried 1,574 million calls, as well as providing connection to 220,260 basic telephony customers with cellular access. The number of base stations has doubled, with an average of eight a day having been installed. In



consequence, at the end of 1996, and in terms of vehicle phones, coverage reached 99% of the population and 95% of the country in the MoviLine service. Regarding MoviStar, the growth in coverage has been even more spectacular, as at year-end it had reached 90% of the population and 77% of the country. Lastly, the network has not been any the less, with the MoviStar network having installed an average of two exchanges a month. The overall investment figure resulting from this effort amounted to 141,102 million pesetas in 1996.

MoviLine and MoviStar coverage at December 1996



Guaranteed quality

The Company's constant desire to improve its services and customer care has paid off as, in November of last year, Telefónica Móviles received the AENOR Quality Rating of ISO 9000 in all its processes and services.

The best services on offer

Telefónica's mobile communications group, made up of Telefónica Servicios Móviles, CGS MensaTel and the

**SERVICE QUALITY STANDARDIZATION OF THE TELEFÓNICA DE ESPAÑA
GROUP COMPANIES**

	Rating	Date	Scope of rating
TEMASA (Maritime telecommunications)	ISO 9002 (Lloyd's)	August 1996	Quality of the management of installation and maintenance services of underwater cable communications using cable-laying ships and remote control vehicles.
TELEFÓNICA MÓVILES	ISO 9001	November 1996	Mobile telephony service, designing of mobile telephony and value-added services, designing of construction and operating of networks, marketing and distribution management, customer care and billing.
TELEFÓNICA SISTEMAS INGENIERÍA PRODUCTOS (T.S.I.P.)	ISO 9001	October 1996	Quality of network systems engineering services and telecommunications infrastructures.

SERVICE QUALITY STANDARDIZATION IN TELEFÓNICA DE ESPAÑA

	Rating	Date	Scope of rating
Provincial/territorial divisions	ISO 9001 (Aenor)	1994-1996	Basic telephony services, International communications, Data transmission, Public telephony, Information and Advertising. All the provincial divisions, along with the three territorial divisions (Canary Islands, Extremadura and Galicia) formed to date, have been standardized.
Billing	ISO 9001 (Aenor)	June 1996	All billing procedures.
International Communications	ISO 9001 (Aenor)	October 1996	International telecommunications services both domestically and internationally, and international network global services for operators and high volume customers in Spain and worldwide.



TELEFÓNICA MÓVILES GROUP HIGHLIGHTS (million ptas.)

	1995 (*)	1996
Operating Revenue	120,548	258,906
Pre-tax Income	23,181	21,109
Capital Expenditure	89,401	141,102
Own Workforce	1,096	1,831
Total Assets	201,598	352,744

(*) Includes the activities carried out by Telefónica de España S.A. up to the transfer of licences to Telefónica Servicios Móviles, S.A.

RadioRed group, recorded consolidated revenues for 1996 of over 268,000 million pesetas, assets of more than 352,000 million pesetas and a workforce of over 3,500 people; with an average age of 29, of which 1,831 are directly employed and the remaining number carry out specific activities for Telefónica Móviles through subcontractors.

The combination of liberalized services offered by this Group, confirm our position as the sector's undeniable leader.

MoviLine has found its niche in the combining of mobile services that are ideal for personal use -

sightseeing, mountaineering, adventure sports - and business activities - agriculture, cattle farming, hunting, fisheries, distribution, etc - which offer extensive coverage even in sparsely populated areas. In these areas (both land and sea), which now have almost complete coverage, MoviLine provides high sound quality, coverage and complementary services, compatible with the most advanced analog technology. Despite this, MoviLine continues to pay close attention to the marketing and management effort required to maintain its leading position in the different segments that contribute to the business's global profitability.

MoviStar continues to be the best and most competitive answer for those customers that need communications in highly populated urban areas and major roadways. This service is able to offer a vast range of advanced data and text applications, in accordance with the most demanding quality standards throughout the world and with

international coverage. To be precise, MoviStar customers can use their handset to receive or make calls in 51 countries and with 78 service operators, a number that is constantly increasing.

MensaTel offers its radio-paging service nationally in the form of written, numeric or alphanumeric messages, along with the possibility to receive updated information on such things as the stock market and general information, etc. This company has maintained its leading position in a market that has been highly competitive for several years, and will shortly be boosted by the introduction of new types of contracts.

Regarding radio telephony in closed user groups, the **RadioRed** Group is the only operator that has aimed to gain presence in the eleven licenced areas, having been granted the three remaining ones in 1996, these being the Balearic and Canary Islands and the region of Estremadura. This therefore permits a more global and

personal offer, making RadioRed the market's leader and reference point.

Telefónica Móviles is therefore the only mobile communications operator who provides a global range of services, and, in the case of mobile telephony, offers more services, more diversified pricing, the greatest levels of coverage, the best relationship with customers and distributors, and, most importantly, the highest quality.





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International Businesses

Throughout 1996, Telefónica Internacional strengthened its position of leadership in its existing telecommunications markets, at the same time as seizing the new expansion opportunities that arose in the Brazilian and cable TV market.

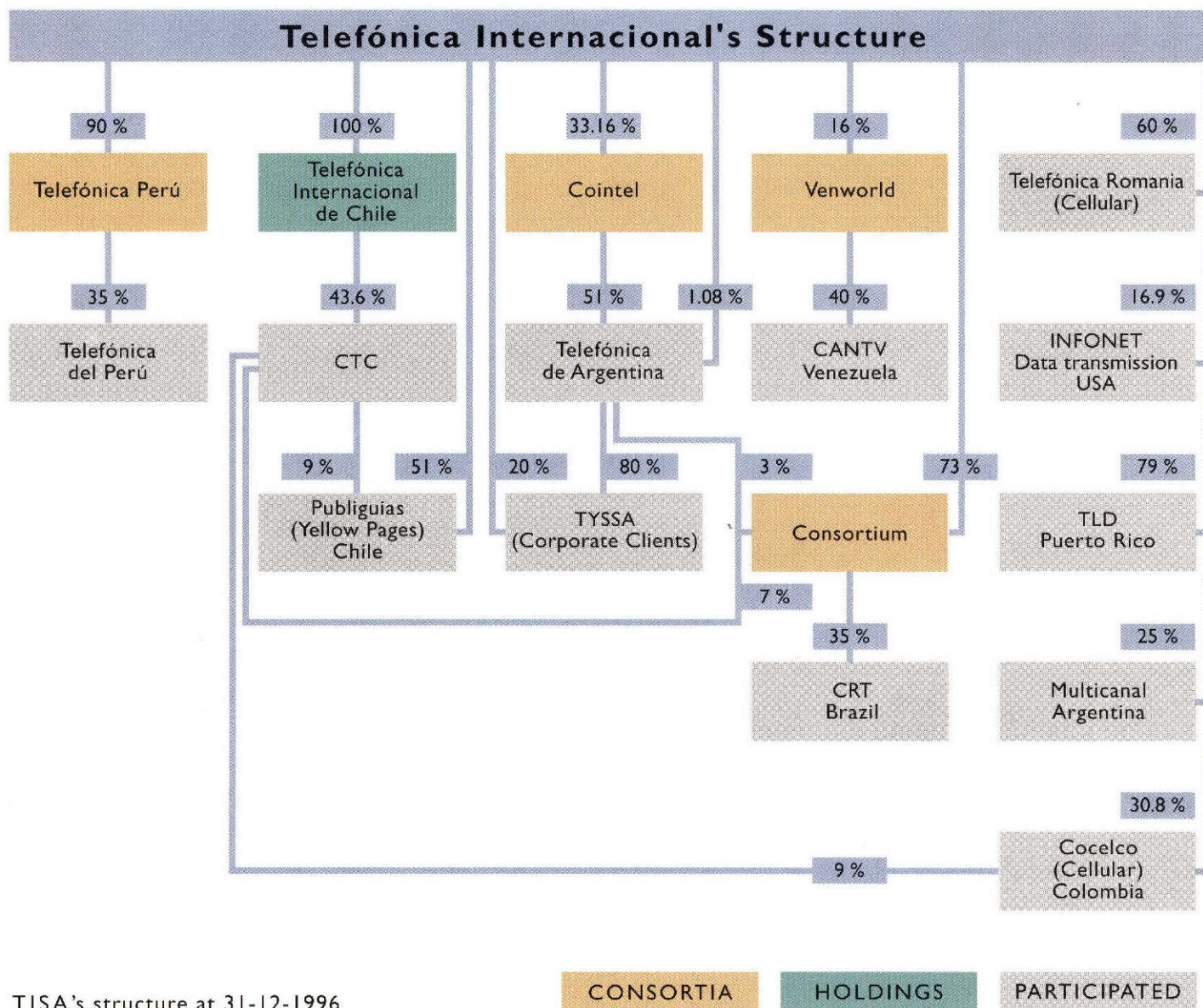
At year-end 1996, approximately 12.4 million customers used the basic telephony, cellular telephony and cable TV provided by one of Telefónica Internacional's participated companies. In the businesses open to competition, such as long distance, cellular telephony or cable TV, these participated operators achieved positions of leadership.

Taking advantage of growth opportunities

On December 17, 1996, the consortium lead by Telefónica Internacional, in which participations are held by the local company RBS (Participações Rede Brasil Sul), Telefónica de Argentina (TASA), and Compañía de Telecomunicaciones de Chile (CTC), were granted 35% of

Companhia Riograndense de Telecomunicações (CRT), following the conclusion of the international bidding process. This operation was of high strategic value for the Telefónica Group, as it completes the Group's positioning in the Mercosur area, gaining access to the principal Latin American telecommunications market in a region that is the gateway to the Argentinian market.

CRT operates in the region of Rio Grande do Sul, which has over 796,043 lines in service, representing 8.3 lines per 100 inhabitants, and more than 177,300 mobile customers. The growth potential is extremely high, reflected by the demand figure of over half a million customers. Besides this, CRT could also be the gateway to other telecommunications businesses, such as long distance and cable TV. The state of Rio Grande do Sul, on the frontier with Argentina, has an income per capita 30% higher than the average for Brazil and a population of almost ten million inhabitants.



TISA's structure at 31-12-1996

The development of businesses and services

At the end of 1996, the Telefónica Internacional participated operators had 10.3 million lines in service. Telefónica de Argentina, with 3.5 million lines, is the leading telecommunications company in Latin America with a ratio of 21 lines per 100 inhabitants. CTC's plant in service grew by 17%, to surpass the figure of 2 million lines, reflecting a penetration level of 14.7 lines per 100 inhabitants. In Telefónica del Perú the number of lines in service rose to more than 1.4 million, a 29% increase over the figure for the previous year. At the same time, the degree of digitalization reached 85% in Peru and 83% in Argentina, while the figure for CTC's network was 100%, as it has been totally digitalized since 1993.

Regarding mobile telephony, these participated companies strengthened their market position registering an overall year-end figure of 985,000 mobile customers.

In March 1996, Telefónica de Argentina launched its domestic cellular service

through its subsidiary TCP, with 39,000 subscribers by the end of the year, complementing Miniphone's 188,000 cellular customers in Buenos Aires. The total number of subscribers to this service therefore amounts to 227,000.

In reference to Chile, the creation of the new company Startel must be mentioned, as this comes as a result of the merger between CTC Móviles and VTR Celular, with CTC holding 55% of the share capital. Startel is the only company to hold a licence to operate throughout the whole of Chile, where it has 175,000 customers to whom it provides cellular telephony, radio-paging, trunking and mobile data transmission, therefore making it Chile's leading operator in mobile services.

Telefónica del Perú Celular tripled its customer portfolio over the twelve-month period, reaching the figure of 131,000.

The cable TV business was also an area of outstanding interest for Telefónica Internacional, as it comfortably passed the figure of one million customers, due



to the strength of the Chilean and Peruvian cable TV companies, combined with the expansion of this service in Argentina.

Chile also witnessed the completion of the merger, in June 1996, of the new company Metrópolis-Intercom, in which CTC holds a 30% participation. This company has become the second most important in the Chilean cable TV market with more than 215,000 customers and 800,000 homes passed.

In 1996, Telefónica del Perú, through its Cable Mágico service, surpassed the figure of 100,000 customers, a five-fold increase over the customer portfolio for the previous year. At the end of 1996, Cable Mágico had passed 400,000



homes, reflecting a 664% increase compared with 1995.

In February 1996, Telefónica Internacional acquired 25% of Argentina's leading cable TV operator Multicanal, which had 831,000 customers at year-end, and 3.5 million homes passed.

The Panamerican Project

In response to the new competitive environment in the international traffic business, and in order to attend to the needs of our global customers in Latin

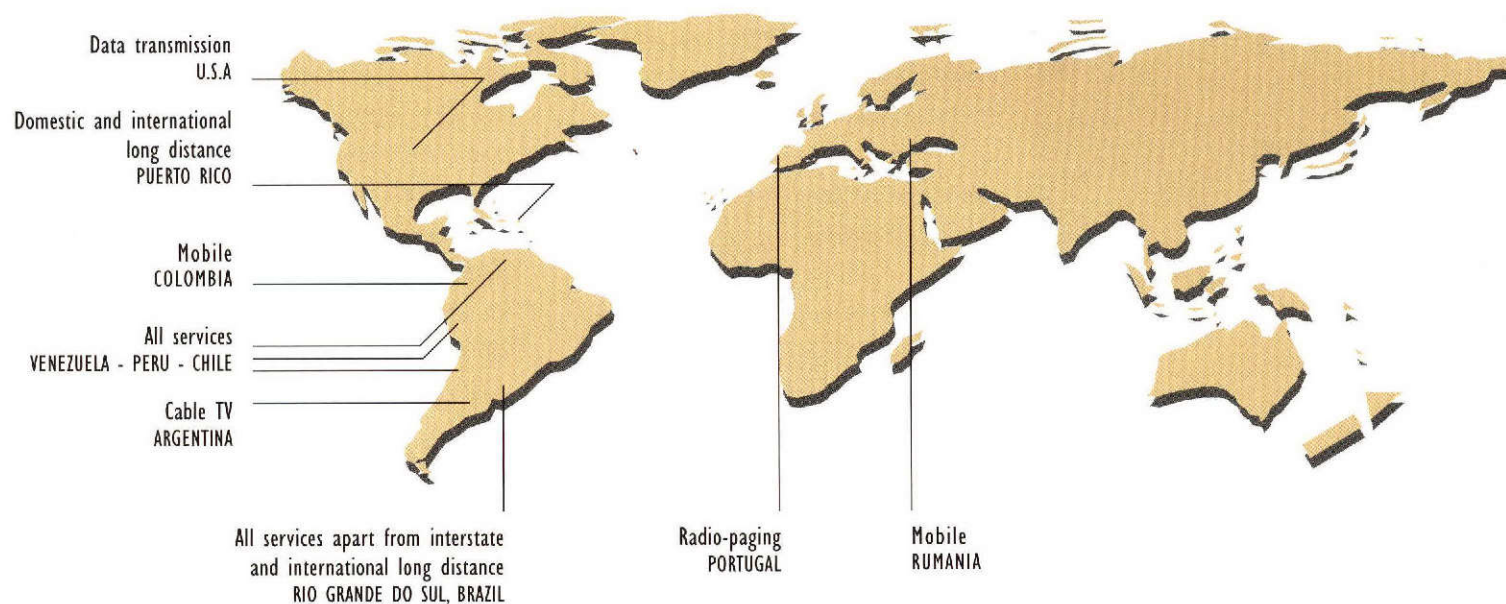
America, Telefónica Internacional continued the development of its Panamerican Project, which is now undergoing pre-commercial launching tests.

The Panamerican Project aims to consolidate the Telefónica Group's position as the leading telecommunications operator in the region of Latin America and to strengthen its multinational position. Once the Panamerican network is launched, Telefónica Internacional will be able to carry international traffic for multinationals and telecommunications

PARTICIPATIONS: COUNTRIES AND BUSINESSES

Argentina	All telecommunications services in the southern region through TASA. Cable TV throughout country provided by Multicanal
Brazil	All telecommunications services in the state of Rio Grande do Sul, except interstate and international long distance
Chile	All telecommunications services through CTC and Publiguías
Colombia	Cellular and value-added services through COCELCO
Peru	All telecommunications services through Telefónica del Perú
Portugal	Radio-paging through CONTACTEL
Puerto Rico	Domestic and international long distance through TLD
Rumania	Cellular through Telefónica Rumanía
Venezuela	All telecommunications services through CANTV
US	Data transmission through Infonet

Telefónica Internacional: Geographical Location



COUNTRY	Population (31 / 12 / 1995) (Mill. in hab.)	Lines in service (31 / 12 / 1996)	Cellular customers (31 / 12 / 1996)	Cable TV customers (31 / 12 / 1996)	Radio-paging customers (31 / 12 / 1996)
Argentina	34.6	3,493,717	227,964	831,243	29,975
Brazil	168.4	796,043	177,300	—	—
Chile	14.2	2,056,353	175,085	216,630	37,657
Colombia	35.2	—	42,253	—	—
Peru	23.5	1,436,022	130,895	101,387	10,963
Portugal	9.9	—	—	—	53,468
Puerto Rico	3.7	—	—	—	—
Rumania	22.8	—	17,660	—	—
Venezuela	21.6	2,494,859	213,655	—	—
TOTAL	—	10,276,994	984,812	1,149,260	132,063



operators (an operator's operator), and will also be able to provide corporate customers with global services.

Increased profitability of businesses

As can be seen, the management of Telefónica Internacional is oriented towards taking maximum advantage of the potential to create shareholder value through the increased profitability of its businesses, in this way ensuring customer satisfaction and its market leadership.

Throughout 1996, the productivity indicators of the participated operators continued to improve significantly, reflected by the 277 lines per employee in Chile's CTC, 228 lines per employee in Telefónica del Perú or the 256 lines per employee in Telefónica de Argentina. These figures represent annual increases of 18% in CTC, 28% in Telefónica de Argentina and 74% in Telefónica del Perú.

Throughout the year, the operators also intensified their cost-cutting

programmes and investment processes. Likewise, special attention was paid to the joint negotiation of procurements and coordinated management systems were also introduced. The coordinated introduction of information systems for plant maintenance and operating structure was also initiated among the participated companies in Argentina, Chile and Peru.

Among the services worth underlining, it must be mentioned that Chile and Peru coordinated the launching of InfoVia, also be launched shortly in Argentina, and which offers international access to the Telefónica Group's customers. The Automatic Roaming project was also launched among all the Group's cellular operators, which will include the interconnection with the North American market, to take place in the near future.

The trust of our investors

Regarding the trust placed in us by our investors, in July 1996, Telefónica del Perú successfully floated its previously

In Japanese, in English or in German,

Telefónica means the same:

Profitability

state-owned shares on the New York Stock Exchange. This floating received support from the international investor community and also recorded a highly successful domestic tranche. Another operation worthy of mention was that of CTC's first issuance of «Yankee Bonds», carried out in July 1996, permitting investors direct access to the North American long-term debt market with the lowest cost ever registered by a Chilean company.

Other investments

The successful floating, in the month of November, of CANTV (Compañía Anónima Nacional de Teléfonos de Venezuela) on the Caracas and New York stock exchanges must also be underlined. At year-end 1996, this company had 2.5 million lines in service and over 210,000 cellular customers. It also registered favourable results for the year.

Telefónica Larga Distancia de Puerto Rico (TLD), recorded a market share of 43% of the country's lines and 15% growth in its outgoing international

traffic, due to its increased number of services to other carrier companies.

Telefónica Romania registered significant 107% growth in its analog mobile telephony customer portfolio, having 17,660 subscribers at the end of 1996. Regarding its GSM system, Telefónica is presently negotiating with the Rumanian government.

Finally, Colombia's cellular operator Cotelco had approximately 42,000 customers at year-end 1996 and continued to hold its position of leadership with a market share of 55% in the licenced area.

The consortium in which AT&T and Unisource participate won the bidding process called by the German railway company Deutsch Bahn, in order to select a strategic partner for the acquisition of a 49.8% stake in DBKom, a Deutsche Bahn subsidiary in the telecommunications sector, Germany's second leading operator and Deutsche Telekom's principal competitor.

ANNUAL ACCOUNTS

*Consolidated
Annual Accounts
and Management Report
for the Telefónica Group
in 1995 - 1996,
along with Auditor's Report*

ARTHUR ANDERSEN

Raimundo Fdez. Villaverde, 65
28003 Madrid

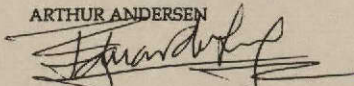
Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25).
In the event of a discrepancy, the Spanish-language version prevails.

AUDITORS' REPORT ON CONSOLIDATED FINANCIAL STATEMENTS

To the Shareholders of
Telefónica de España, S.A.:

1. We have audited the consolidated financial statements of TELEFÓNICA DE ESPAÑA, S.A. and DEPENDENT COMPANIES (TELEFÓNICA GROUP) comprising the balance sheet as of December 31, 1996, and the related statement of income and notes to financial statements for the year then ended. The preparation of these consolidated financial statements is the responsibility of the controlling Company's directors. Our responsibility is to express an opinion on the consolidated financial statements taken as a whole based on our audit work performed in accordance with generally accepted auditing standards, which require examination, by means of selective tests, of the documentation supporting the financial statements and evaluation of their presentation, of the accounting principles applied and of the estimates made.
2. As required by Spanish corporate law, for comparison purposes the directors present, in addition to the 1996 figures for each item in the consolidated balance sheet and statement of income, the figures for 1995. Our opinion refers only to the 1996 consolidated financial statements. The joint auditors' report of Price Waterhouse Auditores, S.A. and Audiberia Auditores, S.L. dated March 1, 1996, on the 1995 consolidated financial statements contained an unqualified opinion.
3. As indicated in Notes 2-c, 7 and 11, the Company restated its assets pursuant to Royal Decree-Law 7/1996, which gave rise to a surplus, net of the single tax, of Ptas. 219,076 million, and this amount is included under the "Restatement Reserves" caption in the consolidated financial statements referred to above.
4. In our opinion, the consolidated financial statements referred to above present, in all material respects, a true and fair view of the net worth and financial position of Telefónica de España, S.A. and Dependent Companies as of December 31, 1996, and of the results of their operations and of the funds obtained and applied by them in the year then ended, and contain the required information, sufficient for their proper interpretation and comprehension, in conformity with generally accepted accounting principles and standards which were applied on a basis consistent with that of the preceding year, except for the change in the method of recording investment tax credits described in Note 2-c, with which we concur.
5. The accompanying consolidated management report for 1996 contains the explanations which the directors of Telefónica de España, S.A. consider appropriate about the Telefónica Group's situation, the evolution of its business and other matters, but is not an integral part of the consolidated financial statements. We have checked that the accounting information in the management report is consistent with that contained in the consolidated financial statements for 1996. Our work as auditors was confined to checking the management report with the aforementioned scope, and did not include a review of any information other than that drawn from the Companies' accounting records.

ARTHUR ANDERSEN



Eduardo Sanz Hernández

February 27, 1997

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Inscrita en el Registro Oficial de Auditores de
Cuentas (ROAC)
Inscrita en el Registro de Economistas Auditores (REA)

Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

TELEFÓNICA DE ESPAÑA, S.A. AND DEPENDENT COMPANIES
CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 1996 AND 1995
(Currency - Millions of Spanish Pesetas)

ASSETS	1996	1995
A Due from stockholders for uncalled capital	—	174
B) Fixed and other noncurrent assets		
I. Start-up expenses	577	714
II. Intangible assets (Note 6)-	337,825	317,239
Research and development expenses	104,047	79,628
Rights on leased assets	15,425	10,711
Other intangible assets	313,336	295,201
Amortization	(94,983)	(68,301)
III. Property and equipment (Note 7)-	3,973,870	3,597,426
Land and structures	656,279	570,203
Technical installations and machinery	130,487	135,885
Telephone installations	5,598,023	5,285,469
Furniture	237,582	231,059
Construction in progress	327,861	291,302
Advances on property and equipment	23,640	10,574
Installation materials	50,804	14,014
Depreciation	(3,050,806)	(2,941,080)
IV. Long-term financial investments (Note 8)-	272,871	148,977
Holdings in associated companies	116,317	85,339
Other holdings	128,540	45,875
Other loans	31,374	20,429
Other long-term loans, deposits and guarantees	1,369	1,262
Provisions	(4,729)	(3,928)
	4,585,143	4,064,356
C) Goodwill in consolidation (Note 5)	49,798	47,687
D) Deferred charges (Note 9)	130,294	141,310
E) Long-term prepaid taxes (Note 18)	70,007	50,336
F) Current assets		
I. Due from stockholders for capital calls	—	4
II. Inventories	33,834	29,036
III. Accounts receivable-	505,653	398,837
Customer receivables (Note 10)	405,722	352,750
Receivable from associated companies	4,453	6,599
Sundry accounts receivable	77,811	42,580
Employee receivables	14,417	15,077
Tax receivables (Note 18)	53,839	25,180
Allowance for bad debts	(43,196)	(36,485)
Allowance for sundry accounts receivable	(7,393)	(6,864)
IV. Short-term financial investments-	35,843	68,247
Loans to associated companies	61	530
Short-term investment securities	8,779	7,262
Other loans	27,496	60,456
Provisions	(493)	(1)
V. Cash	12,647	11,933
VI. Accrual accounts	12,396	6,338
	600,373	514,395

Total assets (a+b+c+d+e+f)

5,435,615

4,818,258

The accompanying Notes I to 25 and Exhibits I and II are an integral part of these consolidated balance sheets.

Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

TELEFÓNICA DE ESPAÑA, S.A. AND DEPENDENT COMPANIES
CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 1996 AND 1995
(Currency - Millions of Spanish Pesetas)

STOCKHOLDERS' INVESTMENT AND LIABILITIES	1996	1995
A) Stockholders' investment (Note 11)		
I. Subscribed capital stock	469,735	469,735
II. Paid-in surplus	43,067	43,067
III. Restatement reserves	868,392	649,316
IV. Reserves-	355,053	279,177
Legal reserve	86,071	75,453
Other reserves	157,061	130,149
Consolidation reserve	75,935	51,597
Translation differences in consolidation	35,986	21,978
V. Prior years' income	112	147
VI. Income for the year-	160,282	133,214
Income of the parent company and subsidiaries	211,149	175,599
Income of associated companies	7,811	8,754
Income attributed to minority interests	(58,678)	(51,139)
VII. Interim dividend paid during the year	(32,881)	(28,184)
	1,863,760	1,546,472
B) Minority interests (Note 12)	374,693	313,753
C) Deferred revenues (Note 13)	87,486	91,258
D) Provisions for contingencies and expenses (Note 14)	336,615	287,996
E) Long-term deferred taxes (Note 18)	83,743	71,013
F) Long-term debt		
I. Debentures, bonds and other negotiable instruments (Note 15)-	654,378	643,938
Nonconvertible debentures and bonds	637,919	614,329
Convertible debentures and bonds	14,645	13,553
Other marketable debt securities	1,814	16,056
II. Payable to credit entities (Note 16)	843,349	901,885
III. Payable to associated companies	271	-
IV. Other accounts payable-	103,147	116,947
Other accounts payable	103,147	116,434
Notes payable	-	513
V. Uncalled capital payments payable-	2,751	2,738
Group companies	-	10
Associated companies	243	184
Other companies	2,508	2,544
	1,603,896	1,665,508
G) Current liabilities		
I. Debentures, bonds and other negotiable instruments (Note 15)-	147,427	108,154
Debentures	63,580	64,993
Other negotiable instruments	68,854	29,170
Interest on debentures and other securities	14,993	13,991
II. Payable to credit entities (Note 16)-	244,617	168,246
Loans and other accounts payable	234,136	151,105
Interest payable	10,481	17,141
III. Payable to associated companies	28,458	19,392
IV. Trade accounts payable-	374,580	257,112
Advances received on orders	933	1,938
Payables for purchases and services	370,564	246,430
Notes payable	3,083	8,744
V. Other nontrade payables-	264,204	260,771
Accrued taxes payable (Note 18)	104,167	100,545
Other nontrade payables	160,037	160,226
VI. Accrual accounts	26,136	28,583
	1,085,422	842,258
Total stockholders' investment and liabilities (A+B+C+D+E+F+G)	5,435,615	4,818,258

Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

TELEFÓNICA DE ESPAÑA, S.A. AND DEPENDENT COMPANIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995
(Currency - Millions of Spanish Pesetas)

DEBIT	1996	1995
A) Expenses		
Reduction in inventories	3,253	1,286
Supplies-		
Purchases from associated companies and other	136,314	88,434
Work performed by other companies	92,290	39,609
	228,604	128,043
Personnel expenses (Note 20)	554,682	543,547
Period depreciation and amortization-		
Property and equipment	499,924	477,616
Intangible assets	26,087	23,700
Deferred charges	218	164
	526,229	501,480
Variation in operating provisions-		
Variation in provision for inventories	266	644
Variation in allowance for bad debts	17,161	17,383
Variation in other operating provisions	9,142	7,132
	26,569	25,159
Other operating expenses-		
Outside services	207,638	153,431
Taxes other than income tax	35,106	27,667
Other operating expenses	19,307	9,728
	262,051	190,826
I. Operating income	575,965	509,882
Interest on payables to associated companies	60	82
Other interest on accounts payable (Note 20)	181,645	200,448
Amortization of deferred interest expenses	3,603	3,317
Variation in financial investment provisions	665	621
Exchange losses	20,452	19,188
II. Financial income	—	—
Share in losses of companies carried by the equity method	8,114	1,787
Amortization of goodwill in consolidation (Note 5)	16,786	6,985
III. Income from ordinary activities	390,399	319,482
Variation in control portfolio provisions	246	(9)
Losses on fixed assets	45,034	47,871
Losses on disposals of consolidated companies	2,609	102
Extraordinary expenses and losses (Note 20)	98,570	77,681
IV. Extraordinary income	—	—
V. Income before taxes	275,881	223,711
Corporate income tax (Note 18)	25,804	16,594
Foreign taxes (Note 18)	31,117	22,764
VI. Consolidated income for the year	218,960	184,353
Income attributed to minority interests (Note 12)	59,287	51,235
VII. Income for the year	160,282	133,214

The accompanying Notes I to 25 and Exhibits I and II are an integral part of these consolidated statements of income.

Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

TELEFÓNICA DE ESPAÑA, S.A. AND DEPENDENT COMPANIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1996 AND 1995
(Currency - Millions of Spanish Pesetas)

CREDIT	1996	1995
B) Revenues		
Net sales and services (Note 20)	2,006,058	1,740,557
Increase in inventories	6,218	4,716
Capitalized expenses of in-house work on fixed assets	127,319	121,548
Other operating revenues-		
Sundry and other current operating revenues	32,653	27,817
Subsidies	1,643	1,188
Overprovision for contingencies and expenses	3,462	4,397
	37,758	33,402
 I. Operating loss	—	—
Income from shareholdings-		
Associated companies	25	18
Other companies	2,350	1,803
	2,375	1,821
Revenues from other securities and loans-		
Associated companies	889	378
Other companies	15,892	16,603
	16,781	16,981
Exchange gains	10,678	12,685
II. Financial loss	176,591	192,169
Equity in income of companies carried by the equity method	15,925	10,541
 III. Loss on ordinary activities	—	—
Gains on fixed asset disposals	2,150	5,187
Gains on disposals of holdings in consolidated companies	10,335	7,278
Capital subsidies	10,315	7,983
Extraordinary revenues (Note 20)	9,141	9,426
IV. Extraordinary loss	114,518	95,771
V. Loss before taxes	—	—
 VI. Consolidated loss for the year	—	—
Loss attributed to minority interests (Note 12)	609	96
Loss for the year	—	—

Translation of a report and consolidated financial statements originally issued in Spanish and prepared in accordance with generally accepted accounting principles in Spain (see Note 25). In the event of a discrepancy, the Spanish-language version prevails.

TELEFÓNICA DE ESPAÑA, S.A. " **AND DEPENDENT COMPANIES**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR 1996 AND 1995

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I. GROUP DESCRIPTION AND STATE CONTRACT

Group companies-

Telefónica de España, S.A. ("Telefónica") and its dependent companies make up an integrated group of companies ("the Telefónica Group") operating in the telecommunications industry.

Exhibit I to these notes to consolidated financial statements lists the subsidiaries, associated companies and investees in which Telefónica has direct or indirect holdings and their lines of business, net worth and results. Exhibit II describes the main operating data on the subsidiaries that are telecommunications operators.

Parent Company-

Telefónica de España, S.A. is a company which was incorporated pursuant to the Spanish Commercial Code for an indefinite period of time on April 19, 1924. Its registered office is at c/ Gran Vía, 28 - 28013 Madrid.

a) Corporate purpose-

The Company's corporate purpose, per Article 4 of its bylaws, is as follows:

1. The provision and operation of all manner of public and private telecommunications services, and for this purpose, the design, installation, upkeep, repair, improvement, acquisition, disposal, interconnection, management, administration and any other activity not included in the foregoing list, in connection with all manner of existing or future telecommunications networks, lines, satellites, equipment, and technical systems and infrastructures, including the land and buildings where they are located.
2. The supply and operation of all manner of ancillary or supplementary telecommunications services or the services derived therefrom.
3. The research and development, promotion and application of all manner of components, equipment and systems, directly or indirectly used for telecommunications.
4. Manufacturing, production and, in general, all other industrial activities relating to telecommunications.
5. Acquisition, disposal and, in general, all other commercial activities relating to telecommunications.

All the activities that constitute the corporate purpose described in the preceding paragraphs may be performed either in Spain or abroad and may be carried on either wholly or partially by the Company, or through shareholdings or participations in other companies or legal entities with an identical or similar corporate purpose.

b) Framework for the provision of services-

Telefónica is the State licensee for rendering certain public telecommunications services pursuant to the License Contract entered into with the Spanish Administration on December 26, 1991. In accordance with the provisions of such Contract, Telefónica may also carry on any financial, industrial or service-related activities deemed necessary for its interests, provided they do not cause any

deterioration in the normal operation of the ultimate carrier services forming the subject matter of the aforementioned Contract or involve the assumption of obligations contrary to the provisions of the Spanish National Telecommunications Plan.

As the licensee of said services, Telefónica undertakes, in general, to provide them observing such general interest criteria of a noneconomic nature as may be determined in the regulations on telecommunications services, particularly taking into account the maintenance of security in the operation of networks and services, the integrity and the interoperativeness thereof, data protection and the confidentiality of communications.

The deregulation of the telecommunications industry in Spain has paved the way for the emergence of restricted or full competition systems for part of the services forming the subject matter of the State License Contract entered into with the State on December 26, 1991. In particular, Royal Decree-Law 6/1996 granted Retevisión an enabling instrument to provide urban, national and international basic telephony services as well as supporting carrier services in connection with basic telephony services, for which purpose it has incorporated a company which will be charged with rendering the service under an indirect management arrangement.

The Cable Telecommunications Law empowers Telefónica to supply this service on an integrated basis with the basic telephony service in all areas where it is requested, after 24 months have elapsed from the award of the cable operator tender in each area, unless the tender is declared void, in which case commencement of the provision of services will be immediate. In response to a proposal by the Spanish National Telecommunications Market Commission, the Government may reduce this period depending on market conditions.

c) *Rate system-*

The License Contract established a system of regulated rates and prices aimed at guaranteeing, except with respect to the modifications expressly provided by the Contract deriving from the change from a monopoly to a competitive system, the overall financial balance of the concession, while safeguarding the principle of universal service. To that end, within the framework of cost discipline and efficient management of the Company's production resources, the rate system must ensure that Telefónica is able to cover its operating expenses, appropriations to reserves and return on capital, while striving to align the rate structure and the cost structure.

Recently, Royal Decree-Law 6/1996, deregulating the telecommunications industry, determined that the Government, at the proposal of the Ministry of Development, shall establish the cases in which fixed maximum and minimum rates and simple price adjustment rates will apply, and the methods to be used to set them, based on the degree of market demand for the various services.

d) *Tax regime-*

In accordance with Telefónica Taxation Law 15/1987 and Royal Decree 1334/1988, partially enacting the former, since January 1, 1988, Telefónica has been subject to general tax legislation for central State taxes. As regards local taxes, Telefónica is subject to property tax, the other local taxes being replaced by an annual cash compensation payment equal to 2% of gross billings.

2. BASIS OF PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

a) *True and fair view-*

The accompanying consolidated financial statements of the Telefónica Group were prepared from the accounting records of Telefónica de España, S.A., and from those of each of the dependent companies which, together with Telefónica, compose the Group, modified by the effects of the restatement carried out pursuant to Royal Decree-Law 7/1996. The respective individual financial statements were prepared by each company's directors in accordance with the accounting principles and standards provided by the Spanish Corporations Law as enacted by Legislative Royal Decree 1564/1989, implemented by the Spanish National Chart of Accounts, as enacted by Royal Decree 1643/1990, and by the regulations for the preparation of consolidated financial statements, as approved by Royal Decree 1815/1991 and the applicable specific regulations. Accordingly, these consolidated financial statements give a true and fair view of the net worth, financial position and income for each year.

The 1996 consolidated financial statements and the 1996 individual financial statements of Telefónica de España, S.A. and of each Group company will be submitted for approval by the respective Stockholders' Meetings, and it is considered that they will be approved without any changes. The 1995 individual financial statements of each of the consolidated Group companies were approved by the respective Stockholders' Meetings. The 1995 consolidated financial statements of the Telefónica Group were approved by the Stockholders' Meeting on March 29, 1996.

Accounts payable are recorded at their repayment value, except for zero-coupon debentures and bonds, which are recorded in the balance sheet at their issue value plus the accrued interest (see Note 15).

b) *Consolidation principles-*

The companies over which effective control is exercised by virtue of ownership of a majority of the voting rights in their representation and decision-making bodies were consolidated by the global integration method; the multigroup companies which are managed jointly

with third parties were consolidated by the proportional integration method; and those in which there is significant influence but not ownership of a majority of the voting rights or joint management with third parties are carried by the equity method. Significant influence is deemed to exist if the ownership interest exceeds 20% in the case of unlisted companies or 3% in the case of listed companies.

All material accounts and transactions between the consolidated companies were eliminated in consolidation. In the case of investees whose accounting and valuation methods differed from those of Telefónica, adjustments were made in consolidation so as to present the consolidated financial statements on a uniform basis. The margins included in the invoices issued by subsidiaries to Telefónica for installations are eliminated at the time of the transaction, and this income is recognized as the related installations are depreciated.

The equity of the minority interests in the net worth and results of the consolidated dependent companies consolidated by the global integration method is recorded under the "Minority Interests" and "Income Attributed to Minority Interests" captions (see Note 12).

In accordance with standard practice in Spain, the accompanying consolidated financial statements do not include the tax effect, if any, of transferring the reserves of the consolidated subsidiaries to the parent company's accounts, since it is considered that such reserves will be used to finance their operations and that those that may be distributed will not give rise to a material additional tax cost.

c) Comparative information-

- The figures for property and equipment and equity in the consolidated balance sheet as of December 31, 1996, are not comparable with the figures for 1995 because they include the restatement of assets pursuant to Royal Decree-Law 7/1996 (see Notes 7 and 11).
- In 1996, the Group changed its method of recording the expense for corporate income tax as a result of the changes in tax legislation on investment tax credits. From 1996 it accrues the tax credits earned and reported in its tax return over the average useful life of the assets giving rise to the tax credits, as provided by the applicable accounting regulations.
As a result of this change, the corporate income tax expense for 1996 increased by Ptas. 17,027 million. This amount will be recoverable in future years as the above-mentioned assets are depreciated. This change does not affect the amount of tax payable.
- The changes in the consolidated Group in 1996 and 1995 were as follows:

1996-

1. Telefónica acquired 25% of Unisource N.V. by exchanging all the shares of Telefónica Transmisión de Datos, S.A. and Telefónica V.S.A.T., S.A. Unisource N.V. is carried by the equity method (see Notes 8D.1 and 8D.2). Telefónica's acquisition of the holding in Unisource N.V. has received preliminary approval by the European Union, but definitive approval has not yet been granted.
2. On December 17, 1996, the consortium led by Telefónica Internacional de España, S.A. ("Telefónica Internacional") submitted the successful bid in an international call for tender for the acquisition of 35% of the voting stock of Companhia Riograndense de Telecomunicações (CRT), equivalent to 13.45% of the latter's stock with dividend rights, for 681 million reais. The portion of the holding acquired and attributable to the Telefónica Group represents 7.87% of the company's total capital stock. The companies participating in the consortium with Telefónica Internacional are R.B.S. Participações, S.A., Compañía de Telecomunicaciones de Chile, S.A. Telefónica de Argentina, S.A. and Citicorp.
The acquisition of the aforementioned shares was formally executed on December 30, 1996. The holding in this company was recorded at cost as of December 31, 1996, but it will be carried by the equity method in 1997.
3. Telefónica sold its entire holding in Sistemas e Instalaciones de Telecomunicación, S.A. (SINTEL) and, accordingly, Sintelperú, S.A. and Sintelar, S.A. (each 25% owned by Telefónica Internacional and 38% and 50% owned, respectively, by Sintel, S.A.), are now carried by the equity method (see Note 8D.3).
4. Telefónica continued to incorporate companies to operate the cable television system and to provide added value services at local level. The companies incorporated in 1996 were as follows:
 - Sociedad General de Cablevisión Sevilla, S.A.
 - Sociedad General de Cablevisió Balears, S.A.
 - Sociedad General de Cablevisión Cádiz, S.A.
 - Sociedad General de Cablevisión Navarra, S.A.
 - Sociedad General de Cablevisión Murcia, S.A.

- Sociedad General de Cablevisión Lleida, S.A.
- Sociedad General de Cablevisión Bizkaia, S.A.
- Sociedad General de Cablevisión Rioja, S.A.
- Sociedad General de Cablevisión Asturias, S.A.
- Sociedad General de Cablevisión Burgos, S.A.
- Sociedad General de Cablevisión León, S.A.
- Sociedad General de Cablevisión Valladolid, S.A.
- Sociedad General de Cablevisión Valencia, S.A.
- Sociedad General de Cablevisión Alicante, S.A.
- Sociedad General de Cablevisión Málaga, S.A.
- Sociedad General de Cablevisión Granada, S.A.

all of which were consolidated by the global integration method.

5. Telefónica Internacional acquired 25% of the Argentine companies Multicanal, S.A. and PEM, S.A., both of which are carried by the equity method.
6. T.S. Telefónica Sistemas, S.A. participated in the incorporation of Negocios Cibernéticos, S.A. by acquiring 50% of the capital stock of the new company, which was consolidated by the global integration method.

It also participated in the incorporation of Madrid 112, in which it has a 49% ownership interest. This company is consolidated by the equity method.

T.S. Telefónica Sistemas, S.A. acquired 50% of Gestión y Operación de Redes, S.A. (GESTIRED) from its subsidiary Telefónica Gestión de Sistemas, S.A. (T.G.S.). It subsequently acquired the remaining 49% of this company, bringing its total shareholding to 100%. GESTIRED continues to be consolidated by the global integration method.

T.S. Telefónica Sistemas, S.A. also acquired 50% of the capital stock of Servicios y Contenidos por la Red, S.A., bringing its current ownership interest to 100%. This latter company continues to be consolidated by the global integration method.

Maptel, S.A. and T.S.C. Telefónica Seguridad y Comunicaciones, S.A. changed their corporate names to Telefónica Sistemas de Información Geográfica, S.A. (T.S.I.G.) and Telefónica Sistemas de Ingeniería de Productos, Seguridad, S.A. (T.S.I.P.S.), respectively.

7. T.S. Telefónica Sistemas, S.A. sold all its holding (55.64%) in T.P. Servicios Integrales de Protección Civil, S.A. (TEPESA) (see Note 8D.3).

It also sold all its holding (24.99%) in Telecom Vallés, S.A. (see Note 8D.3).

8. Telefónica Publicidad e Información, S.A. (TPI) participated in the incorporation of REM Infográfica, S.A., acquiring 60% of the capital stock of the new company, which is consolidated by the global integration method.

TPI also acquired 51% of the capital stock of T.M.P. Worldwide España, S.A., which is consolidated by the global integration method.

On December 20, 1996, TPI dissolved and liquidated Promotora de Mercados Telemáticos, S.A. and Central de Compras de Papel, S.A., both of which were wholly-owned subsidiaries.

9. Estrategias Telefónicas, S.A. (ESTRATTEL) incorporated Tempotel, Empresa de Trabajo Temporal, S.A. and subscribed all its capital stock. This company is consolidated by the global integration method.
10. Telefónica Multimedia, S.A. sold all its holdings in Cable del Guadalquivir, S.A. (20%) and Grupo Gallego de Empresas para el Cable, S.A. (10%) (see Note 8D.3).
11. Radiored I, S.A. acquired a 9% holding in the capital stock of Radiored Zaragoza, S.A., bringing its shareholding in this company to 100%. This company continues to be consolidated by the global integration method.

During the year Radiored I, S.A. incorporated the following companies: Radiored Extremadura, S.A., Radiored Canarias, S.A. and Radiored Baleares, S.A. These three companies, which were consolidated by the global integration method, all are wholly owned by Radiored, S.A.
12. In November 1996 Telecartera, S.A. exchanged with Sogecable its 50% holding in Sociedad General de Cablevisión, S.A. for Sogecable's holdings in local operators (10% holdings, except for the local operators in the Canary Islands, Madrid and Barcelona). Telecartera also acquired from Cablevisión its holdings in local operators (39% holdings except in the case of the companies in Madrid and Barcelona -49%- and Burgos -24%) for Ptas. 635 million.
13. Servicios de Teledistribución, S.A. (ST-Hilo) sold its 33% holding in Sociedad Anónima de Productos Electrónicos y de Comunicación (S.A.P.E.C.) (see Note 8D.3).

14. Hispasat, S.A. increased capital in 1996. Telefónica, however, did not subscribe all the shares corresponding to it, thereby reducing its holding in this company by 2.26% to 22.74%. This company continues to be consolidated by the equity method.

Telefónica sold 30 shares of Telecartera, S.A., thereby reducing its holding in this company to 75%. This company continues to be consolidated by the global integration method (see Note 8D.3).

It also sold 48,000 shares of Amper, S.A., reducing its holding to 15%. This company continues to be carried by the equity method (see Note 8D.3).

Telefónica sold all its holdings in European Silicon Structures, S.A. (ES-2) (0.38%) and Financial Network Association (F.N.A.) (8.33%) (see Note 8D.3).

15. STARTEL, S.A., a CTC Group company, was incorporated in 1996 as a result of agreements entered into on March 11, 1996, between CTC-Celular and VTR-Comunicaciones Móviles, S.A. to jointly operate in the cellular telephony business. CTC's and VTR's holdings of 55% and 45%, respectively, in the new company, were obtained through the contribution of 75% and 25% of STARTEL, S.A.'s assets, respectively, and through the subsequent sale of 20% of the company's capital stock for US\$ 67 million. As a result of this sale, the Telefónica Internacional Group recorded extraordinary income of Ptas. 2,444 million, net of taxes and the equity of minority interests, the gross amount of which (Ptas. 6,597 million) is recorded under the "Gains on Disposals of Holdings in Consolidated Companies" caption in the accompanying 1996 statement of income.

1995-

1. In 1995 Sistemas e Instalaciones de Telecomunicación, S.A. (SINTEL) acquired an additional 2.1% holding in the capital stock of Informática y Comunicaciones, S.A. (INCOSA) and 2% of the capital stock of Construcciones de las Conducciones del Sur, S.A. (COTRONIC). These acquisitions gave the Telefónica Group a majority holding in the capital stock of the two companies and, accordingly, in 1995 they were consolidated by the global integration method for the first time. SINTEL sold its holdings of 44% in Inalca, S.A. and of 42.12% in Sistemas Avanzados de Control, S.A. and, accordingly, these companies were deconsolidated. SINTEL also participated in the formation of Sintel-Abengoa Multimedia, A.I.E. and acquired 50% of its capital stock. This company was consolidated by the proportional integration method.
2. Telefónica started to incorporate companies to operate the cable television system and to provide added value services at local level. The companies incorporated in 1995 were as follows: Sociedad General de Cablevisión Madrid, S.A.; Societat General de Cablevisió Barcelona, S.A.; Sociedad General de Cablevisión Cantabria, S.A.; and Sociedad General de Cablevisión Canarias, S.A. These companies were consolidated by the global integration method.
3. Telefónica VSAT, S.A. was incorporated to provide satellite telecommunications services. This company was consolidated by the global integration method.
4. Telecartera, S.A. acquired 16.67% of Sociedad General de Cablevisión, S.A., bringing its holding up to 50%. Accordingly, this company was consolidated by the proportional integration method in 1995.
5. Telefónica Sistemas, S.A. participated in the incorporation of Telefónica Sistemas Portugal, S.A. (consolidated by the global integration method), Hispaseservices, S.A. and Portel Servicios Telemáticos, S.A. (carried by the equity method).

d) Unless otherwise indicated, the figures in the consolidated financial statements are expressed millions of pesetas.

3. DISTRIBUTION OF THE INCOME OF THE CONTROLLING COMPANY

The proposed distribution of Telefónica de España, S.A.'s 1996 income that the Board of Directors will submit for approval by the Stockholders' Meeting is as follows:

	Millions of Pesetas
Basis of distribution:	
1996 net income	120,414
Prior year's retained earnings	112
Total amount to be distributed	120,526
Distribution to:	
Interim dividend of 7%, declared on January 20, 1997	32,881
Supplementary dividend of 10.8%, pending approval	50,732
Dividends	83,613
Legal reserve	7,876
Voluntary reserves	28,900
Retained earnings	137
Total amount distributed	120,526

Interim dividend-

In accordance with Article 216 of the revised Corporations Law, on December 18, 1996, the Board of Directors, based on the economic and financial information submitted to it, approved the distribution of an interim dividend of Ptas. 35 gross per share out of 1996 income.

The accounting statement prepared in accordance with legal requirements (Article 216 of the revised Corporations Law), evidencing the existence of sufficient liquidity for the distribution of the interim dividend for 1996, was as follows:

Accounting Statement Supporting Liquidity for Distribution of Interim Dividend	
	Millions of Pesetas
Income from January 1 to November 30, 1996	113,610
1995 retained earnings	112
Prior years' losses	—
Mandatory appropriation to reserves	(7,876)
Distributable income	105,846
Proposed interim dividend	32,881
Financial Position (forecast at 11/30/96)	
Distributable funds-	
Cash	5,074
Unrestricted loans	295,069
Proposed interim dividend	(32,881)
Difference	267,262

The proposed distribution of the income of Telefónica de España, S.A. that will be submitted for approval by the next Stockholders' Meeting will be accompanied by a request for the distribution of a supplementary dividend for 1996 of Ptas. 54 gross per share.

4. VALUATION STANDARDS

The main valuation methods applied in preparing the consolidated financial statements for 1996 and 1995 were as follows:

a) Goodwill in consolidation-

The accompanying 1996 and 1995 consolidated balance sheets include goodwill, net of amortization, arising from the positive difference in consolidation between the amounts paid to acquire the shares of the dependent companies consolidated or carried by the equity method and their underlying book values at the acquisition date.

Goodwill is amortized on a straight-line basis over ten years, since this is the period over which it is estimated that the goodwill will contribute to the obtaining of income at the Group.

b) Translation methods (year-end exchange rate method)-

The financial statements of the Group companies abroad were translated to pesetas at the exchange rates ruling at year-end, except for:

1. Capital stock and reserves, which were translated at historical exchange rates.
2. Income statements, which were translated at the average exchange rate for the year.
3. The companies using accounting methods that include inflation adjustments apply the accounting standards in force in their respective countries, which consist of valuing monetary assets and liabilities at face value and adjusting the historical cost of nonmonetary assets by the inflation from the date of inclusion of the asset in the company's balance sheet to year-end. The effect of the year's inflation on the monetary assets and liabilities is included in the statement of income for the year. In 1995 the Argentinean legislation abolished the application of the inflation adjustment in the financial statements of companies located in Argentina.

The exchange difference arising from application of these procedures is included under the "Stockholders' Investment - Translation Differences in Consolidation" caption in the accompanying consolidated balance sheets, net of the portion of said difference relating to minority interests, which is recorded under the "Minority Interests" caption on the liability side of the accompanying consolidated balance sheets.

c) Start-up expenses-

Start-up expenses, which comprise incorporation and capital increase expenses, are recorded at cost and are amortized on a straight-line basis over five years.

d) Intangible assets-

This caption in the accompanying consolidated balance sheets includes the following items:

Research and development expenses-

These relate to the costs incurred in developing new products to be marketed or used for the Group's own network, which are amortized by the straight-line method over five years. Costs incurred in projects which are not viable for the future are expensed currently.

Rights on leased assets-

The rights under financial lease contracts are recorded at the cost of the related assets, and the total debt for lease payments plus the amount of the purchase option are recorded as a liability. The difference between the two amounts, which represents the interest expenses on the transaction, is recorded as a deferred expense and is allocated to income each year by the interest method. The existing contracts, which relate to computer hardware, are amortized by the straight-line method over five years, which coincides with the years of useful life of the hardware.

Software licenses-

Software licenses are recorded at cost and are amortized by the straight-line method over three years.

Other intangible assets-

This caption includes other intangible assets; the main items relate to the costs incurred in acquiring capacity and rights of way in other operators' cables. These rights are amortized on a straight-line basis over 25 years.

The administrative concessions related to a concession granted by the Peruvian Government to CPT and Entel Perú at the time of acquisition of these two companies by Telefónica Internacional. It is recorded at the difference between the acquisition cost and the proportional part of the equity of the companies acquired at that date, adjusted by estimates of certain costs to be incurred in the merger and restructuring of these two companies' operations. This intangible asset will be amortized over 20 years (the concession period) and on the basis of the number of lines installed, since this is the variable which determines the obtaining of revenues allocable to the concession.

e) Property and equipment-

Property and equipment is carried at cost restated pursuant to the applicable enabling legislation from 1946 to 1996, including Royal Decree-Law 7/1996 (see Note 7). If the regulations applicable in each country so require, the property and equipment is valued at cost or appraisal value adjusted by inflation.

Cost includes external costs plus internal costs comprising materials used, direct labor used in installation work and the allocable portion of the indirect costs required for the related investment. The latter two items are recorded as revenue under the "Capitalized Expenses of In-House Work on Fixed Assets" caption.

The costs of expansion, modernization or improvements leading to increased productivity, capacity or efficiency or to a lengthening of the useful lives of the assets are capitalized.

Upkeep and maintenance expenses are expensed currently.

The companies depreciate their property and equipment by the straight-line method at annual rates based on the years of estimated useful life, calculated in accordance with technical studies conducted by Telefónica and the Group companies, reviewed periodically based on technological advances and the rate of dismantling, as follows:

	Years of Estimated Useful Life
Buildings	30 - 50
Power equipment	10 - 20
Switching equipment	7 - 17
Transmission equipment	5 - 14
Local and domestic long-distance networks	7 - 25
Subscriber equipment and other installations	4 - 8
Furniture, office equipment and other	4 - 15

The increases in value resulting from the restatements are depreciated over the years of residual useful life of the restated assets.

f) Long- and short-term financial investments-

Long- and short-term financial investments, except for companies carried by the equity method (see Note 2.b), are recorded as follows:

1. Listed securities:

At the lower of cost or market. The market value was taken to be the lower of average market price in the last quarter or market price at year-end.

2. Unlisted securities:

At cost, net, if appropriate, of the required provisions for depreciation if cost was higher than reasonable value at year-end.

Unrealized losses (cost higher than market or reasonable value at year-end) are recorded in the "Provision for Financial Investments" account.

g) Deferred charges-

This caption in the accompanying consolidated balance sheets includes the following items:

Debt arrangement expenses-

These relate to long-term debt arrangement expenses and paid-in surpluses on debentures and bonds and are amortized by the interest method on the basis of the principal amounts outstanding.

Exchange losses-

Unrealized exchange losses are charged to income by the interest method, as provided by a Ministry of Economy and Finance Order dated March 12, 1993, adapting the Spanish National Chart of Accounts to certain companies (see Note 4.j).

Interest on promissory notes-

This relates to the difference between the par value and the effective issue value of the promissory notes issued at over one year. This interest is charged to income by the interest method.

Interest on financial lease contracts-

This relates to the interest expenses on financial lease contracts, which are charged to income by the interest method (see Note 4.d).

Supplementary pension payments to retired employees (shortfall)-

These relate to the shortfall in the provisions recorded for the commitments made by Telefónica to retired employees as of June 30, 1992. Since then, the shortfall has been allocated to income over 15 years by the straight-line method (see Notes 4-k and 14).

h) Inventories-

Warehouse materials for installation in capital expenditure projects and consumables and replacement parts are valued at weighted average cost, monetarily adjusted in the countries whose legislation so requires.

Obsolete, defective or slow-moving inventories have been reduced to realizable value. The provisions for depreciation of inventories are recorded based on age and turnover.

i) Capital subsidies-

Capital subsidies are valued at the amount granted and are allocated to income on a straight-line basis over a maximum period of ten years, which does not differ materially from the estimated useful life of the subsidized assets.

The main subsidies obtained were granted as follows:

Grantor	Reason for Granting
Official agencies, autonomous community governments and regional and local authorities	Extension of supply to rural areas
European Union	Promotion and development of telecommunications activities
European Union (FEDER Programme)	Infrastructures for depressed areas

All the aforementioned subsidies were granted to the parent company and all the subsidy grant requirements are being met in all cases.

j) Foreign currency transactions-

Fixed-income securities and receivables and payables denominated in foreign currencies are translated to pesetas at the exchange rates ruling at the transaction date, and are adjusted at year-end to the exchange rates then prevailing.

Exchange differences arising on adjustment of foreign currency accounts payable and receivable to year-end exchange rates are classified by currency and due date, and for this purpose currencies which, although different, are officially convertible are grouped together.

The positive net differences in each group of currencies are recorded under the "Deferred Revenues" caption on the liability side of the consolidated balance sheet, unless exchange losses in a given group have been charged to income in prior years, in which case the net positive differences are credited to period income up to the limit of the negative net differences charged to income in prior years.

The positive differences deferred in prior years are credited to income in the year in which the related accounts receivable and payable fall due or are repaid early, or as negative exchange differences for the same or a higher amount are recognized in each homogeneous group.

In accordance with a Ministry of Economy and Finance Order dated March 12, 1993 (published in Official State Gazette No. 64 of March 16, 1993), which adapts the foreign currency transaction valuation method in the Spanish National Chart of Accounts for certain companies, including Telefónica, exchange differences on each transaction in the year must be allocated by the interest method over the term of the transaction.

In view of the foreseeable full deregulation of telecommunications from January 1, 1998, in 1995 Telefónica wrote off (with a charge to income) the potential unrealized exchange losses relating to debts maturing after the aforementioned date. In 1996 Telefónica recorded the deferred losses for the period with a charge to income. Exchange losses allocable to 1997 are included under the "Deferred Charges" caption and will be expensed in that year (see Notes 9 and 20).

k) Pension and similar commitments-

Until December 31, 1991, Telefónica de España, S.A. personnel benefited from a social welfare system provided by Institución Telefónica de Previsión (ITP), currently in liquidation. A Ministry of Labor and Social Security Order dated December 30, 1991, provided for the inclusion of the serving and retired employees of ITP be included in the general social security system. Since January 1, 1992, Telefónica and its employees have been contributing to the general social security system.

The methods used to record and calculate the commitments arising from the aforementioned events are as follows:

Cost of including the pensioners in the social security system-

A resolution issued by the Directorate-General of Planning and Economic Organization of the Social Security System on May 25, 1992, stipulated that the cost of including ITP pensioners in the social security system would amount to Ptas. 130,683 million. ITP had to pay this amount as follows.

1. An initial payment of Ptas. 75,000 million.
2. The remaining Ptas. 55,683 million will be paid over a period of ten years in constant annual installments plus interest at 8%.

Since ITP is in liquidation and does not have sufficient resources to meet the payments, Telefónica, which is vicariously liable, has been contributing the necessary funds to make the payments. As of December 31, 1996 and 1995, the outstanding debt to the social security authorities amounted to Ptas. 38,688 million and Ptas. 44,794 million, respectively, for which Telefónica has recorded the related provisions under the "Provisions for Contingencies and Expenses" caption (see Note 14).

Economic compensation for the inclusion of serving employees-

As a result of the inclusion of serving employees in the social security system, during a period of 25 years Telefónica must make additional contributions to the social security system, based on the serving employees' contribution bases. These contributions consist of the payment of an additional 1% during the first four years and of an additional 2.2% over the remainder.

In 1992, Telefónica entered into a collective labor agreement, pursuant to the Workers' Statute, with the workers' representatives for the creation of a pension plan for serving employees. The agreement also recognized the entitlement of retired employees to receive pension payments supplementing their social security pensions. The commitments undertaken and the methods for recording them are as follows:

Pension plan-

Following an after made on June 30, 1992, and accepted by the workers on September 17, 1992, Telefónica reached a collective labor agreement, pursuant to the workers' statute, with the workers' representatives. The main features of the pension plan are as follows:

Creation of a pension plan pursuant to Pension Plans and Funds Law 8/1987 with the following features:

- a) Employment system pension plan
- b) Defined contribution
- c) Mandatory contributions by the participating employees
- d) Individual and financial capitalization
- e) Contribution by the promoter of 6.87% of the participating employees' regulatory base salary. For employees who joined Telefónica after June 30, 1992, the contribution is 4.51% of the regulatory base salary
- f) The obligatory contribution of the participants will be a minimum of 2.2% of his/her regulatory base salary

The plan came into effect on July 1, 1992. The past service benefits recognized for employees availing themselves of the plan amounted to Ptas. 228,489 million, which, in accordance with the Rebalancing Plan approved on July 18, 1995, by the Directorate-General of Insurance and by a Ministry of Economy and Finance Resolution dated April 24, 1996, will be financed as follows:

1. Telefónica will contribute the Ptas. 121,350 million that it had recorded under the "Long-Term Debt - Other Accounts Payable" caption. This amount will be transferred through the year 2000 at an annual effective interest rate of 6.7%.
2. The resulting shortfall (Ptas. 107,139 million) must be contributed to the pension plan within 28 years in monthly installments payable in advance at an annual interest rate of 6%. The Company records provisions for the shortfall over 28 years pursuant to a systematic plan, with installments increasing each year by Ptas. 1,042 million through the year 2002 and based on the Rebalancing Plan thereafter. The resulting cumulative difference (Ptas. 9,121 million as of December 31, 1996) between the provisions recorded and the contributions made to the pension plan is recorded in the "Provisions for Contingencies and Expenses - Provisions for the Rebalancing Plan" account. The provision for 1996 was Ptas. 4,677 million (Ptas. 4,486 million in 1995) (see Note 14).

In accordance with the conditions for adhesion to the Plan, transfers have been made for a total amount of Ptas. 124,099 million, as follows:

	Transfer Plan		Underprovision		Extraordinary Contribution	Total
	Principal	Interest	Principal	Interest		
Through 12/31/94	30,142	18,261	4,900	14,628	1,308	69,239
Transferred in 1995	14,304	5,391	2,761	5,648	575	28,679
Transferred in 1996	13,961	4,486	1,625	5,531	578	26,181
Total	58,407	28,138	9,286	25,807	2,461	124,099

At year-end, the principal not yet transferred to the Plan amounted to Ptas. 158,335 million.

3. As of December 31, 1996, 67,135 employees (66,830 at the same date in 1995) had joined the Plan. The retirement, disability and death benefits earned affected a total of 4,615 participants in 1996 (3,446 in 1995).

Supplementary pension payments to retired employees-

On July 8, 1992, Telefónica reached an agreement with its employees whereby it recognized supplementary pension payments for employees who were retired as of June 30, 1992, equal to the difference between the pension payable by the social security system and that which would be paid to them by ITP. Once the aforementioned supplementary pension payments have been quantified, they become fixed, lifelong and nonrevaluable. 60% of the payments are transferable to the spouse recognized as such as of June 30, 1992, and to underage children.

In accordance with an actuarial study conducted by Telefónica, applying GRM-80 tables and an assumed interest rate of 8%, as of June 30, 1992, the discounted present value of the commitments amounted to Ptas. 132,025 million, and this amount was recorded under the "Provisions for Contingencies and Expenses" caption. Through that date, the Company had recorded provisions totaling Ptas. 14,356 million in this connection. The resulting underprovision (Ptas. 117,669 million) was recorded under the "Deferred Charges" caption and has been allocated to income since that date by the straight-line method over 15 years, the estimated remaining life of the retired employees. The balances of these accounts as of December 31, 1996, are shown in Notes 9 and 14.

At each year-end the Company conducts a new actuarial study using the aforementioned assumptions. The increase in discounted present value due to the financial provisions to the fund are recorded as an expense under the "Extraordinary Expenses" caption (see Note 20).

The fall in market interest rates in 1996 induced Telefónica to reduce from 8% to 6.5% the assumed interest rate used in calculating the commitments. Accordingly, the value of the provision required increased by Ptas. 10,597 million. This provision was recorded with a charge to the "Deferred Charges" caption and is being allocated to income over the expected life of the retired employees which, as of January 1, 1996, is 11.5 years.

An external fund must be created for this commitment pursuant to Private Insurance Law 30/1995, within the time limits established in Transitory Provision 14 thereof.

Group life insurance-

Retired employees who did not join the pension plan continue to be entitled to receive survivorship benefits at the age of 65. The Company has recorded an internal allowance to cover these commitments, based on the actuarial studies conducted internally, applying the GRM/F-80 mortality table and an assumed interest rate of 6%. As of December 31, 1996 and 1995, this allowance amounted to Ptas. 13,219 million and Ptas. 16,549 million, respectively, and was recorded under the "Provisions for Contingencies and Expenses" caption (see Note 14).

An external fund must be created for this commitment pursuant to Private Insurance Law 30/1995, within the time limits established in Transitory Provision 14 thereof.

1) Provisions for voluntary early retirements-

The deregulation of the telecommunications industry in Spain made it necessary to adapt the labor force to Telefónica's actual needs and, accordingly, the voluntary redundancy plan initiated in 1994 was continued and extended to provide for voluntary early retirement of employees above 58 years of age. Also, the Company's Strategic Plan for 1996-2000 envisages the possibility of early retirement starting at the age of 57. These plans provide for the possibility of retiring without a notable loss in compensation, thus enabling the labor force to be tailored to the actual needs of each line of business in a nontraumatic manner.

The Company records provisions for the present value of the estimated payments that will be generated in future years as a result of the voluntary early retirements, in accordance with a systematic plan (see Note 14).

m) Technical provisions-

This caption relates mainly to mathematical provisions for life insurance, pension and reinsurance commitments taken on by Seguros de Vida y Pensiones Antares, S.A. and Casiopea Re.

n) Corporate income tax-

The expense for corporate income tax of each year is calculated on the basis of book income before taxes, increased or decreased, as appropriate, by permanent differences. Tax relief and tax credits, excluding tax withholdings and prepayments, are deducted from the corporate income tax charge in the year in which they are definitively taken, except in the case of investment tax credits earned from 1996, which, at the time when they are taken, are deferred over the average life of the assets which gave rise to the tax credits. The difference between the expense incurred and the tax paid is due to revenue and expense recognition timing differences giving rise to prepaid and deferred taxes (see Note 18).

o) Derivatives-

Transactions aimed at eliminating or significantly reducing exchange, interest rate or market risks on balance sheet positions or on other transactions are treated as hedging transactions. The Group performs its hedging transactions through currency and interest rate swaps. The amounts accrued and not paid or collected at year-end are accrued correlatively to the revenues or costs on the hedged transaction in the appropriate asset or liability accrual account (see Note 17).

p) Recognition of revenues and expenses-

Revenues and expenses are recognized on an accrual basis, i.e. when the actual flow of the related goods and services occurs, regardless of when the resulting monetary or financial flow arises.

The revenues from telephony and other services are recognized on an accrual basis. These services are generally billed every two months. Uninvoiced revenues from the beginning of the billing cycle to the end of each month are estimated or recorded as soon as they are known. The differences between the estimated revenues and those subsequently invoiced are not material and are recorded in the following period. In accordance with the accounting principle of prudence, only realized income is recorded at year-end, whereas foreseeable contingencies and losses, including possible losses, are recorded as soon as they become known (see Note 20).

5. GOODWILL IN CONSOLIDATION

The detail of the balance of goodwill in consolidation, the related accumulated amortization and the variations therein in 1996 is as follows:

	Millions of Pesetas					
	Balance at 12/31/95	Additions	Retirements	Transfers	Translation Differences	Balance at 12/31/96
Companies consolidated						
by the global integration method:						
C.T.C. (Chile)	5,508	—	—	—	—	5,508
T.L.D. (Puerto Rico)	7,595	—	(116)	—	—	7,479
Publiguías (Chile)	426	—	—	—	—	426
T. Perú Holding	463	—	—	(2)	—	461
Multicable T.V. (Chile)	992	—	—	2	101	1,095
Invercom	6,710	—	—	(6,710)	—	—
Instacom	1,216	—	(126)	—	244	1,334
Intercom	—	(111)	—	—	—	(111)
Servicios y Contenidos por la Red	—	126	—	—	—	126
TMP Worldwide	—	8	—	—	—	8
	22,910	23	(242)	(6,710)	345	16,326
Companies carried by the equity method:						
Sofres, A.M.	157	—	—	—	—	157
Venworld (Venezuela)	19,982	—	—	2,348	—	22,330
Tepesa	7	—	(7)	—	—	—
Cointel (Argentina)	23,835	—	—	1	—	23,836
Multicanal	—	9,155	—	—	—	9,155
Invercom	—	—	—	6,648	775	7,423
Unisource, N.V.	—	7,742	—	—	—	7,742
Siris y DBKOM	—	1,130	—	—	—	1,130
	43,981	18,027	(7)	8,997	775	71,773
Total goodwill	66,891	18,050	(249)	2,287	1,120	88,099
Companies consolidated						
by the global integration method:						
C.T.C. (Chile)	3,151	551	—	1	—	3,703
T.L.D. (Puerto Rico)	2,360	748	(116)	—	—	2,992
Publiguías (Chile)	128	43	—	—	—	171
T. Perú Holding	52	46	—	(1)	—	97
Multicable T.V. (Chile)	35	105	—	1	7	148
Invercom	1,114	—	—	(1,114)	—	—
Instacom	230	130	(126)	—	165	399
Intercom	—	(8)	—	—	(20)	(28)
Servicios y Contenidos por la Red	—	126	—	—	—	126
TMP Worldwide	—	8	—	—	—	8
	7,070	1,749	(242)	(1,113)	152	7,616
Companies carried by the equity method:						
Sofres, A.M.	140	17	—	—	—	157
Venworld (Venezuela)	6,585	2,233	—	2,347	—	11,165
Tepesa	7	—	(7)	—	—	—
Cointel (Argentina)	5,402	2,495	—	1	—	7,898
Multicanal	—	704	—	—	—	704
Invercom	—	716	—	1,052	121	1,889
Unisource, N.V.	—	7,742	—	—	—	7,742
Siris y DBKOM	—	1,130	—	—	—	1,130
	12,134	15,037	(7)	3,400	121	30,685
Total accumulated amortization	19,204	16,786	(249)	2,287	273	38,301
Unamortized goodwill in consolidation	47,687	1,264	—	—	847	49,798

Because of the long maturation period of the investments to be made by UNISOURCE, N.V. and the difficulty in predicting the impact on this company of the deregulation of telecommunications in Europe, Telefónica decided to amortize, with a charge to 1996 income, the goodwill arising on the acquisition of the shares of UNISOURCE, N.V.

The detail of the balance of goodwill in consolidation, the related accumulated amortization and the variations therein in 1995 is as follows:

	Millions of Pesetas					
	Balance at 12/31/94	Additions	Retirements	Transfers	Translation Differences	Balance at 12/31/95
Companies consolidated by the global integration method:						
C.T.C. (Chile)	5,508	—	—	—	—	5,508
T.L.D. (Puerto Rico)	7,595	—	—	—	—	7,595
Publiguías (Chile)	426	—	—	—	—	426
T. Perú Holding	463	—	—	—	—	463
Multicable T.V. (Chile)	—	992	—	—	—	992
Invercom	6,710	—	—	—	—	6,710
Instacom	1,216	—	—	—	—	1,216
	21,918	992	—	—	—	22,910
Companies carried by the equity method:						
Sofres, A.M.	157	—	—	—	—	157
Venworld (Venezuela)	19,982	—	—	—	—	19,982
Tepesa	7	—	—	—	—	7
Cointel (Argentina)	23,823	12	—	—	—	23,835
	43,969	12	—	—	—	43,981
Total goodwill	65,887	1,004	—	—	—	66,891
Companies consolidated by the global integration method:						
C.T.C. (Chile)	2,601	550	—	—	—	3,151
T.L.D. (Puerto Rico)	1,612	748	—	—	—	2,360
Publiguías (Chile)	86	42	—	—	—	128
T. Perú Holding	6	46	—	—	—	52
Multicable T.V. (Chile)	—	37	—	—	(2)	35
Invercom	373	678	—	—	63	1,114
Instacom	94	126	—	—	10	230
	4,772	2,227	—	—	71	7,070
Companies carried by the equity method:						
Sofres, A.M.	109	31	—	—	—	140
Venworld (Venezuela)	4,349	2,234	—	—	2	6,585
Tepesa	7	—	—	—	—	7
Cointel (Argentina)	2,909	2,493	—	—	—	5,402
	7,374	4,758	—	—	2	12,134
Total accumulated amortization	12,146	6,985	—	—	73	19,204
Unamortized goodwill in consolidation	53,741	(5,981)	—	—	(73)	47,687

6. INTANGIBLE ASSETS

The detail of the balances of the intangible asset accounts and the variations therein in 1996 and 1995 are as follows:

Millions of Pesetas					
	Research and Development Expenses	Leased Assets	Indefinite Software User Licenses	Other Intangible Assets	Total
Balance at 12/31/94	60,193	9,132	39,875	236,793	345,993
Additions	19,522	1,588	14,304	3,288	38,702
Retirements	—	—	(35)	(1,203)	(1,238)
Transfers	(87)	(70)	25	2,584	2,452
Inclusion of companies	—	61	9	8	78
Variation in exchange rate and other	—	—	—	(447)	(447)
Balance at 12/31/95	79,628	10,711	54,178	241,023	385,540
Additions	21,170	4,080	19,330	802	45,382
Retirements	—	—	(168)	(38)	(206)
Transfers	3,170	732	80	(2,155)	1,827
Inclusion of companies	—	—	—	—	—
Variation in exchange rate	79	1	52	295	427
Exclusion of companies	—	(99)	(6)	(57)	(162)
Balance at 12/31/96	104,047	15,425	73,466	239,870	432,808

The main item included under the "Other Intangible Assets" caption was the administrative concession described in Note 4.d, amounting to Ptas. 224,491 million.

The variations in the related accumulated amortization were as follows:

Millions of Pesetas					
	Research and Development Expenses	Leased Assets	Indefinite Software User Licenses	Other Intangible Assets	Total
Balance at 12/31/94	17,814	741	21,764	5,467	45,786
Provisions	11,084	1,242	5,604	5,770	23,700
Retirements	—	—	(31)	(1,041)	(1,072)
Transfers	(36)	(16)	(49)	85	(16)
Inclusion of companies	—	2	4	10	16
Variation in exchange rate and other	—	—	—	(113)	(113)
Balance at 12/31/95	28,862	1,969	27,292	10,178	68,301
Provisions	11,768	1,784	5,846	6,863	26,261
Retirements	—	—	(63)	(46)	(109)
Transfers	536	(29)	55	(112)	450
Inclusion of companies	—	—	—	—	—
Variation in exchange rate	61	44	65	(57)	113
Exclusion of companies	—	(2)	(3)	(28)	(33)
Balance at 12/31/96	41,227	3,766	33,192	16,798	94,983
Intangible assets, net	62,820	11,659	40,274	223,072	337,825

7. PROPERTY AND EQUIPMENT

The detail of the balances of property and equipment, the related accumulated depreciation and the variations therein in 1996 is as follows:

	Millions of Pesetas								Balance at 12/31/96
	Balance at 12/31/95	Additions	Retirements	Inclusion of Companies	Exclusion of Companies	Exchange Differences	Transfers	Account Restatement	
Cost:									
Land and structures	570,203	643	(4,098)	90	(900)	4,638	33,896	51,807	656,279
Technical installations and machinery	135,885	3,855	(6,752)	—	(1,029)	—	(1,472)	—	130,487
Telephone installations, networks and equipment	5,285,469	80,178	(430,982)	2,619	—	59,547	429,028	172,164	5,598,023
Furniture, tools and other	231,059	13,702	(6,521)	1,117	(5,365)	6,170	(4,461)	1,881	237,582
Total property and equipment in service	6,222,616	98,378	(448,353)	3,826	(7,294)	70,355	456,991	225,852	6,622,371
Net variation in construction in progress	291,302	564,848	(69)	—	—	6,936	(535,156)	—	327,861
Advances to fixed-asset suppliers	10,574	5,812	(238)	—	—	47	7,445	—	23,640
Installation materials in warehouses	14,014	7,338	—	—	—	(183)	29,635	—	50,804
Total property and equipment	6,538,506	676,376	(448,660)	3,826	(7,294)	77,155	(41,085)	225,852	7,024,676
Accumulated depreciation:									
Structures	133,389	14,196	(729)	8	(142)	1,477	(22)	—	148,177
Technical installations and machinery	68,861	9,066	(5,950)	—	(601)	—	223	—	71,599
Telephone installations, networks and equipment	2,605,859	454,045	(381,334)	234	—	21,977	(18,024)	—	2,682,757
Furniture, tools and other	132,971	23,674	(6,170)	100	(3,727)	2,329	(904)	—	148,273
Total accumulated depreciation	2,941,080	500,981	(394,183)	342	(4,470)	25,783	(18,727)	—	3,050,806
Property and equipment, net	3,597,426	175,395	(54,477)	3,484	(2,824)	51,372	(22,358)	225,852	3,973,870

The detail of the balances of property and equipment, the related accumulated depreciation and the variations therein in 1995 is as follows:

Millions of Pesetas							
	Balance at 12/31/94	Additions	Retirements	Inclusion of Companies	Exchange Differences	Transfers	Balance at 12/31/95
Cost:							
Land and structures	529,777	3,261	(604)	182	(1,333)	38,920	570,203
Technical installations and machinery	132,412	3,420	(5,795)	118	(10)	5,740	135,885
Telephone installations, networks and equipment	5,189,741	118,480	(315,566)	—	(16,315)	309,129	5,285,469
Furniture, tools and other	188,039	11,013	(3,727)	239	(87)	35,582	231,059
Total property and equipment in service	6,039,969	136,174	(325,692)	539	(17,745)	389,371	6,222,616
Net variation in construction in progress	247,143	446,513	(1,281)	—	362	(401,435)	291,302
Advances to fixed-asset suppliers	8,221	2,474	—	—	—	(121)	10,574
Installation materials in warehouses	16,194	6,432	—	—	—	(8,612)	14,014
Total property and equipment	6,311,527	591,593	(326,973)	539	(17,383)	(20,797)	6,538,506
Accumulated depreciation:							
Structures	118,674	13,212	(67)	36	(451)	1,985	133,389
Technical installations and machinery	62,830	11,071	(4,606)	103	(4)	(533)	68,861
Telephone installations, networks and equipment	2,461,283	429,673	(258,868)	—	(8,045)	(18,184)	2,605,859
Furniture, tools and other	109,156	23,660	(2,991)	150	(590)	3,586	132,971
Total accumulated depreciation	2,751,943	477,616	(266,532)	289	(9,090)	(13,146)	2,941,080
Property and equipment, net	3,559,584	113,977	(60,441)	250	(8,293)	(7,651)	3,597,426

The installation materials in warehouses are recorded net of provisions, which amounted to Ptas. 5,936 million as of December 31, 1996 (Ptas. 4,921 million in 1995). The provision for inventory depreciation recorded in 1996 based on actual diminution in value, amounted to Ptas. 2,496 million (Ptas. 2,598 million in 1995).

The "Inclusion of Companies" account in 1996 includes the variations in property and equipment as a result of the merger of the Chilean companies VTR and CTC Celular, since this merger resulted in the contribution of assets to the Group.

The "Exclusion of Companies" account in 1996 includes the accumulated balances as of December 31, 1995, of the Sintel Group companies, Tepesa, Telefónica Transmisión de Datos (TTD), Sociedad General de Cablevisión and Telefónica VSAT, since they were excluded from the consolidated Group in 1996.

The "Exchange Differences" column includes both the effect of the variation in exchange rates on the beginning balances and the monetary adjustment applied by certain companies to their balances to adjust for inflation, in accordance with the accounting practices in their respective countries. The effect of exchange rates on the period variations is included under the appropriate column for each variation.

As of December 31, 1996 and 1995, the following items had been fully depreciated:

Millions of Pesetas		
	1996	1995
Buildings	7,201	4,716
Power equipment	26,583	29,732
Switching equipment	334,529	328,525
Transmission equipment	157,050	174,764
Local and domestic long-distance networks	160,350	160,617
Subscriber equipment and other installations	155,987	119,769
Furniture, office equipment and other	87,454	67,905
Total	929,154	886,028

Telefónica's fixed assets used to provide telephone services cannot be mortgaged unless so authorized by the Government Delegate after they cease to be used for such purpose.

Telefónica has taken out insurance policies to cover the possible risks affecting its property and equipment used in operations, except for the deductible applicable to local and domestic long-distance networks and subscriber equipment.

On December 31, 1996, Telefónica restated its property and equipment pursuant to Royal Decree-Law 7/1996 and paid the related single 3% tax. The Company had previously restated its accounts pursuant to the enabling legislation specifically applicable to Telefónica de España. The 1996 restatement was performed by applying the maximum coefficients authorized under this Royal Decree-Law, with the 40% reduction provided for the effect of Company financing and observing the restatement limit imposed by the market value of the restated assets.

The restatement surplus, net of the single 3% tax, was credited to the "Restatement Reserves" caption, with a charge to the appropriate restated asset accounts, without altering the recorded accumulated depreciation amount.

The net increase in value resulting from this restatement will be depreciated over the tax periods in the remaining useful lives of the restated assets. It is estimated that the 1996 restatement will increase the 1997 depreciation charge by approximately Ptas. 35,320 million.

The account restatements made from 1946 to 1987 gave rise to variations in the following accounts:

	Millions of Pesetas		
	Total Effect		
	Gross Values	Accumulated Depreciation	Restatement Reserves
Land lots	30,041	—	30,041
Structures	93,282	25,034	68,248
Power equipment	31,525	14,973	16,552
Switching equipment	504,642	215,690	288,952
Transmission equipment	151,036	95,018	56,018
Local and domestic long-distance networks	648,945	331,751	317,194
Subscriber equipment and other installations	(4,153)	27,649	(31,802)
Total	1,455,318	710,115	745,203

The effect of these restatements on the 1996 and 1995 depreciation charges was Ptas. 10,786 million and Ptas. 12,548 million, respectively.

The detail of the property and equipment included in the consolidated Group and owned by Group companies located abroad as of December 31, 1996 and 1995, is as follows:

	Millions of Pesetas	
	1996	1995
Cost	1,133,947	864,724
Accumulated depreciation	(374,528)	(292,142)
Total	759,419	572,582

8. LONG-TERM FINANCIAL INVESTMENTS

A) The detail of the balances of and variations in financial investments in 1996 and 1995, of the related provision for depreciation, and of the capital payments outstanding is as follows:

1. Variations in financial investments:

Millions of Pesetas									
	Balance at 12/31/94	Additions	Retirements	Transfers and Consol.	Balance at 12/31/95	Additions	Retirements	Transfers and Consol.	Balance at 12/31/96
Holdings in associated companies	88,843	2,173	(498)	(5,179)	85,339	35,350	(6,395)	2,023	116,317
Other holdings	36,406	15,365	(4,598)	(1,298)	45,875	85,276	(2,649)	38	128,540
Other loans	10,490	14,954	(4,896)	(119)	20,429	17,913	(19,416)	12,448	31,374
Guarantees and deposits	1,313	247	(298)	—	1,262	409	(304)	2	1,369
Total	137,052	32,739	(10,290)	(6,596)	152,905	138,948	(28,764)	14,511	277,600

2. Variations in the provision for depreciation of financial investments:

Millions of Pesetas									
	Balance at 12/31/94	Additions	Retirements	Transfers and Consol.	Balance at 12/31/95	Additions	Retirements	Transfers and Consol.	Balance at 12/31/96
Other holdings	4,642	88	(802)	—	3,928	1,702	(901)	—	4,729
Total	4,642	88	(802)	—	3,928	1,702	(901)	—	4,729
Total financial investments	132,410	32,651	(9,488)	(6,596)	148,977	137,246	(27,863)	14,511	272,871

3. Variations in capital payments outstanding:

Millions of Pesetas									
	Balance at 12/31/94	Additions	Retirements	Transfers and Consol.	Balance at 12/31/95	Additions	Retirements	Transfers and Consol.	Balance at 12/31/96
Group companies	—	10	—	—	10	—	(10)	—	—
Associated companies	—	184	—	—	184	169	(110)	—	243
Other companies	50	2,503	—	(9)	2,544	—	(36)	—	2,508
Total	50	2,697	—	(9)	2,738	169	(156)	—	2,751
Total financial investments, net	132,360	29,954	(9,488)	(6,587)	146,239	137,077	(27,707)	14,511	270,120

B) Exhibit I to these notes to financial statements provides detailed information on the Group companies, the percentages of ownership therein and the consolidation method used.

C) As part of the reorganization of its corporate group, Telefónica carried out the following transactions:

1. In 1995, in application of Law 29/1991, adapting certain tax concepts to EC Directives and regulations:

— Contribution of mobile telephony lines of business to the subsidiary Telefónica Servicios Móviles, S.A.

— By means of a share exchange transaction, Telefónica de España, S.A. contributed to Telefónica Publicidad e Información, S.A. all the capital stock of Estrategias Telefónicas, S.A.

The disclosures referred to in Article 14 of Law 29/1991 are included in the first annual report approved following the transactions.

D) In 1995 Telefónica carried out the following transactions in accordance with Chapter VIII of Corporate Income Tax Law 43/1995.

1. With Telefónica Transmisión de Datos, S.A.:

Nonmonetary contribution of assets to Telefónica Transmisión de Datos, S.A., based on values verified by independent appraisers, as follows:

Assets Contributed, Net of Depreciation and Amortization	Millions of Pesetas	
	Liabilities Assigned	Net Value of the Contribution
26,036	12,500	13,536

As a consideration for the aforementioned contribution, Telefónica received from Telefónica Transmisión de Datos, S.A. shares of the capital increase carried out for this purpose with a par value of Ptas. 9,328 million and a share premium of Ptas. 6,219 million. This investment was recorded in the "Long-Term Financial Investments" of Telefónica for the difference between the net book value of the assets contributed and the amount of the financial liabilities assigned to the assets transferred. Telefónica Transmisión de Datos, S.A. undertook to repay to Telefónica de España, S.A. the amount of such liabilities within three years.

The tax benefits obtained by Telefónica from the accelerated depreciation of the assets will be reversed at Telefónica in the year in which the contribution takes place. The investment tax credits relating to the assets contributed by Telefónica amount to Ptas. 27,335 million for 1991 to 1995. Ptas. 250 million of the unused tax credits, which were earned in 1991, were transferred to Telefónica Transmisión de Datos.

2. With Unisource, N.V.:

By means of a share exchange transaction, Telefónica de España, S.A. contributed to Unisource, N.V. 1,208,149 shares of Telefónica Transmisión de Datos, S.A. and 26,200 shares of Telefónica VSAT, S.A., representing 100% of the capital stock of both companies, and received in exchange 23,000 new shares of Unisource, N.V. of 1,000 Dutch guilders par value each, representing 25% of its capital stock. The mandatory appraisal was carried out by an independent appraiser.

Telefónica recorded these amounts under "Long-Term Financial Investments" at the same value as that for which it had recorded the shares of Telefónica Transmisión de Datos, S.A. and of Telefónica VSAT, S.A. (i.e. Ptas. 16,804 million).

3. In 1996 the Telefónica Group sold its holdings in various companies with the following results:

		Millions of Pesetas	
	Percentage of Capital Stock Sold	Amount Sold	Gain (Loss)
Subsidiaries and associated companies:			
Sistemas e Instalaciones de Telecomunicaciones, S.A.	100.00	7,935	(2,347)
Sociedad General de Cablevisión, S.A.	50.00	1,069	(222)
Tepesa, S.A.	55.64	139	(30)
Telecartera, S.A.	0.12	1	—
VTR	20.00	67 M US\$	6,597
Telefónica Argentina, S.A.	0.67	2,526	3,666
Telecom Vallés, S.A.	24.90	26	—
S.A.P.E.C.	33.00	13	(10)
Amper, S.A.	0.35	10	72
Investees:			
Investees of CTC	—	—	183
European Silicom Structures, S.A.	0.38	460	(6)
Cable del Guadalquivir, S.A.	20.00	5	—
Grupo Gallego de Empresas para el Cable, S.A.	10.00	5	(1)
Financial Network Association, S.A.	8.33	2	1

The detail of the holdings disposed of by the Telefónica Group in 1995 and of the gains on the disposals is as follows:

	Percentage of Capital Stock Sold	Millions of Pesetas	
		Amount Sold	Gain (Loss)
Industria Electrónica de Comunicaciones, S.A.	20.74	67	353
Fonditel Entidad Gestora de Fondos de Pensiones	19.00	430	—
ATT Network System International, B.V.	5.84	2,849	3,693
Inalca, S.A.	44.00	12	32
Telefónica de Argentina, S.A.	2.15	8,317	7,283
Sistemas Avanzados de Control, S.A.	42.12	—	—

E) The Group companies listed on the stock exchange and their market value at year-end and the average market price in the last quarter are as follows:

			Market Price 12/31/96		
Company		Currency	Stock Exchange	Year-End	Average Last Quarter
Telefónica	shares	Peseta	Madrid	3,015	2,742
Telefónica	ADSs	U.S. dollar	New York	69.25	63.14
Telefónica	shares	Yens	Tokio	2,590	2,378
Telefónica	shares	Deutsch marks	Frankfurt	36.20	32.31
Telefónica	shares	U.S. dollar	SEAQ	69.31	63.06
Telefónica	shares	French francs	Paris	122.50	110.06
Amper		Peseta	Madrid	2,975	2,084
CTC (Chile)	A shares	Chilean peso	Santiago	2,435	2,394
CTC (Chile)	B shares	Chilean peso	Santiago	2,200	2,202
CTC (Chile)	ADSs	U.S. dollar	New York	23.79	23.10
TASA (Argentina)		Argentinean peso	Buenos Aires	2.65	2.51
TASA (Argentina)	ADRs	U.S. dollar	New York	25.88	25.12
Telefónica del Perú (Peru)	B shares	New sol	Lima	4.86	5.31
Telefónica del Perú (Peru)	C shares	New sol	Lima	4.86	5.31
Telefónica del Perú (Peru)	ADRs	U.S. dollar	New York	18.88	20.74
C.A.N.T.V. (Venezuela)		Bolivar	Caracas	1,865	1,787
C.A.N.T.V. (Venezuela)		U.S. dollar	New York	28.13	26.74

The market prices are expressed in the currency in which the shares are traded.

- Telefónica: 1 ADS = 3 shares
- T.A.S.A.: 1 ADR = 10 shares
- C.T.C.: 1 ADS = 4 shares
- Telefónica del Perú: 1 ADR = 10 shares
- C.A.N.T.V.: 1 ADR = 7 shares

9. DEFERRED CHARGES

The breakdown of the balance of this caption and the amortization schedule are as follows:

	Millions of Pesetas								
	Maturity						Subsequent Years	Balance at 12/31/96	Balance at 12/31/95
	1997	1998	1999	2000	2001				
Pension supplements (shortfall)	9,108	9,108	9,108	9,108	9,108	50,102	95,642	94,154	
Debt arrangement expenses	4,913	3,345	2,407	1,839	1,000	2,206	15,710	15,818	
Interest on long-term promissory notes	3,562	3,780	2,740	1,550	183	—	11,815	15,647	
Exchange losses	6,401	—	—	—	—	—	6,401	12,951	
Interest on lease transactions	293	270	36	16	—	1	616	2,579	
Other deferred charges	110	—	—	—	—	—	110	161	
Total	24,387	16,503	14,291	12,513	10,291	52,309	130,294	141,310	

Pension supplements (shortfall)-

This caption relates to supplementary pension commitments to retired employees which have not yet been allocated to income (see Note 4.k).

The variations in the balances of this caption in 1996 and 1995 were as follows:

	Millions of Pesetas
Balance at 12/31/94	101,002
Amortization	(8,455)
Other variations	1,607
Balance at 12/31/95	94,154
Amortization	(9,109)
Change of assumed interest rate (Note 4-k)	10,597
Balance at 12/31/96	95,642

The "Other Variations" account reflects the year-on-year differences in the actuarial calculations of the supplementary pension commitments (see Note 4.k).

Exchange differences-

As indicated in Note 4-j, Telefónica has deferred potential losses relating to exchange losses at each year-end, with maturity through 1997. The deferred amount as of December 31, 1996, amounted to Ptas. 6,401 million (Ptas. 12,951 million as of December 31, 1995). These exchange differences will be amortized in full in 1997.

10. CUSTOMER RECEIVABLES

The detail of the balances of this caption as of December 31, 1996 and 1995, is as follows:

	Millions of Pesetas	
	Balance at 12/31/96	Balance at 12/31/95
Services billed-		
Customers billed	133,294	185,815
Doubtful customer receivables	39,394	22,430
Other	2,978	1,420
	175,666	209,665
Unbilled services	230,056	143,085
	405,722	352,750
Allowance for bad debts	(43,196)	(36,485)
Total	362,526	316,265

The "Unbilled Services" account includes the connection, subscription and metered service charges not yet billed by Telefónica and the other Group operators. This amount arises because these companies' subscriber billing schedules do not coincide with year-end (see Note 4.p).

At Telefónica de España, S.A. the balance of the public-sector customer account receivable in 1996 amounted to Ptas. 52,671 million (Ptas. 59,586 million in 1995). Under a Royal Decree-Law dated July 29, 1996, the government approved the payment of Ptas. 24,758 million of this debt in 1997.

Ptas. 15,522 million of uncollectible accounts were retired in 1996 (Ptas. 21,652 million in 1995).

11. STOCKHOLDERS' INVESTMENT

The detail of the balances and variations in equity accounts in 1996 and 1995 is as follows:

	Millions of Pesetas						
	Balance at 12/31/94	Distribution of 1994 Income	Other Variations	Balance at 12/31/95	Distribution of 1995 Income	Other Variations	Balance at 12/31/96
Capital stock	469,735	—	—	469,735	—	—	469,735
Paid-in surplus	43,067	—	—	43,067	—	—	43,067
Restatement reserve	649,316	—	—	649,316	—	219,076	868,392
Legal reserve	66,279	9,174	—	75,453	10,618	—	86,071
Voluntary reserve	107,280	22,869	—	130,149	26,816	96	157,061
Consolidation reserve	32,035	18,504	1,058	51,597	24,415	(77)	75,935
Retained earnings	91	56	—	147	(35)	—	112
Consolidation translation differences	31,620	—	(9,642)	21,978	—	14,008	35,986
Income for the year	112,608	(112,608)	133,214	133,214	(133,214)	160,282	160,282
Interim dividend	—	—	(28,184)	(28,184)	28,184	(32,881)	(32,881)
Total	1,512,031	(62,005)	96,446	1,546,472	(43,216)	360,504	1,863,760

a) Capital stock-

As of December 31, 1996, Telefónica's capital stock consisted of 939,470,820 fully subscribed and paid bearer shares of Ptas. 500 par value each, all recorded by the book-entry system of trading and listed on the four Spanish stock exchanges and on the Frankfurt, London, Paris, Tokyo and New York stock exchanges. According to the information to which Telefónica has had access, as of December 31, 1996, significant holdings in its capital stock were owned by the State Property Agency, through Sociedad Estatal de Participaciones Patrimoniales (SEPPA) and Sociedad Estatal de Patrimonio II (a total of 22.2% of the capital stock); Caja de Ahorros y Pensiones de Barcelona (5.010%); Banco Bilbao Vizcaya, S.A. (5.005%) and Argentaria (3.090%).

On April 21, 1995, the Stockholders' Meeting authorized the Board of Directors to increase capital, at one or several times, up to a maximum of Ptas. 704,603 million within a maximum period of five years and with no need for further notice or resolution.

b) Legal reserve-

Under the revised Corporations Law, 10% of income for each year must be transferred to the legal reserve until the balance of this reserve reaches at least 20% of capital stock. The legal reserve can be used to increase capital provided that the remaining reserve balance does not fall below 10% of the increased capital stock amount. Otherwise, until the legal reserve exceeds 20% of capital stock, it can only be used to offset losses, provided that sufficient other reserves are not available for this purpose.

c) Restatement reserve-

The balance of the "Restatement Reserves" caption arose as a result of restatements made from 1946 to 1987, and of the restatement pursuant to Royal Decree-Law 7/1996.

As of December 31, 1996 and 1995, the balances of the restatement reserve amounted to Ptas. 868,392 million and Ptas. 649,316 million, respectively, as follows:

	Millions of Pesetas	
	1996	1995
Restatements from 1946 to 1987:		
Restatements made	745,203	745,203
Amounts used-		
Capital increases from 1977 to 1986	(74,487)	(74,487)
Transfer to provisions in 1982	(18,829)	(18,829)
Other variations from 1981 to 1986	(2,571)	(2,571)
	649,316	649,316
1996 restatement:		
Restatement Reserve Royal Decree-Law 7/1996	225,852	—
Single tax on restatements	(6,776)	—
Total	868,392	649,316

As of December 31, 1996, the balance of the reserve relating to the restatements made from 1946 to 1987 was unrestricted as to its use.

From the date on which the tax authorities have reviewed and approved the balance of the "Restatement Reserve Royal Decree-Law 7/1996" account (or the three-year period for review has expired), the aforementioned balance can be used, free of tax, to offset recorded losses which might arise in the future, and to increase capital stock. From January 1, 2007 (ten years from the date of the balance sheet reflecting the restatements), the balance of this account can be taken to unrestricted reserves, provided that the monetary surplus has been realized. The surplus is deemed to be realized in respect of the portion relating to the depreciation recorded for accounting purposes or when the restated assets have been transferred or retired from the accounting records.

d) Consolidation reserve-

The detail of the consolidation reserve and of the variations therein in 1996 and 1995 is as follows:

	Millions of Pesetas			Balance at 12/31/96
	Balance at 12/31/95	Increase	Decrease	
1996				
Companies consolidated by the global and proportional integration methods	27,314	33,864	(2,836)	58,342
Companies carried by the equity method	24,283	917	(7,607)	17,593
Total	51,597	34,781	(10,443)	75,935

	Millions of Pesetas			Balance at 12/31/95
	Balance at 12/31/94	Increase	Decrease	
1995				
Companies consolidated by the global and proportional integration methods	8,168	23,349	(4,203)	27,314
Companies carried by the equity method	23,867	1,346	(930)	24,283
Total	32,035	24,695	(5,133)	51,597

e) Equity of the controlling company-

The detail of the capital and reserves of the controlling company as of December 31, 1996 and 1995, is as follows:

	Millions of Pesetas	
	1996	1995
Capital stock	469,735	469,735
Paid-in surplus	43,067	43,067
Restatement reserve	872,856	653,780
Legal reserve	86,071	75,453
Voluntary reserve	174,698	150,498
Retained earnings	112	147
Income for the year	120,414	106,183
Interim dividend	(32,881)	(28,184)
Total	1,734,072	1,470,679

The differences (amounting to Ptas. 4,464 million) between the restatement reserves in the individual financial statements of Telefónica and those in the consolidated financial statements arose in consolidation, as a result of the reclassifications to the voluntary reserves account of the reserves of the companies sold and to the consolidation reserve account of the reserves of existing companies.

Contribution of the Group companies to the consolidated accounts-

The contribution of the Group companies to consolidated equity as of December 31, 1996, was as follows:

Company	Millions of Pesetas			
	December 31, 1996			
	Contribution			
	To Consolidated Income	To Reserves	To Translation Differences	Total Contribution to Equity
Capital stock of the parent company	—	—	—	469,735
Cabitel	2,794	2,257	—	5,051
Fonditel	390	297	—	687
G. Casiopea	373	1,288	31	1,692
G. Comet	(34)	(848)	—	(882)
G. Servicio Teledistribución	(61)	309	—	248
G. Sintel (until 04/30/96)	710	(30)	—	680
G. Telecartera y Sociedad de Cablevisión	(804)	(82)	—	(886)
G. Telefónica Servicios Móviles	15,135	1,664	—	16,799
G. Telefónica Sistemas	674	2,261	—	2,935
G. Telefónica Internacional	22,445	66,067	34,800	123,312
Telefónica Publicidad e Información	3,611	3,041	—	6,652
Playa de Madrid	12	84	—	96
Taetel	325	1,129	—	1,454
Telefónica Servicios Multimedia	(210)	(131)	—	(341)
Telfisa	65	(107)	—	(42)
Telyco	848	(1,533)	—	(685)
Temasa	1,885	2,791	—	4,676
Tidsa	953	2,021	—	2,974
Urbana Ibérica	4	89	—	93
Telefónica de España	111,364	966,953	1,155	1,079,472
Total Telefónica Group	160,479	1,047,520	35,986	1,243,985
Restatement Royal Decree-Law 7/1996	—	219,076	—	219,076
Variation in income and reserves due to fixed asset transactions	(197)	(35,958)	—	(36,155)
Interim dividend	—	—	—	(32,881)
Contributions to equity of the Telefónica Group	160,282	1,230,638	35,986	1,863,760

The contribution of the Group companies to consolidated equity as of December 31, 1995, was as follows:

Company	Millions of Pesetas			
	December 31, 1995			
	Contribution			
	To Consolidated Income	To Reserves	To Translation Differences	Total Contribution to Equity
Capital stock of the parent company	—	—	—	469,735
Cabitel	2,622	1,435	—	4,057
Fonditel	354	11	—	365
G. Casiopea	453	868	82	1,403
G. Comet	(54)	(794)	—	(848)
G. Servicio Teledistribución	9	387	—	396
G. Sintel	(1,893)	2,016	(27)	96
G. Telecartera y Sociedad de Cablevisión	(36)	(84)	—	(120)
G. Telefónica Servicios Móviles	1,238	427	—	1,665
G. Telefónica Sistemas	552	1,670	—	2,222
G. Telefónica Internacional	22,526	43,480	21,923	87,929
Telefónica Publicidad e Información	2,736	2,698	—	5,434
Playa de Madrid	23	61	—	84
Taetel	422	1,309	—	1,731
Telefónica Servicios Multimedia	(127)	(4)	—	(131)
Telfisa	91	137	—	228
Telyco	147	(1,602)	—	(1,455)
Temasa	1,449	1,843	—	3,292
Tidsa	775	1,848	—	2,623
Telefónica Transmisión de Datos	37	—	—	37
Urbana Ibérica	8	82	—	90
Telefónica de España	103,391	928,394	—	1,031,785
Total Telefónica Group	134,723	984,182	21,978	1,140,883
Variation in income and reserves due to fixed asset transactions	(1,509)	(34,453)	—	(35,962)
Interim dividend	—	—	—	(28,184)
Contributions to equity of the Telefónica Group	133,214	949,729	21,978	1,546,472

12. MINORITY INTERESTS

Minority interests-

This caption relates to the holdings of minority stockholders in the equity and income/loss for the year of the Group companies consolidated by the global integration method.

As of December 31, 1996, the balance of this caption comprised the holdings of minority stockholders in the following companies:

Company	% of Minority Interests	Millions of Pesetas			
		Net Worth	Translation Differences	Income (Loss)	Balance at 12/31/96
C.T.C. Chile	56.38	91,955	12,107	21,052	125,114
Other Chilean companies	—	4,472	14	831	5,317
Telefónica del Perú	65.00	105,712	7,949	28,518	142,179
Negocios Cibernéticos	50.00	5	—	—	5
Mensatel	10.00	102	—	4	106
Publiguías	45.07	565	80	609	1,254
T.I. Telefónica Internacional	23.78	48,914	10,858	7,003	66,775
T.L.D. Puerto Rico	21.00	2,424	187	(268)	2,343
Telecartera (4)	25.00	135	—	(166)	(31)
T. Romania	40.00	572	58	307	937
T. Perú Holding	10.00	27,824	998	868	29,690
Other Peruvian companies	—	90	—	—	90
REM Infográfica	40.00	20	—	(63)	(43)
TMP Worldwide España	49.00	14	—	2	16
Radio Red Cataluña	9.00	11	—	(4)	7
Fonditel	19.00	539	—	92	631
S.G. Cablevisión Madrid (1)	12.25	12	—	(3)	9
S.G. Cablevisión Barcelona (1)	12.25	12	—	(11)	1
S.G. Cablevisión Cantabria (2)	12.25	12	—	(3)	9
S.G. Cablevisión Canarias (3)	49.00	105	—	(15)	90
S.G. Cablevisión Alicante	12.25	12	—	(1)	11
S.G. Cablevisión Asturias	12.25	12	—	1	13
S.G. Cablevisión Bizkaia	12.25	12	—	(3)	9
S.G. Cablevisión Burgos	23.50	24	—	(1)	23
S.G. Cablevisión Cádiz	12.25	13	—	(1)	12
S.G. Cablevisión Granada	12.25	13	—	—	13
S.G. Cablevisión León	12.25	13	—	—	13
S.G. Cablevisión Lleida	12.25	13	—	(2)	11
S.G. Cablevisión Málaga	12.25	13	—	—	13
S.G. Cablevisión Murcia	12.25	12	—	(1)	11
S.G. Cablevisión Navarra	12.25	12	—	(2)	10
S.G. Cablevisión Rioja	12.25	12	—	—	12
S.G. Cablevisión Sevilla	12.25	12	—	(2)	10
S.G. Cablevisión Valencia	12.25	12	—	(1)	11
S.G. Cablevisión Valladolid	12.25	12	—	—	12
S.G. Cablevisión Balears	12.25	12	—	(2)	10
Gestired	—	21	—	(21)	—
Servicios y Contenidos por la Red	—	39	—	(39)	—
Total		283,764	32,251	58,678	374,693

As of December 31, 1995, the balance of this caption comprised the holdings of minority stockholders in the following companies:

Company	% of Minority Interests	Millions of Pesetas			
		Net Worth	Translation Differences	Income (Loss)	Balance at 12/31/95
C.T.C. Chile	56.38	86,426	4,870	15,933	107,229
Telefónica del Perú	65.00	93,818	(3,827)	26,519	116,510
Gestired	49.00	24	—	10	34
Mensatel	10.00	97	—	5	102
Publiguías	45.07	509	(96)	482	895
Sintel Peru	37.00	53	—	82	135
Sintelar	25.00	431	(18)	(41)	372
Telefónica Internacional	23.78	42,105	6,798	7,011	55,914
T.L.D. Puerto Rico	21.00	2,254	177	(10)	2,421
Telecartera	24.88	247	—	(3)	244
T. Romania	40.00	300	96	175	571
T. Perú Holding	10.00	27,603	(56)	880	28,427
Cotronic	49.00	40	—	28	68
Incosa	48.90	55	—	39	94
Servicios y Contenidos por la Red	50.00	11	—	1	12
Tepesa	44.36	136	—	(25)	111
Rred. Zaragoza	9.00	17	—	(6)	11
Rred. Cataluña	9.00	17	—	(8)	9
Fonditel	19.00	433	—	67	500
S.G. Cablevisión Madrid	48.70	10	—	—	10
S.G. Cablevisión Barcelona	48.70	10	—	—	10
S.G. Cablevisión Cantabria	34.35	14	—	—	14
S.G. Cablevisión Canarias	39.99	60	—	—	60
Total		254,670	7,944	51,139	313,753

Variations in minority interests-

The variations in minority interests in 1995 and 1996 were as follows:

	Millions of Pesetas
Balance at December 31, 1994	292,293
Income for the year	51,139
Dividends distributed	(16,910)
Inclusion of companies	1,003
Exclusion of companies	—
Translation differences	(10,853)
Other variations	(2,919)
Balance at December 31, 1995	313,753
Income for the year	58,678
Dividends distributed	(25,496)
Inclusion of companies	4,722
Exclusion of companies	(873)
Translation differences	24,289
Other variations	(380)
Balance at December 31, 1996	374,693

13. DEFERRED REVENUES

The detail of the balances of and variations in this caption in the accompanying consolidated balance sheets is as follows:

	Millions of Pesetas			
	Capital Subsidies	Exchange Gains	Nonrefundable Third-Party Contributions and Other	Total
Balance at 12/31/94	60,136	8,684	6,209	75,029
Additions	18,513	10,477	939	29,929
Allocation to income	(7,983)	(5,381)	(336)	(13,700)
Balance at 12/31/95	70,666	13,780	6,812	91,258
Additions	13,485	(8,724)	4,352	9,113
Allocation to income	(10,317)	(2,067)	(501)	(12,885)
Balance at 12/31/96	73,834	2,989	10,663	87,486

Capital subsidies

The detail of the capital subsidies not yet allocated to income is as follows:

Grantor	Millions of Pesetas	
	12/31/96	12/31/95
From official agencies, autonomous community governments, regional and local governments and other	31,452	30,220
EU		
STAR Programme	14,223	16,952
FEDER Programme	6,570	7,243
IRTA Programme	2,000	2,322
FEDER 94/95 Programme	16,368	10,481
Other	3,221	3,448
	73,834	70,666

Exchange differences-

The amortization schedule for exchange gains is as follows:

1997	1998	1999	2000	2001	Subsequent Years	Total
3	—	—	1,361	1,625	—	2,989

14 PROVISIONS FOR CONTINGENCIES AND EXPENSES

The detail of the balances of and variations in provisions for contingencies and expenses is as follows:

	Millions of Pesetas								
	Balance at 12/31/94	Provisions	Amount Used	Other	Balance at 12/31/95	Provisions	Amount Used	Other	Balance at 12/31/96
Provision for cost of integrating employees in the social security system (Notes 4-k and 4-g)	62,198	—	(5,654)	(11,750)	44,794	—	(6,106)	—	38,688
Provision for Rebalancing Plan	4,344	4,486	(2,761)	—	6,069	4,677	(1,625)	—	9,121
Provision for supplementary pension payments (Notes 4-k and 9)	122,049	9,195	(14,938)	1,607	117,913	7,853	(14,328)	10,597	122,035
Group insurance (Note 4-k)	19,853	2,040	(5,344)	—	16,549	1,620	(4,950)	—	13,219
Provision for voluntary early retirement (Note 4-l)	22,500	46,452	(16,333)	—	52,619	58,519	(24,354)	—	86,784
Technical provisions (Note 4-m)	25,162	10,573	(512)	—	35,223	13,263	(18)	(30)	48,438
Claims	763	—	(197)	534	1,100	—	(160)	(563)	377
Other provisions	14,007	1,194	(2,202)	730	13,729	11,807	(6,790)	(793)	17,953
Total	270,876	73,940	(47,941)	(8,879)	287,996	97,739	(58,331)	9,211	336,615

Most of the provisions are explained in Note 4. The "Technical Provisions" account includes the provisions recorded by the Group companies engaging in the insurance business. The balancing items for these provisions are recorded under the "Short-Term Financial Investments" and "Long-Term Financial Investments" captions.

15. DEBENTURES, BONDS AND OTHER NEGOTIABLE INSTRUMENTS

The detail of the balances as of December 31, 1996 and 1995 of debentures, bonds and other negotiable instruments is as follows:

	CONSOLIDATED					
	Peseta Debentures and Bonds		Foreign Currency Debentures and Bonds		Corporate Promissory Notes	Total
	Nonconvertible	Convertible and/or Exchangeable	Nonconvertible	Convertible and/or Exchangeable		
Balance at 12/31/94	707,734	—	58,935	14,728	52,968	834,365
New issues	—	—	—	—	144,653	144,653
Redemptions, conversions and exchanges	(131,657)	—	(7,363)	(135)	(150,835)	(289,990)
Restatements and other variations	52,307	—	(634)	(1,040)	(1,560)	49,073
Balance at 12/31/95	628,384	—	50,938	13,553	45,226	738,101
New issues	—	—	50,809	1,087	168,774	220,670
Redemptions, conversions and exchanges	(61,206)	—	(18,670)	(1,094)	(150,955)	(231,925)
Restatements and other variations	(46,700)	—	4,519	1,124	7,623	59,966
Transfers	—	—	(278)	278	—	—
Balance at 12/31/96	613,878	—	87,318	14,948	70,668	786,812
Maturity:						
Long term	561,533	—	76,386	14,645	1,814	654,378
Short term	52,345	—	10,932	303	68,854	132,434
Unmatured accrued interest	12,967	—	2,026	—	—	14,993

Debentures and bonds-

The detail of the debentures and bonds outstanding as of December 31, 1996, and of the main features thereof is as follows:

Issue	Interest Rate (%)	Maturity					Subsequent Years	Total
		1997	1998	1999	2000	2001		
Debentures:								
Series B 1987	5.80	513	—	—	—	—	—	513
Series C 1987	5.75	1,521	—	—	—	—	—	1,521
Yankee Bonds 1987	7.63	—	—	—	—	—	26,255	26,255
Subscriber Series 1987	3.50	9	—	—	—	—	—	9
Series D 1989	5.80	3,077	3,077	1,539	—	—	—	7,693
July 1989	12.00	—	—	—	—	—	10,300	10,300
December 1989	5.72 (*)	800	800	800	—	—	—	2,400
January 1990	12.00	—	—	—	—	20	27,728	27,748
February 1990 Series A	12.60	—	—	—	9,350	—	—	9,350
February 1990 Series B	12.60	—	—	—	—	—	1,367	1,367
February 1990 Series C	12.60	—	—	—	—	—	626	626
February 1990 Series D	12.89	—	—	—	14,631	—	—	14,631
February 1990 Series E	12.85	—	—	—	—	—	4,768	4,768
February 1990 Series F	12.58	—	—	—	—	—	526	526
December 1990	13.58	—	—	—	—	—	42,989	42,989
Series E 1991	6.00	1,282	1,282	1,282	1,282	1,282	1,925	8,335
Series F 1991	6.00	293	293	293	293	293	4,250	5,715
February 1991 Series A	14.25	—	29,486	—	—	—	—	29,486
February 1991 Series B	14.47	—	65,197	—	—	—	—	65,197
March 1991	14.48	—	8,810	2,202	—	—	—	11,012
Private issue April 1991	14.25	—	20,000	—	—	—	—	20,000
April 1991 Series A	13.50	—	—	—	—	10,000	—	10,000
April 1991 Series B	13.67	—	—	—	—	41,558	—	41,558
Series G 1993	4.50	—	—	—	—	—	14,645	14,645
Series H 1994	5.80	—	—	1,026	2,052	2,052	11,285	16,415
Series I 1994	5.50	—	—	—	256	513	7,438	8,207
C September 1998	10.12	—	41,881	—	—	—	—	41,881
D September 2001	10.25	—	—	—	—	56,612	—	56,612
B November 2000	10.06	—	—	—	20,439	—	—	20,439
C November 2002	10.06	—	—	—	—	—	19,315	19,315
B October 2000	8.00	—	—	—	12,372	—	—	12,372
C October 2004	8.25	—	—	—	—	—	11,520	11,520
		7,495	170,826	7,142	60,675	112,330	184,937	543,405

Issue	Currency	Interest Rate	Maturity	Subsequent			Years	Total
			1997	1998	1999	2000		
			7,495	170,826	7,142	60,675	112,330	184,937
Bonds:								543,405
November 1990	Pesetas	14.06	600	—	—	—	—	600
November 1990	Pesetas	6.76	400	—	—	—	—	400
January 1991	Pesetas	6.76 (*)	1,370	—	—	—	—	1,370
February 1991	Pesetas	13.94	3,440	—	—	—	—	3,440
February 1991	Pesetas	6.76 (*)	400	—	—	—	—	400
April 1991	Pesetas	14.51	—	—	100,894	—	—	100,894
April 1991	Pesetas	12.37	10,160	—	—	—	—	10,160
April 1991	Pesetas	7.65 (*)	300	—	—	—	—	300
May 1991	Pesetas	12.37	4,437	—	—	—	—	4,437
July 1991	Pesetas	6.76 (*)	5,100	—	—	—	—	5,100
July 1991	Pesetas	14.51	—	—	7,342	—	—	7,342
February 1992	Pesetas	11.18	1,470	—	—	—	—	1,470
November 1992	Pesetas	12.94	400	—	—	—	—	400
April 1993	Pesetas	12.25	21,000	—	—	—	—	21,000
May 1993	Pesetas	11.75	2,468	—	—	—	—	2,468
Series A 1996	New sols	15.00	4,540	—	—	—	—	4,540
Series G 1996	New sols	PBU+5.1%	—	—	3,655	—	—	3,655
Series I 1996	New sols	PBU+5.6%	—	—	—	—	4,763	4,763
Total issues			63,580	170,826	119,033	60,675	117,093	716,144

(*) Average interest rate for 1996 on floating-rate issues.

The zero-coupon debentures and bonds are recorded in the consolidated balance sheet at their issue value plus the accrued interest through December 31, 1996.

The detail of the maturities and redemption values as of December 31, 1996, is as follows:

Issue	Maturity Date	%	Millions of Pesetas	
			Current Value	Redemption Value
Debentures:				
February 1990 Series D	02/26/2000	336.154	14,631	21,447
February 1990 Series E	02/26/2005	613.338	4,768	12,776
February 1990 Series F	02/26/2010	1,069.470	526	2,503
December 1990	12/28/2005	675.000	42,989	135,000
February 1991 Series B	02/28/1998	257.500	65,197	76,488
March 1991	03/01/1998	257.729	2,203	2,577
March 1991	06/01/1998	266.659	2,203	2,667
March 1991	09/01/1998	275.899	2,202	2,759
March 1991	12/01/1998	285.353	2,202	2,854
March 1991	03/01/1999	295.022	2,202	2,950
April 1991 Series B	04/17/2001	360.000	41,558	72,000
C September 1998	09/19/1998	196.531	41,881	49,401
D September 2001	09/19/2001	265.543	56,612	89,687
Bonds:				
April 1991	04/15/1999	295.740	100,894	137,519
July 1991	07/15/1999	295.740	7,342	10,351
			387,410	620,979

As of December 31, 1996, the redemption value amounted to Ptas. 620,979 million and the current value to Ptas. 387,410 million.

Corporate promissory notes

There are two corporate promissory note issue programs at Telefónica, as follows:

Millions of Pesetas			
Balance Limit	Addressed to	Pesetas Par Value	Method of Acquisition
75,000	Public	500,000	Monthly competitive auctions
	Companies and institutions	100 million	Monthly competitive auctions
75,000	Companies and institutions	500 million (minimum)	Specific transactions

Payables for negotiable instruments

Other payables for negotiable instruments denominated in foreign currencies relate to corporate promissory notes issued by Telefónica North America Inc. and underwritten by Telefónica. The average interest rates were 5.45% in 1996 and 5.97% in 1995.

EMTN Program

On November 12, 1996, a Euro Medium-Term Notes program was arranged on the EMTN market for successive issues over time of conventional or structured debt securities, issued in a continuous or discretionary manner; denominated in a broad range of currencies, and with widely varying maturities, for up to a maximum amount of US\$ 1.5 billion. The issuer is Telefónica Europe, B.V., a subsidiary set up for this purpose in The Netherlands. Telefónica de España, S.A. is the guarantor. As of December 31, 1996, no issues had been made under this program.

16 PAYABLE TO CREDIT ENTITIES

The detail of accounts payable to credit entities is as follows:

	Millions of Pesetas							
	Average Interest Rate		Balance at 12/31/96			Balance at 12/31/95		
	1996	1995	Short Term	Long Term	Total	Short Term	Long Term	Total
Corporate promissory notes	13.37	13.37	365	36,855	37,220	15,365	37,220	52,585
Loans and credits	8.71	9.97	59,594	249,906	309,500	77,794	325,264	403,058
Foreign currency loans	6.54	7.08	174,177	556,588	730,765	57,946	539,401	597,347
Total			234,136	843,349	1,077,485	151,105	901,885	1,052,990

As of December 31, 1996, the payables were scheduled to mature as follows:

	Millions of Pesetas						
	1997	1998	1999	2000	2001	Subsequent Years	Total
Corporate promissory notes	365	1,314	21,637	1,618	12,286	—	37,220
Loans and credits	59,594	52,288	60,390	49,784	53,397	34,047	309,500
Foreign currency loans	174,177	112,286	112,974	110,250	107,054	114,024	730,765
Total	234,136	165,888	195,001	161,652	172,737	148,071	1,077,485

Loans and credits

The peseta loans and credits include the amount used in pesetas of a multicurrency loan originally granted in ECUs by the European Investment Bank for Ptas. 12,750 million and three swap transactions with the following entities:

- Union Bank of Switzerland and J.P. Morgan relating to the EIB-Telfisa loan of 120,000 million lire, swapped for Ptas. 8,926 million.
- Citibank and J.P. Morgan relating to the EIB-Telfisa loan of 17,000 yen, swapped for Ptas. 23,074 million.
- Union Bank of Switzerland and J.P. Morgan relating to the EIB-Telfisa loan of 65,000 ECUs, swapped for Ptas. 10,575.5 million.
- There are several exchange rate hedging contracts instrumented in swaps at Telefónica Internacional covering loans amounting to US\$ 410 million, the equivalent peseta value of which was set at Ptas. 49,826 million.

Foreign currency loans

The detail of the foreign-currency loans as of December 31, 1996 and 1995, and of the main features thereof is as follows:

Entity	Year	Currency	Maturity	Outstanding Principal					
				Interest Rate		Foreign Currency		Pesetas	
				1996	1995	12/31/96	12/31/95	12/31/96	12/31/95
Telefónica—									
1st ICO—EIB	1988	ECUs	2003	6.15	6.15	106	122	17,347	18,961
1st ICO—EIB	1988	FRF	2003	5.90	5.90	455	520	11,379	12,896
1st ICO—EIB	1988	CHF	2003	4.30	4.30	75	86	7,258	9,014
3rd ICO—EIB	1989	ECUs	2004	7.85	7.85	240	270	39,075	42,043
4th ICO—EIB	1989	DM	2004	6.70	6.70	164	185	13,872	15,681
5th ICO—EIB	1990	ECUs	2005	10.20	10.20	127	142	20,729	22,158
5th ICO—EIB	1990	CHF	2005	7.65	7.65	229	256	22,231	27,002
5th ICO—EIB	1990	NLG	2005	8.80	8.80	98	109	7,356	8,284
4th ICO—EIB	1990	YEN	2005	7.45	7.45	7,668	8,570	8,693	10,095
7th ICO—EIB	1992	ECUs	2007	5.32	6.63	150	150	24,422	23,358
9th ICO—EIB	1992	NLG	2002	3.37	5.09	82	82	6,172	6,219
8th ICO—EIB	1992	YEN	2002	0.77	1.90	19,500	19,500	22,109	22,970
S.B. GRAL. LEASING	1987	YEN	2000	3.11	4.25	6,364	8,182	7,215	9,638
Commercial paper	1986	USD	1996	5.30	5.90	—	145	—	17,622
Credit facility	1995	USD	1996	—	5.61	—	5	—	606
Telfisa—									
EIB	1991	ECUs	2006	6.37	6.33	237	250	49,251	38,929
EIB	1991	NLG	2006	4.20	4.78	137	144	10,312	10,938
EIB	1991	FRF	2006	5.90	6.99	414	435	10,348	10,801
EIB	1991	USD	2006	6.29	5.80	134	141	17,652	17,184
EIB	1995	LIRA	2000	—	—	120,000	120,000	10,303	9,203
EIB	1995	YEN	1999	—	—	17,000	17,000	19,274	20,026
Telefónica Internacional—									
Syndicated	1994	USD	2001	5.95	6.82	690	690	90,579	83,773
CTC (**)	(**)	(**)	(**)	6.17-9.6	5.69-9.65	(**)	(**)	144,356	102,208
ABN Amro Bank	1996	USD	1997	5.66	—	42	—	5,514	-
Other	(**)	(**)	(**)	(**)	(**)	(**)	(**)	165,318	57,738
								730,765	597,347

(*) Since this item relates to several loans, the range of interest rates applicable is indicated.

(**) This item relates to several loans in different currencies and, therefore, the year granted, currency, interest rate and year of maturity are not indicated.

Described below are the main foreign currency loans:

ICO-EIB-

In 1988 Telefónica obtained from the European Investment Bank (EIB) a financing commitment for capital expenditure projects aimed at improving infrastructures and new technologies. This financing is obtained through Instituto de Crédito Oficial (ICO).

At the same time, a 15-year multicurrency loan was arranged, originally for ECU 1,200 million (1st to 5th ICO-EIB tranches), which has been drawn down by Telefónica in six different currencies, has a five-year grace period and is repayable in 20 semiannual installments. The loan bears fixed interest in the first five years and is subsequently renegotiable for five-year periods.

In 1992 a new multicurrency loan was arranged for ECUs 150 million, NLG 82 million and ¥ 19,500 million (7th to 9th ICO-EIB tranches), for the same purpose and under the same repayment terms as those described above. The loan bears interest at three-month Libor less 0.75% for the drawdowns in ECUs and Dutch guilders, and at six-month Libor plus 0.175% for the drawdowns in yen.

Commercial paper-

In 1996 Telefónica arranged a multiple financial transaction for the issue of Euronotes maturing in under six months, with Chase Manhattan Bank as the agent bank, for a total amount of US\$ 250 million. The Euronotes matured and the securities redeemed in 1996.

In order to attract funds in the U.S. market, Telefónica formed the subsidiary Telefónica North America, which in 1987 executed a commercial paper issue program with maturities in under nine months for a maximum amount of US\$ 125 million. The banks backing the program are Fuji Bank Ltd., Mitsubishi Bank Ltd., Mitsui Bank Ltd., Sumitomo Bank Ltd. and Tokyo Trust and Banking Co. Ltd. in equal proportions. The program matures in 1997.

EIB (Telfisa)-

In 1991 Telefonía y Finanzas, S.A. (Telfisa) obtained a 15-year multicurrency loan from the EIB for ECU 600 million, drawn down in four different currencies, with a grace period of five years, repayable in 20 semiannual installments and with floating interest negotiated on a quarterly basis with the EIB.

Syndicated loan (Telefónica Internacional)-

A long-term syndicated loan for US\$ 1,100 million was arranged on December 30, 1994. ABN Amro Bank NV and Banco de Negocios Argentaria acted as lead-managers. The loan is repayable in seven years, with a three-year grace period. The interest periods may be one, three or six months, at the Company's discretion, and the applicable interest rate is Libor for the chosen period plus 0.275%.

ABN Amro Bank (CTC)-

In May 1995 CTC arranged a syndicated loan of US\$ 275 million with a group of banks headed by ABN Amro Bank. The outstanding balance as of December 31, 1996, was Ptas. 36,257 million, of which Ptas. 36,100 million are repayable at long-term.

Credit available-

The loans and credits accounts reflect only the amounts drawn against the credit facilities. The undrawn credit facility funds available were as follows:

	Millions of Pesetas	
	Balance at 12/31/96	Balance at 12/31/95
Credit available at long term	253,848	183,041
Other credit facilities (floating policies)	76,000	88,000
Credit available at short term	140,665	63,635
Total	470,513	334,676

17. DERIVATIVES

The existing positions have been hedged in order to obtain savings on the underlying rates by switching from fixed rates to variable rates. In view of the steady decline in interest rates, transactions generating gains were canceled so as to mitigate interest expenses. Exchange rate insurance has been taken out and swaps to pesetas have been made to provide protection from exchange risk in anticipation of possible exchange rate instability arising in the process of Monetary Union.

As of December 31, 1996, the total outstanding volume of hedging transactions was Ptas. 140,240 million (Ptas. 187,174 million in 1995), and a positive allocation of Ptas. 1,041 million was recorded for accounting purposes in the year (Ptas. 8,679 million in 1995).

The detail, by type of derivative, of the (notional) contractual values of the derivatives held by the Group as of December 31, 1996, is as follows:

Type of Risk Hedged	Millions of Pesetas	
	Notional Value	Currency Value
Interest rate risk:		
Interest rate swaps	47,839	—
Exchange rate risk:		
Currency swaps	8,926	120,000 Lire
	23,074	17,000 Yen
	10,575	65 ECUs
	49,826	410 US\$

The detail, by maturity, of the interest rate swaps and of the interest rates applied is as follows:

Underlying Transactions	Millions of Pesetas						Floating to Fixed
	Amount	Up to 1 Year	1 to 3 Years	3 to 5 Years	Over 5 Years	Fixed to Floating	
Debentures and bonds	88,035	31,160	23,074	33,801	—	88,035	—
Peseta loans	2,379	285	644	771	679	2,379	—
Foreign currency loans	49,826	15,106	34,720	—	—	49,826	—
	140,240	46,551	58,438	34,572	679	140,240	—

18. TAX MATTERS

Since 1990 Telefónica has filed consolidated tax returns with certain Group companies. 33 companies formed the tax consolidation group in 1996, including most notably, in terms of sales, Telefónica de España, S.A., Telefónica Servicios Móviles, S.A., Cabitel, S.A., Telefónica Publicidad e Información, S.A. and Telefónica Sistemas, S.A.

Deferred and prepaid taxes-

The detail as of December 31, 1996 and 1995, of the Telefónica Group's prepaid and deferred taxes, and of the variations therein in the years then ended, is as follows:

	Millions of Pesetas			
	Prepaid Taxes		Deferred Taxes	
	Short Term	Long Term	Short Term	Long Term
Balance at December 31, 1994	728	31,230	—	74,447
Reversal	—	(500)	—	(8,290)
Arising in the year	133	19,677	—	5,500
Other	9	(71)	—	(644)
Balance at December 31, 1995	870	50,336	—	71,013
Reversal	(209)	(2,354)	—	(13,010)
Arising in the year	4,747	22,147	—	26,392
Exclusion of companies and other	69	(122)	—	(652)
Balance at December 31, 1996	5,477	70,007	—	83,743

The prepaid taxes recorded by the Company relate mainly to early retirements and provisions for supplementary pension payments to retired employees. The deferred taxes recorded relate mainly to timing differences for accelerated depreciation.

Accrued taxes payable and tax receivables-

The detail of the "Accrued Taxes Payable" and "Tax Receivables" captions as of December 31, 1996 and 1995, is as follows:

	Millions of Pesetas	
	Balance at 12/31/96	Balance at 12/31/95
Accrued taxes payable:		
Personal income tax withholdings	10,142	9,560
VAT and Canary Islands general indirect tax payable	—	10,230
Withholdings from income from movable capital and other	2,085	2,351
Corporate income tax	36,817	38,194
Single tax on restatement Royal Decree-Law 7/1996	6,776	—
Local taxes	6,633	1,499
Accrued social security taxes	24,797	24,494
Foreign taxes	16,917	14,217
Total	104,167	100,545
Tax receivables:		
Corporate income tax prepayments		
Withholdings at source from income from movable capital	2,547	2,186
Prepayments on consolidated income tax returns	16,514	14,241
Prepayments on individual income tax returns	71	5
Taxes, surcharges and other payments recoverable	529	557
Prepaid taxes	5,477	870
VAT and Canary Islands general indirect tax receivable	8,912	—
VAT deductible	9,224	3,990
Foreign taxes	10,565	3,331
Total	53,839	25,180

Reconciliation of consolidated income per books to consolidated taxable income-

	Millions of Pesetas	
	1996	1995
Consolidated income per books	275,881	223,711
Permanent differences	(102,081)	(95,856)
Timing differences:		
Arising in the year	68,288	40,504
Arising in prior years	22,364	22,258
Taxable income	264,452	190,617

The adjustments for permanent differences relate mainly to income earned by subsidiaries taxed abroad, income relating to certain companies and amortization of goodwill in consolidation.

The variations in timing differences in 1996 were as follows:

	Millions of Pesetas	
	Increase	Decrease
Voluntary early retirement	44,310	596
Provisions for supplementary pension payments to retired employees	2,633	—
Pension fund	3,052	—
Allowance for bad debts	18,299	—
Unrealized gains on transactions involving fixed assets	—	6,467
Other	8,539	1,482
Timing differences arising in the year	76,833	8,545
Reversal of accelerated depreciation taken in prior years	25,080	—
Provision for diminution in value of securities portfolio in 1995	—	413
Exchange differences	—	5,192
Unrealized gains on transactions involving fixed assets	3,578	—
Other	135	824
Timing differences arising in prior years	28,793	6,429

Calculation of corporate income tax expense and net corporate income tax payable-

The corporate income tax expense and the net corporate income tax payable in 1996 and 1995 were as follows:

	Millions of Pesetas	
	1996	1995
Consolidated income	275,881	223,711
Permanent differences	(102,081)	(95,856)
Adjusted income per books	173,800	127,855
Gross tax at 35%	60,830	44,749
Tax credits and relief	(34,759)	(28,522)
Corporate income tax expense	26,071	16,227
Deferred revenues and other	(21,643)	-
Tax effect of timing differences	32,389	21,967
Corporate income tax payable	36,817	38,194
Spanish corporate income tax expense	26,071	16,227
Tax accrual	(267)	367
Accrued foreign taxes	31,117	22,764
Total corporate income tax and similar taxes	56,921	39,358

Ptas. 55,755 million and Ptas. 30,909 million of tax credits and tax relief were taken in 1996 and 1995, respectively. In view of the limits applicable to investment tax credits, as of December 31, 1996, after deducting the tax credits taken in 1996, the Telefónica Group has Ptas. 67,725 million of tax credits available from prior years, as follows:

Year	Millions of Pesetas					Total
	1992	1993	1994	1995	1996	
Amount	19,214	19,047	—	19,128	10,336	67,725

The years open for review by the tax inspection authorities for the main applicable taxes vary from one consolidated company to another, although they are generally all years since 1993.

19. OTHER NONTRADE PAYABLES

The detail of the balances of this caption in the consolidated balance sheets as of December 31, 1996 and 1995, is as follows:

	Millions of Pesetas	
	Balance at 12/31/96	Balance at 12/31/95
Accrued expenses payable	31,261	35,061
Dividends payable	39,327	28,224
Provision for extra-payroll	23,440	22,761
Exchange of telephone service with other operators	13,168	11,034
Guarantees and deposits	11,291	10,076
Provision for third-party liability	18,245	7,978
Other accounts payable	23,305	45,092
Total	160,037	160,226

20. REVENUES AND EXPENSES

Sales and services-

The detail, by business line, of net sales and services is as follows:

	Millions of Pesetas	
	1996	1995
Basic telephony-		
Basic telephone service	947,748	843,748
Rental of circuits	73,317	29,809
Ibercom	69,290	58,517
Digital exchanges, intelligent network, ISDN and other	49,898	19,493
Terminals	71,696	75,983
Directories	11,547	15,435
	1,223,496	1,042,985
International communications	136,124	145,222
Public telephony	64,655	65,452
Data transmission	44,645	38,642
Mobile telephony	—	76,494
Other revenues (*)	4,125	3,879
Total revenues of Telefónica	1,473,045	1,372,674
Telefónica Internacional	331,598	281,050
Telefónica Servicios Móviles	256,384	35,028
Other subsidiaries	252,354	212,927
Group revenues before intercompany sales	2,313,381	1,901,679
Intercompany sales	(307,323)	(161,122)
Total revenues from Group operations	2,006,058	1,740,557

(*) Including Publicidad e Información and Multimedia.

Personnel expenses-

The detail of personnel expenses is as follows:

	Millions of Pesetas	
	1996	1995
Compensation	413,668	412,651
Provisions to the pension allowance and other commitments to employees	22,823	22,751
Employee welfare expenses and other	118,191	108,145
	554,682	543,547

Average number of employees-

Professional Category	1996	1995
General management	1,694	1,590
University graduates and special technicians	5,255	5,532
Junior college graduates and technicians	12,911	12,075
Internal plant supervisors and operators	17,051	17,605
External plant supervisors and operators	18,552	19,302
Applications operators and data processing assistants	713	750
Clerical staff	22,294	26,252
Subscriber service personnel	3,289	3,426
Operations personnel	5,696	5,816
Warehouse, office and garage personnel	1,640	1,691
Messengers, etc.	928	1,038
Manual workers	970	3,164
Other	1,155	962
Total	92,148	99,203

Interest expenses-

The detail of the "Interest Expenses" account is as follows:

	Millions of Pesetas	
	1996	1995
Debentures, bonds and other negotiable instruments	81,361	85,879
Promissory notes	3,946	4,373
Loans and credits	33,124	32,815
Foreign currency loans	45,017	43,861
Other	18,197	33,520
	181,645	200,448

Exchange differences-

The detail of exchange losses charged to income is as follows:

	Millions of Pesetas	
	1996	1995
Write-off of potential losses maturing in 1998 and subsequent years (Note 4-j)	7,431	16,545
Repayment of loans	6,827	7,114
Deferred losses per Ministerial Order dated 3/12/93 (Note 4-j)	4,226	(6,300)
Operating transactions	1,968	1,829
	20,452	19,188

Extraordinary revenues-

The detail of extraordinary revenues is as follows:

	Millions of Pesetas	
	1996	1995
Prior years' revenues	2,077	1,182
Indemnity payments for breach of contract	1,063	1,121
Amortization of exchange rate insurance premium	—	636
Consortium for compensation of insurance	934	507
Gain on sale of shares	—	469
Share in EURESCOM	67	419
Other	5,000	5,092
	9,141	9,426

Extraordinary expenses-

	Millions of Pesetas	
	1996	1995
Supplementary pension payments to retired employees (Note 4-k)	9,109	8,455
Court-ordered indemnity payments	—	4,708
Provisions recorded:		
Cost of inclusion of retired employees in social security system	3,676	4,035
Voluntary early retirement and early retirement indemnities	58,519	54,798
Other	13,707	—
Compensation for transfers	897	1,198
Subsidies and voluntary donations	882	879
PRI Program	4,444	—
Sundry	7,336	3,608
	98,570	77,681

Losses on fixed assets-

This caption includes Ptas. 47,918 million in 1996 and Ptas. 56,210 million in 1995 recorded as a result of the dismantling of Telefónica's network digitalization plant.

Management contract with Telefónica de Argentina, S.A.-

In November 1990, Telefónica de España, S.A. and Telefónica Argentina, S.A. entered into a management contract expiring in 2003 regulating the counseling services rendered by Telefónica de España, S.A. and the price thereof. The revenues received in this connection, net of the payments for third-party counseling, amounted to Ptas. 8,296 million in 1996 and Ptas. 8,403 million in 1995.

21. DIRECTORS' REMUNERATION AND OTHER BENEFITS

In 1996 and 1995 the compensation paid to Telefónica de España, S.A. Board members, together with pension and alternative system obligations to directors, amounted to Ptas. 278 million and Ptas. 147 million, respectively.

In 1996, Telefónica de España, S.A. granted no loans or credits to its directors.

22. OTHER INFORMATION

a) Sundry commitments and rights-

	Millions of Pesetas	
	1996	1995
Financial transaction guarantees	84,434	94,603
Guarantees provided for employees	219	2,253

The "Financial Transaction Guarantees" caption includes mainly the guarantees provided by Telefónica for its subsidiaries and investees through bank guarantees of their transactions with third parties.

b) Put option on Telefónica Perú Holding, S.A.-

Telefónica Internacional arranged a put option whereby it undertook, within three years from the original sale (i.e. by November 8, 1997), to repurchase from the current owners the 10% of Telefónica Perú Holding, S.A. that had previously been sold to them by Telefónica Internacional in 1994 if the owners exercise the sale option.

If the put option is exercised, the option exercise price which Telefónica Internacional undertakes to pay for the shares will be the difference between:

1. The acquisition price of the shares capitalized at a market interest rate,
2. Less any cash flows collected by the purchaser for maintenance of the investment and for participation in the know-how transfer and management contract, capitalized at the same interest rate.

c) Litigation between CTC and Entel Chile-

On January 15, 1996, Compañía de Telecomunicaciones de Chile, S.A. (CTC) and Empresa Nacional de Telecomunicaciones, S.A. (Entel Chile) entered into an agreement with respect to all the outstanding litigation from previous years between the companies that was before the courts and administrative agencies, whereby CTC was claiming approximately Ptas. 21,000 million. Under this agreement, the parties waived all the claims and proceedings between them and, accordingly, no claim was outstanding at the date of signature of the aforementioned agreement. The effect of this contract on the 1995 income attributable to Telefónica Internacional was Ptas. 325 million.

d) Put option on CRT shares-

Telefónica Internacional entered into a put option contract with RBS, a Brazilian partner in the consortium to which the shares of CRT were awarded. Under this contract, Telefónica Internacional undertakes to buy 10% of the shares of the consortium or of such investor company as may replace it, owned by RBS. This option will be exercisable on December 27, 2001, depending on whether or not RBS has fulfilled certain financial obligations. The price will be the initial acquisition price of the shares. If a loss arises as a result of the difference between the option exercise price and the market price of the shares at the time of sale, RBS must compensate Telefónica Internacional by means of shares of the consortium (or of such company as may replace it) owned by RBS. If, on the contrary, a capital gain should arise, it would correspond to RBS.

RBS also holds a purchase option on 17% of the shares of the consortium (or of such company as may replace it) owned by Telefónica Internacional. The exercise of this option, if appropriate, will take place on the 1,097th day from the date of acquisition of the shares of CRT. Until the date of the possible exercise of the option, the voting rights on these shares are held by RBS. If the option is not exercised on the date stipulated for exercise, the aforementioned voting rights will automatically be assigned to Telefónica Internacional. The price of the above-mentioned option will be the initial acquisition price, capitalized at three-year LIBOR plus 40 basis points.

e) Litigation in progress-

There is litigation against certain Telefónica Group operators for disconnection of entertainment lines and certain competition-related and other matters. This litigation is at the processing or appeal stage. The companies' legal advisers consider that the outcome of this litigation will not lead to material liabilities.

23. SUBSEQUENT EVENTS

a) Acquisition of shares of Telefónica Internacional-

Telefónica is negotiating with the State Property Agency the acquisition of the latter's 23.78% holding in Telefónica Internacional. To date, no final agreement has been reached on the transaction price or on when the acquisition will be made.

b) Public share purchase offer-

Under the public share purchase offer for Telefónica de España, S.A. shares made by Sociedad Estatal de Participaciones Patrimoniales SEPPA, which concluded on February 17, 1997, 20.3% of the Company's capital stock was placed with private investors. The remainder of the State's holding is guaranteeing payment of the premiums included in the public share purchase offer.

The government reserves certain rights of veto provided for in the Privatization Law in connection with strategic decision-making by Telefónica.

c) Digital platform-

Distribuidora de Televisión Digital, S.A., in which Telefónica has a 35% holding, was incorporated on January 24, 1997, and groups together various Spanish and foreign media companies. The new company will start to provide satellite television services through Hispasat from the first half of 1997, before any cable television companies commence operations. The company's capital stock amounts to Ptas. 10,000 million.

The Company expects the investments required for the launching and development of the project to be made over ten years, and that the annual amounts earmarked for it will not be significant.

(24) 1996 AND 1995 STATEMENTS OF CHANGES IN FINANCIAL POSITION

Application of funds	Millions of Pesetas		Source of funds	Millions of Pesetas	
	1996	1995		1996	1995
Funds applied in operations	—	—	Funds from operations	948,690	853,230
Start-up and debt arrangement expenses	4,581	1,598	Contributions from shareholders-		
Fixed asset additions-			Capital increases	—	—
Intangible assets	45,382	38,702	Paid-in surplus	—	—
Property and equipment	678,871	594,191	Minority interests	4,722	852
Long-term financial investments	142,944	30,958	Deferred revenues	17,837	19,452
Restatement reserve	6,776	—	Long-term deferred taxes	5,032	-
Dividends	101,593	107,099	Long-term debt	188,469	132,758
Repayment or transfer of long-term debt	316,587	267,615	Fixed asset disposals-		
Provisions	58,331	47,941	Intangible assets	—	—
Other funds applied	7,398	11,750	Property and equipment	13,076	17,247
Decrease in working capital due to acquisition			Long-term financial investments	36,053	21,580
of shareholdings	(1,474)	129	Deferred provisions and expenses	—	423
Variation in working capital due to translation			Variation in working capital due to disposal of		
differences	(924)	7,446	shareholdings	(11,000)	44
			Increase in working capital due to inclusion		
			of subsidiaries	—	—
Total funds applied	1,360,065	1,107,429	Total funds obtained	1,202,879	1,045,586
Funds obtained in excess			Funds applied in excess		
of funds applied			of funds obtained		
(Increase in working capital)	—	—	(decrease in working capital)	157,186	61,843
Total	1,360,065	1,107,429	Total	1,360,065	1,107,429

VARIATION IN WORKING CAPITAL	Millions of Pesetas			
	1996		1995	
	Increase	Decrease	Increase	Decrease
Due from stockholders for capital calls	—	4	4	—
Inventories	4,798	—	3,674	—
Accounts receivable	106,816	—	29,039	—
Accounts payable	—	245,611	—	85,385
Short-term financial investments	—	32,404	—	4,819
Cash	714	—	—	6,008
Accrual accounts	8,505	—	1,652	—
Total	120,883	278,019	34,369	96,212
Variation in working capital	157,186	—	61,843	—
Total	278,019	278,019	96,212	96,212

The reconciliation of the balances in the statements of income to the funds obtained from operations is as follows:

	Millions of Pesetas	
	1996	1995
Income	160,282	133,214
Income attributed to minority interests	58,678	51,139
Income (loss) attributable to associated companies	(7,811)	(8,754)
	211,149	175,599
ADD-		
Dividends at companies carried by the equity method	5,550	6,766
Depreciation and amortization	526,229	501,480
Amortization of debt arrangement expenses	3,603	3,317
Amortization of goodwill in consolidation	16,786	6,985
Provision for diminution in value of financial investments	911	(9)
Exchange differences	1,416	7,834
Undepreciated plant dismantled	47,918	56,210
Provision for inventory adjustment	2,496	2,598
Other provisions	97,739	74,220
Deferred interest	55,987	60,979
Amortization of COOB 92 and EXPO 92 expenses	12	33
Property, plant and equipment and intangible assets	5,707	1,611
Financial provision and supplementary pension payments to retired employees	9,109	8,455
Loss on disposal of consolidated companies	2,609	—
LESS-		
Gain on disposal of financial investments	73	3,926
Gain on disposal of property and equipment	10,435	12,293
Capital subsidies	10,317	7,983
Deferred taxes and long-term advances	7,935	20,926
Gain on disposal of consolidated companies	10,335	7,287
Other	(564)	433
Funds from operations	948,690	853,230

The funds used for acquisition or disposal of holdings were as follows:

Effect on Working Capital	Millions of Pesetas			
	12/31/96		12/31/95	
	Acquisitions	Disposals	Acquisitions	Disposals
Financial investments and change in consolidation method	(5,155)	5,852	(183)	—
Due from stockholders for uncalled capital	—	(198)	—	—
Start-up expenses	—	(67)	—	—
Intangible assets	—	(129)	—	—
Property and equipment	3,484	(2,824)	62	—
Financial investments	225	(3,096)	250	—
Deferred charges	—	(121)	—	—
Capital increase	—	(3,000)	—	—
Prepaid taxes	—	(121)	—	—
Minority interests	—	1,243	—	—
Deferred revenues	—	4	—	—
Income for the year through date of sale	—	(903)	—	—
Provisions	—	1,520	—	—
Long-term debt	(28)	8,542	—	—
Loss on disposal of holdings	—	2,843	—	—
Deferred taxes	—	1,455	—	—
Working capital	(1,474)	11,000	129	—
Price of acquisition or disposal of holdings	5,155	5,852	3	—

(25) EXPLANATION ADDED FOR TRANSLATION TO ENGLISH

These consolidated financial statements are presented on the basis of accounting principles generally accepted in Spain. Certain accounting practices applied by the Group that conform with generally accepted accounting principles in Spain may not conform with generally accepted accounting principles in other countries.

EXHIBIT I

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1996

Group companies and their holdings	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
Cabinas Telefónicas, S.A. (CABITEL) (*) (**) (1) Installation of public telephones Plaza de Carlos Trias Bertrán 7, 28020 Madrid	100.00%	—	100.00%	200	2,257	2,795	201	G.I.	—
Casiopea Reaseguradora, S.A. (3) Reinsurance Immeuble "Centre Europe" 5 Place de la Gare L-1616 Luxembourg	100.00%	—	100.00%	498	88	—	498	G.I.	—
Pléyade Peninsular, Compañía de Seguros de Telefónica, S.A. (3) Distribution, promotion or preparation of insurance contracts, operating as a broker Avenida General Perón 38, 28020 Madrid	16.67%	83.33%	100.00%	60	150	146	60	G.I.	—
Seguros de Vida y Pensiones Antares, S.A. (3) Life insurance and pensions Avenida General Perón 38, 28020 Madrid	21.33%	78.67%	100.00%	1,500	1,001	397	1,960	G.I.	—
Fonditel Entidad Gestora de Fondos de Pensiones, S.A. (3) Other holdings	N/A	3.78%	—	—	—	—	—	—	—
Compañía Española de Tecnología, S.A. (COMET) (**) (3) Promotion of business initiatives and holding of securities Villanueva 2 Duplicado planta 1ª, 28001 Madrid	100.00%	—	100.00%	1,049	(215)	(34)	1,682	G.I.	—
Satel, S.A. (5) Comandante Zarita 4, 28020 Madrid	—	85.00%	85.00%	125	N/D	N/D	81	I.	81
Clean, S.A. Property development Villanueva, 2 duplicado planta 1ª 28001 Madrid	50.00%	50.00%	—	1,370	(57)	5	685	Pl.	—
Barcelona Tecnología, S.A. Venture capital company c/50-25, 27 Sector A Polígono Industrial Zona Franca, 08040 Barcelona	—	4.21%	4.21%	238	N/D	N/D	10	I.	10
Catalana D'Iniciatives, C.R., S.A.	—	1.26%	—	—	—	—	—	—	—
Fonditel Entidad Gestora de Fondos de Pensiones, S.A. (3) Pension fund management Pedro Teixeira 8, 28020 Madrid	77.22%	3.78%	81.00%	2,471	367	481	2,002	G.I.	—
Other holdings	N/A	N/A	N/A	N/A	N/A	N/A	224	I.	224
Playa de Madrid, S.A. (*) (**) (2) Distribution of all manner of goods, operation of sporting and hospitality facilities Doctor Fleming 3, 28036 Madrid	100.00%	—	100.00%	40	98	12	54	G.I.	—
Servicios de Teledistribución, S.A. (S.T. HILO) (*) (**) (2) Supply of services in the teledistribution industry Luchana 23, 28010 Madrid	100.00%	—	100.00%	210	458	(52)	297	G.I.	—
Taetel, S.L. (**) (3) Acquisition, holding and disposal of shares and holdings in other companies Beatriz de Bobadilla 3, 28040 Madrid	100.00%	—	100.00%	4,700	1,129	338	4,700	G.I.	—
Telecartera, S.A. (2) Acquisition, holding and disposal of shares and holdings in other companies Beatriz de Bobadilla 3, 28040 Madrid	75.00%	—	75.00%	1,025	(73)	(666)	797	G.I.	—
Sociedad General de Cablevisión Madrid, S.A. Cable television systems and value-added services Gran Vía 32, 28013 Madrid	51.00%	49.00%	87.750%	100	—	(23)	88	G.I.	—
Societat General de Cablevisió Barcelona, S.A. Cable television systems and value-added services Avinguda Icona 136, 08005 Barcelona	51.00%	49.00%	87.750%	100	1	(92)	55	G.I.	—
Sociedad General de Cablevisión Cantabria, S.A. Cable television systems and value-added services La Magdalena 2, 39001 Santander	51.00%	49.00%	87.750%	100	—	(25)	87	G.I.	—
Sociedad General de Cablevisión Alicante, S.A. Cable television systems and value-added services Avenida Pérez Galdós 5-7, 03004 Alicante	51.00%	49.00%	87.750%	100	—	(7)	97	G.I.	—
Sociedad General de Cablevisión Asturias, S.A. Cable television systems and value-added services Elozo 17, 33001 Oviedo	51.00%	49.00%	87.750%	100	—	2	101	G.I.	—
Sociedad General de Cablevisión Bizkaia, S.A. Cable television systems and value-added services Gregorio de la Revilla 27, 48010 Bilbao	51.00%	49.00%	87.750%	100	—	(22)	89	G.I.	—

(*) Companies filing consolidated corporate income tax returns in 1995.

(**) Companies filing consolidated corporate income tax returns in 1996.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1996

Group companies and their holdings	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
Sociedad General de Cablevisión Cádiz, S.A. Cable television systems and value-added services Santa María Soledad, 6 - 11006 Cádiz	51.00%	49.00%	87.750%	100	—	(9)	96	G.I.	—
Sociedad General de Cablevisión Granada, S.A. Cable television systems and value-added services Avda. del Sur 1, 18014 Granada	51.00%	49.00%	87.750%	100	—	1	101	G.I.	—
Sociedad General de Cablevisión León, S.A. Cable television systems and value-added services Pedre iso 16, 24002 León	51.00%	49.00%	87.750%	100	—	1	101	G.I.	—
Sociedad General de Cablevisión Lleida, S.A. Cable television systems and value-added services Clot de Les Monges 6-8, 25007 Lleida	51.00%	49.00%	87.750%	100	—	(17)	92	G.I.	—
Sociedad General de Cablevisión Málaga, S.A. Cable television systems and value-added services Hileria 2, 29007 Málaga	51.00%	49.00%	87.750%	100	—	2	101	G.I.	—
Sociedad General de Cablevisión Murcia, S.A. Cable television systems and value-added services San Antonio 4, 30005 Murcia	51.00%	49.00%	87.750%	100	—	(1)	94	G.I.	—
Sociedad General de Cablevisión Navarra, S.A. Cable television systems and value-added services Monasterio de la Oliva 9, Pamplona	51.00%	49.00%	87.750%	100	—	(16)	92	G.I.	—
Sociedad General de Cablevisión Rojía, S.A. Cable television systems and value-added services San Martín 3, 26004 Logroño	51.00%	49.00%	87.750%	100	—	(1)	100	G.I.	—
Sociedad General de Cablevisión Sevilla, S.A. Cable television systems and value-added services Graham Bell 5, Sevilla	51.00%	49.00%	87.750%	100	—	(14)	93	G.I.	—
Sociedad General de Cablevisión Valencia, S.A. Cable television systems and value-added services San Vicente 148, 46007 Valencia	51.00%	49.00%	87.750%	100	—	(8)	96	G.I.	—
Sociedad General de Cablevisión Valladolid, S.A. Cable television systems and value-added services Duque de la Victoria 10, 47001 Valladolid	51.00%	49.00%	87.750%	100	—	—	100	G.I.	—
Societat General de Cablevisió Balears, S.A. Cable television systems and value-added services Federico García Lorca 2, 07014 Palma de Mallorca	51.00%	49.00%	87.750%	100	—	(14)	93	G.I.	—
Sociedad General de Cablevisión Burgos, S.A. Cable television systems and value-added services Avda. Reyes Católicos 38-A-Burgos	51.00%	34.00%	76.500%	100	—	(4)	84	G.I.	—
Sociedad General de Cablevisión Canarias, S.A. Cable television systems and value-added services Alcalde Manólio Tejeral 8, 38007 Santa Cruz de Tenerife	51.00%	—	51.000%	215	—	(31)	110	G.I.	—
Sociedad General de Cablevisión A Coruña, S.A. (4)	51.00%	—	51.000%	—	—	—	51	L	51
Sociedad General de Cablevisión Santiago, S.A. (4)	51.00%	—	51.000%	—	—	—	51	L	51
Sociedad General de Cablevisión Vigo, S.A. (4)	51.00%	—	51.000%	—	—	—	51	L	51
Telecomunicaciones Marinas, S.A. (TEMASA) (*) (**) (2) Drilling, laying and repair of underwater cables Silva, 1 - 28013 Madrid	100.00%	—	100.00%	1,376	2,791	1,885	1,326	G.I.	—
Telefonía y Finanzas, S.A. (TELFISA) (*) (**) (3) Integrated cash management, counseling and financial support for Group companies Paseo de la Castellana 151, 10 ^a , 28046 Madrid	100.00%	—	100.00%	500	229	64	2,099	G.I.	—
Telefónica Investigación y Desarrollo, S.A. (TIDSA) (*) (**) (2) Telecommunications research activities and projects Emilio Vargas 6, 28043 Madrid	100.00%	—	100.00%	1,000	2,021	963	1,000	G.I.	—
Telefónica North America, INC (3) Financial intermediation 1209 Orange Street, Wilmington/New Castle County Delaware (USA)	100.00%	—	100.00%	1	—	—	1	G.I.	—
Telefónica Multimedia, S.A. (*) (**) (2) Organization and operation of multimedia service activities and businesses Rafael Calvo 18, 28010 Madrid	100.00%	—	100.00%	1,250	(131)	(206)	1,250	G.I.	—
Audiovisual Realtime BIT, S.A. (ARBIT) Generation of synthetic images Polígono Industrial Inca. Solar en intersección de las vías C y D Mallorca 07300 Inca	—	25.00%	25.00%	100	—	(108)	25	E	(4)

(*) Companies filing consolidated corporate income tax returns in 1995.

(**) Companies filing consolidated corporate income tax returns in 1996.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1996

Group companies and their holdings	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
T.I. Telefónica Internacional de España, S.A. (I) (6) <i>Investment in the telecommunications industry abroad</i> <i>Jorge Manrique 12, 28006 Madrid</i>	76.22%	—	76.22%	119,009	260,968	31,223	90,713	G.I.	—
Telefónica Internacional, S.A. (LUXEMBOURG) <i>Holding company</i>	—	100.00%	76.22%	US\$ 470 K	(18)	(11)	961	G.I.	—
Telefónica USA INC. (USA) <i>Representation of Telefónica</i>	—	100.00%	76.22%	US\$ 5 K	(123)	(8)	1	G.I.	—
Telefónica Finance Limited (ISLE OF MAN) <i>Finance</i>	—	100.00%	76.22%	£ 2 K	7,288	21	1	G.I.	—
Telefónica Perú Holding, S.A. (PERU) <i>Holding company</i>	—	90.00%	68.60%	US\$ 1,956 M.	(7)	5	249,701	G.I.	—
Telefónica del Perú, S.A. (PERU) <i>Operator of local, long-distance and international telephone services in Peru</i>	—	35.00%	24.01%	NSOL 2,338 M.	55,333	43,891	262,836	G.I.	—
Multicanal, S.A. (ARGENTINA) <i>Closed-circuit television</i>	—	25.00%	19.06%	ARGP 249 M.	6,170	7,284	18,219	E.	11,587
Sintelar, S.A. (ARGENTINA) <i>Telecommunications equipment systems and installation</i>	—	25.00%	19.06%	ARGP 2 M.	5	148	10	E.	378
Telefónica International Holding, B.V. (THE NETHERLANDS) <i>Holding company</i>	—	100.00%	76.22%	FL 1,154 M.	14,248	11,530	69,410	G.I.	—
Telefónica Chile Holding, B.V. (THE NETHERLANDS) <i>Holding company</i>	—	100.00%	76.22%	FL 100 K	6,858	(2)	26,992	G.I.	—
Telefónica Chile, S.A. (CHILE) <i>Holding company</i>	—	100.00%	76.22%	US\$ 74 M.	32,459	9,762	11,146	G.I.	—
Compañía de Telecomunicaciones de Chile, S.A. (C.T.C.), (CHILE) <i>Telecommunications operator in Chile</i>	—	43.62%	33.25%	CHP 325,864 M.	106,012	44,850	37,178	G.I.	—
Impresora y Comercial Publicitaria, S.A. (CHILE) <i>Publishing and sale of advertising. White and yellow pages</i>	—	54.93%	41.87%	CHP 2,101 M.	926	1,505	829	G.I.	—
Telefónica Venezuela Holding, B.V. (THE NETHERLANDS) <i>Holding company</i>	—	100.00%	76.22%	FL 40 K.	(7,988)	2,254	10,318	G.I.	—
Venworld Telecom, C.A. (VENEZUELA) <i>Holding company</i>	—	16.00%	12.20%	BOL 114,420 M.	N/D	N/D	N/D	E.	—
Compañía Andina de Teléfonos de Venezuela (CANTV) (VENEZUELA) <i>Telecommunications operator</i>	—	40.00%	4.88%	BOL 36,901 M.	312,600	55,218	N/D	E.	19,536
Compañía de Inversiones en Telecomunicaciones, S.A. (COINTEL) (ARGENTINA) <i>Holding</i>	—	33.16%	25.27%	ARGP 531 M.	140,054	15,923	52,143	E.	57,918
Telefónica de Argentina, S.A. (ARGENTINA) <i>Telecommunications operator in southern Argentina</i>	—	51.00%	12.89%	—	—	—	—	—	—
Telefónica de Argentina, S.A. (ARGENTINA)	—	1.08%	0.82%	ARGP 2,358 M.	98,415	48,773	7,827	E.	4,343
TYSSA, Telecomunicaciones y Sistemas, S.A. (ARGENTINA) <i>Telecommunications systems consulting</i>	—	34.39%	26.21%	ARGP 4 M.	40	(41)	100	L.	100
Telefónica Larga Distancia de Puerto Rico, INC. (PUERTO RICO) <i>Telecommunications operator</i>	—	79.00%	60.21%	US\$ 111 M.	(862)	(238)	14,855	G.I.	—
Telefónica Romania, S.A. (ROMANIA) <i>Cellular mobile telephony services</i>	—	60.00%	45.73%	US\$ 8 M.	382	868	650	G.I.	—
SintelPerú, S.A. (PERU) <i>Telecommunications equipment systems and installation</i>	—	25.00%	19.06%	NSOL 5 M.	25	269	33	E.	111
Contactel (PORTUGAL) <i>Telecommunications operator (Radiohaging)</i>	—	15.00%	11.43%	ESC 1,200 K	N/D	(198)	261	L.	261
Telecomunicaciones Ultramarinas de Puerto Rico (PUERTO RICO) <i>Telecommunications operator</i>	—	14.90%	11.36%	US\$ 1 K	N/D	N/D	3,280	L.	3,280
Infonet Services Corporation (USA) <i>Telecommunications operator</i>	—	8.74%	14.28%	US\$ 68 M.	2,359	101	4,604	L.	4,604
Geostar Corporation	—	—	—	N/D	N/D	N/D	559	L.	559
Companhia Riograndense de Telecomunicações, S.A. (Rio do Sul) (BRASIL) <i>Telefónica Sistemas de Portugal (PORTUGAL)</i>	—	10.30%	7.85%	702 M. REAL	105,019	539	68,876	L.	68,876
Teiur, S.A. (RUSSIAN FEDERATION) <i>Manufacture of telecommunications equipment</i>	—	5.00%	10.57%	RUB 6 M.	N/D	N/D	53	L.	53
Other holdings	—	N/A	N/A	N/A	N/A	N/A	—	E.	1,075
Other holdings	—	N/A	N/A	N/A	N/A	N/A	5,489	L.	5,489

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1996

Group companies and their holdings	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
T.S. Telefónica Sistemas, S.A. (*) (**) (2) <i>Telecommunications systems, network and infrastructure engineering</i> <i>Sor Ángela de la Cruz 3, 28020 Madrid</i>	100.00%	—	100.00%	1,403	2,273	554	2,366	G.I.	—
Telefónica Sistemas de Información Geográfica, S.A. (TSIG) (*) (**) (2) <i>Computer advisory services and digital cartography</i> <i>Ortense 11, 28020 Madrid</i>		100.00%	100.00%	215	25	87	230	G.I.	—
Telefónica Sistemas de Satélites, S.A. (TSS) (*) (**) (2) <i>Engineering, management and marketing of satellite networks</i> <i>Romírez de Arellano 19, 28043 Madrid</i>		100.00%	100.00%	10	305	158	10	G.I.	—
Telefónica Servicios Avanzados de Información, S.A. (TSAI) (*) (**) (2) <i>Value added services relating to public or private infrastructures</i> <i>Julián Comanillo 6, 28037 Madrid</i>		100.00%	100.00%	310	167	219	310	G.I.	—
Telefónica Gestión de Sistemas, S.A. (TGS) (*) (**) (2) <i>Systems outsourcing</i> <i>Sor Ángela de la Cruz 3, 28020 Madrid</i>		100.00%	100.00%	50	58	50	50	G.I.	—
Telefónica Sistemas Ingeniería de Productos, S.A. (TSIP) (*) (**) (2) <i>Public communications network infrastructure</i> <i>Torrelaguna 79, 28027 Madrid</i>		100.00%	100.00%	150	100	195	150	G.I.	—
Telefónica Sistemas Ingeniería de Productos Seguridad, S.A. (TSIPS) (*) (**) (2) <i>Security and control installation and systems</i> <i>Julián Comanillo 6, 28037 Madrid</i>		100.00%	100.00%	40	13	8	53	G.I.	—
Servicios y Contenidos por la Red, S.A. (SCR) (2) <i>Provision of services in the leisure and entertainment areas</i> <i>Julián Comanillo 6, 28037 Madrid</i>		100.00%	100.00%	25	1	(223)	117	G.I.	—
Gestión y Operación de Redes, S.A. (GESTIRED) (2) <i>Management and marketing of networks</i> <i>Rosario Pina, 5 - Madrid</i>		100.00%	100.00%	70	(1)	(42)	35	G.I.	—
T.S. Telefónica Sistemas de Portugal (PORTUGAL) (2) <i>Communications systems equipment engineering</i> <i>Plaza Alvalade 6, 1700 Lisbon</i>		74.99%	94.05%	25	(16)	(18)	25	G.I.	—
Negocios Cibernéticos, S.A. (2) <i>Development of security software in the card environment</i> <i>Julián Comanillo 6, 28037 Madrid</i>		50.00%	50.00%	10	—	(1)	5	G.I.	—
Portel Servicios Telemáticos, S.A. <i>Systems engineering and telecommunications in port areas</i> <i>Avenida del Portón 10, Campo de las Naciones 28042 Madrid</i>		49.00%	49.00%	500	—	(63)	245	E.	214
Madrid 112 <i>Emergency services in the Autonomous Community of Madrid</i>		49.00%	49.00%	150	—	—	74	E.	74
Brite Baleares Innovación Telemática, S.A. <i>Provision of systems engineering services in the information technologies and communications fields</i> <i>Paseo Marítimo 38 A 07005 Palma de Mallorca</i>		44.00%	44.00%	316	(69)	(19)	139	E.	100
Tecnología e Ingeniería de Sisi y Servicios Avanzados de Telex, S.A. (TISAT) <i>Systems engineering and marketing of advanced services</i> <i>Correos 1, 46002 Valencia</i>		40.00%	40.00%	100	16	(18)	40	E.	39
Hispaservices, S.A. <i>Data processing through communication networks and computer media</i> <i>Avenida de Burgos 17, Torre A 10º, 28036 Madrid</i>		39.00%	39.00%	350	(49)	(148)	137	E.	60
Other holdings	N/A	N/A	N/A	N/A	N/A	N/A	1	E.	1
Telefónica Telecomunicaciones Públicas, S.A. (**) <i>Public telecommunications activities</i> <i>Paseo de Recoletos 41, 28004 Madrid</i>	100.00%	—	100.00%	10	—	—	10	G.I.	—
Teleinformática y Comunicaciones, S.A. (TELYCO) (*) (**) (2) <i>Promotion, marketing and distribution of telephone and telematic equipment and services</i> <i>Raimundo Fernández Villaverde 28, 28003 Madrid</i>	100.00%	—	100.00%	460	130	828	2,075	G.I.	—
Urbana Ibérica, S.A. (3) <i>Collection of debts outstanding and management of the cash generated by the sale of land and buildings</i> <i>Pº de la Castellana 151, 10º b, 28046 Madrid</i>	100.00%	—	100.00%	264	(46)	4	14	G.I.	—

(*) Companies filing consolidated corporate income tax returns in 1995.

(**) Companies filing consolidated corporate income tax returns in 1996.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1996

Group companies and their holdings	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
Telefónica Servicios Móviles, S.A. (*) (**) (1) <i>Management and marketing of automatic mobile telephony</i> <i>Plaza de la Independencia 6, 28001 Madrid</i>	100.00%	—	100.00%	68,100	11,694	(6,151)	78,460	G.I.	—
Radiored 1, S.A. (*) (**) (1) Group company management support. Trunking (Parent Company) Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	1,250	461	(628)	2,250	G.I.	—
Radiored Madrid, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	150	(66)	(91)	150	G.I.	—
Radiored Bilbao, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	150	(64)	(75)	150	G.I.	—
Radiored Valencia, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	140	(58)	(61)	140	G.I.	—
Radiored Málaga - Costa del Sol, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	145	(61)	(41)	145	G.I.	—
Radiored Sevilla - Cádiz, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	160	(72)	(61)	160	G.I.	—
Radiored Santiago - La Coruña, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	130	(56)	(71)	130	G.I.	—
Radiored Zaragoza, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	185	(54)	(114)	177	G.I.	—
Radiored Canarias, S.A. Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	10	—	—	10	G.I.	—
Radiored Extremadura, S.A. Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	10	—	—	10	G.I.	—
Radiored Baleares, S.A. Trunking Manuel Tovar 35, 28034 Madrid		100.00%	100.00%	10	—	—	10	G.I.	—
Radiored Catalunya, S.A. (*) (**) (1) Trunking Manuel Tovar 35, 28034 Madrid		91.00%	91.00%	200	(80)	(40)	182	G.I.	—
Compañía Gestora del Servicio Mensatel, S.A. (1) Management and marketing of the Mensatel radiopaging service Manuel Tovar 35, 28034 Madrid		90.00%	90.00%	667	353	45	622	G.I.	—
Telefónica Publicidad e Información, S.A. (*) (**) (2) <i>Publishing of directories and advertising for all types of support</i> <i>Avda. de Manoteras, 12, 28050 Madrid</i>	100.00%	—	100.00%	502	2,823	3,303	996	G.I.	—
Estrategias Telefónicas, S.A. (ESTRATEL) (*) (**) (2) Services promotion, marketing and market surveys relating to direct marketing Orense 4, 28020 Madrid		100.00%	100.00%	230	343	364	411	G.I.	—
Tempotel, Empresa de Trabajo Temporal, S.A. Temporary employment agency Príncipe de Vergara 26, 28001 Madrid		100.00%	100.00%	10	—	(2)	10	G.I.	—
Rem Informática, S.A. (2) Production of 3D objects, promotion and marketing of computer products and services Plaza Santa Bárbara 10, Madrid		60.00%	60.00%	50	—	(157)	30	G.I.	—
TMP Worldwide España, S.A. Marketing of advertising of large customers in yellow pages Príncipe de Vergara 112, 28001 Madrid		51.00%	51.00%	45	(16)	2	23	G.I.	—
Venturini España, S.A. Printing and graphic arts Industria 17, Tres Cantos, Madrid		25.00%	25.00%	500	35	37	125	E	143
Euredit, S.A. Publishing of European directories Avda. Friedland 9, 79008 Paris (France)		5.00%	5.00%	62	N/D	N/D	13	I	13
Telefónica Europe, B.V. <i>Attracting funds in capital markets</i> <i>Aert van Nesstraat 45, 4° Rotterdam - 3012 CA - The Netherlands</i>	100.00%	—	00.00%	8	—	—	8	G.I.	—

(*) Companies filing consolidated corporate income tax returns in 1995.

(**) Companies filing consolidated corporate income tax returns in 1996.

DETAIL OF GROUP AND ASSOCIATED COMPANIES AND INVESTEEES AS OF DECEMBER 31, 1996

Associated companies	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
Telefónica Fiat Factoring, Entidad de Financiación, S.A. <i>Sociedad de factoring</i> <i>Pedro Teixeira, 8 - 28020 Madrid</i>	50.00%		50.00%	1,560	55	(259)	795	PE	700
Torre de Colçerola, S.A. <i>Operation of a telecommunications tower</i> <i>Ctra. Vallvidrera - Tibidabo s/n, 08017 Barcelona</i>	42.00%	—	42.00%	2,000	(17)	12	845	E	839
Pabellón de Op. Europeas de Telecomunicaciones, S.A. (P.O.E.T.) (5) <i>Gron Via, 28, 28013 Madrid</i>	38.46%	—	38.46%	520	—	—	200	E	1
Indra SSI, S.A. <i>Software</i> <i>Velázquez, 132, 28006 Madrid</i>	36.56%	—	36.56%	2,302	2,235	167	2,121	E	1,784
Sistemas Técnicos de Loterías del Estado, S.A. <i>Operation of a gaming terminal system for Organismo Nacional de Loterías y Apuestas del Estado</i> <i>Manuel Tovar 9, 28034 Madrid</i>	31.75%	—	31.75%	2,000	3,333	1,467	635	E	1,887
Unisource, N.V. <i>Pan-European provider of telecommunications services</i> <i>Polarisavenue 97-2132 JH Hoofddorp, The Netherlands</i>	25.00%	—	25.00%	6,838	43,867	(22,018)	20,418	E	4,572
Hispasat, S.A. <i>Operation of a satellite telecommunications system</i> <i>Gobelos 41-45, 28023 Madrid</i>	22.74%	—	22.74%	15,312	(3,770)	(1,231)	5,339	E	2,113
Sofres Audiencia de Medios, S.A. <i>Market surveys and audience measurement</i> <i>Plaza Carlos Trias Bertrán 7, 28020 Madrid</i>	25.00%	—	25.00%	210	112	425	435	E	190
Compañía Celular de Colombia, S.A. (COCELCO) (COLOMBIA) <i>Celular mobile telephony services in western Colombia</i> <i>Santa Fe de Bogotá D.I. Colombia</i>	14.51%	20.25%	29.94%	75,017 M.PCOL	8,222	743	6,882	E	7,086
Amper, S.A. <i>Development, manufacture and repair of telecommunications systems and equipment and their components</i> <i>Torrelogueta 75, 28027 Madrid</i>	15.00%	—	15.00%	6,977	1,657	894	3,039	E	1,551

Investees	Percentage of ownership			Capital	Reserves	Income (loss)	Book value	Consolidation method	Value in consolidation
	Direct	Indirect	Telefónica Group						
Compañía de Fibra Óptica Telcor, S.A.	35.00%	—	35.00%	100	N/D	N/D	35	L	35
Reto 2000, S.A. <i>Design of a project to eliminate overhead lines in the historical center of Toledo</i> <i>Plaza de San Vicente 3, 45001 Toledo</i>	21.74%	—	21.74%	2	N/D	N/D	1	L	1
Agrupació d'Empreses Llei 18/1982 de 26 Maig (A.C.E.F.H.A.T.)	20.00%	—	20.00%	110	N/D	N/D	22	L	22
Centro de Investigación en Tecnologías y Aplicaciones Mult.(CITAM)	20.00%	—	20.00%	1	N/D	N/D	—	L	—
Compañía Inmobiliaria Darsa Gaditana, S.A. <i>Construction of urban buildings for use as housing units, commercial premises or warehouses for lease or sale</i> <i>Avenida Marconi 34, 11011 Cádiz</i>	10.23%	—	10.23%	25	N/D	N/D	3	L	3
Promoció de Ciutat Vella, S.A. <i>Urban improvements in the Ciutat Vella of Barcelona</i> <i>Rambles 77, 08002 Barcelona</i>	3.57%	—	3.57%	2,800	N/D	N/D	100	L	100
Catalana D'Iniciatives, C.R., S.A. <i>Promotion of nonfinance entities</i> <i>Passeig de Gràcia 2, 08007 Barcelona</i>	2.35%	1.26%	3.61%	5,000	N/D	N/D	240	L	240
I-CO Global Communications (HOLDINGS) Limited	2.18%	—	2.18%	189,069	75,621	(2,604)	3,852	L	3,852
Club de Inversores para el Desarrollo de la provincia de Alicante, S.A.	1.00%	—	1.00%	250	N/D	N/D	2	L	2
Agencia EFE, S.A. <i>Obtainment and distribution of news throughout the world</i> <i>Espronceda 32, 28003 Madrid</i>	0.16%	—	0.16%	3,475	N/D	N/D	140	L	140
Other holdings	N/A	N/A	N/A	N/A	N/A	N/A	5,710	L	5,710

(1) Companies audited by Arthur Andersen.

(2) Companies audited by Price Waterhouse

(3) Companies audited by K.P.M.G. Peat Marwick.

(4) Companies not yet formed.

(5) Companies in liquidation.

(6) Consolidated figures.

Figures in foreign currencies: M=Millions, t=Thousands

G.I. Companies consolidated by the global integration method.

P.I. Companies consolidated by the proportional integration method.

E. Companies carried by the equity method.

I. Investees.

EXHIBIT II

The main telecommunications operators in the Telefónica Group, the percentages of ownership in which and methods of consolidation of which are disclosed in Exhibit I, are as follows:

Telefónica del Perú, S.A.-

This company provides local, long distance and international telephone services in Peru, under a licensing agreement entered into with the Government of Peru on May 16, 1994. The agreement has a term of 20 years, renewable for a further 20 years, the first five years being subject to an exclusive regime. As of December 31, 1996, the company had 6,338 employees (8,456 in 1995), it operated 1,764,809 lines (1,309,908 in 1995) and it had 130,895 cellular mobile telephone customers (38,465 in 1995) and 101,387 cable television subscribers (19,060 in 1995). As of December 31, 1996, Telefónica del Perú had an 85% holding in Telefónica Multimedia, S.A.

Compañía de Telecomunicaciones de Chile, S.A. (CTC)

This company supplies telephony services in Chile. As of December 31, 1996, it had 9,430 employees (9,276 in 1995), operated 2,296,042 lines (1,999,028 in 1995), and had 186,059 cellular mobile telephone customers (57,842 in 1995), 216,630 cable television subscribers (77,034 in 1995) and 37,657 radio trunking and radiopaging service subscribers. The holding was acquired in April 1990 and in January 1991, when a call option was exercised on a small number of shares. CTC is the parent company of a group of companies, comprising:

	Percentage of ownership
— CTT-Red Multimedia, S.A.	99.99%
— CTC-Isapre, S.A.	99.99%
— CTC-Equipos y Servicios de Telecomunicaciones, S.A.	99.99%
— CTC-Corp., S.A.	99.99%
— CTC-Transmisiones Regionales, S.A.	99.15%
— CTC-Marketing e Información, S.A.	60.00%
— Invercom, S.A.	80.00%
— Metrópolis	32.00%
— Instacom, S.A.	99.99%
— CTC Internacional	99.99%
— Startel, S.A.	55.00%
— Multicable Televisión, S.A.	99.93%

Telefónica de Argentina, S.A. (TASA)

This company provides telephony services in southern Argentina. As of September 30, 1996, its fiscal year-end, TASA had 14,279 employees (15,928 in 1995) it operated 3,911,965 lines (3,562,123 in 1995) and had 189,241 cellular mobile telephone customers, 28,094 radiopaging service subscribers and 37,783 directory customers.

	Percentage of ownership
— Telinver, S.A.	99.99%
— Telintar, S.A.	50.00%
— Miniphone, S.A.	50.00%
— Startel, S.A.	50.00%
— Tyssa	80.00%
— Radio Llamada, S.A.C.I.	50.00%
— Telefónica Comunicaciones Personales	99.99%
— Telefónica Servicios Globales, S.A.	99.99%

Compañía Anónima de Teléfonos de Venezuela (CANTV)

This company supplies telephony services in Venezuela. As of December 31, 1996, it operated 3,214,214 lines (2,942,544 in 1995), had 210,885 cellular mobile telephony subscribers (169,758 in 1995), and had 17,983 employees (20,993 in 1995). The holding was acquired in December 1991. In turn, CANTV has holdings in the following companies:

	Percentage of Ownership
— MOVILNEL	100%
— CAVEGUÍAS	80%
— INVERCANTV	100%
— CANTV SERVICIOS	100%

Telefónica Larga Distancia (TLD)

This company provides long-distance terrestrial telephony services in Puerto Rico. As of December 31, 1996, it had 307 employees (268 in 1995). The holding was acquired on December 22, 1992.

Telecomunicaciones Ultramarinas-

This company provides long-distance satellite and radio telephony services in Puerto Rico.

Telefónica Romania, S.A.-

This company renders cellular mobile telephone services in Romania under a license granted on March 24, 1992. The service came into operation on April 5, 1993. The license provides for the possibility of developing the rural telephone service using the infrastructure of the mobile telephone network. As of December 31, 1996, the company had 189 employees and (112 in 1995) and 17,660 cellular mobile telephony subscribers (9,068 in 1995).

Compañía Celular de Colombia, S.A.-

This Colombian company renders cellular mobile telephony services in western Colombia under license agreements entered into with the Colombian government on March 28, 1994, with a term of ten years, extendible for a further ten years. As of December 31, 1996, it had 42,253 cellular telephone customers.

Multicanal, S.A.-

This Argentinean company provides multimedia services in the cable television industry. As of December 31, 1996, it operated 22 licenses and had 831,243 customers and 2,154 employees.

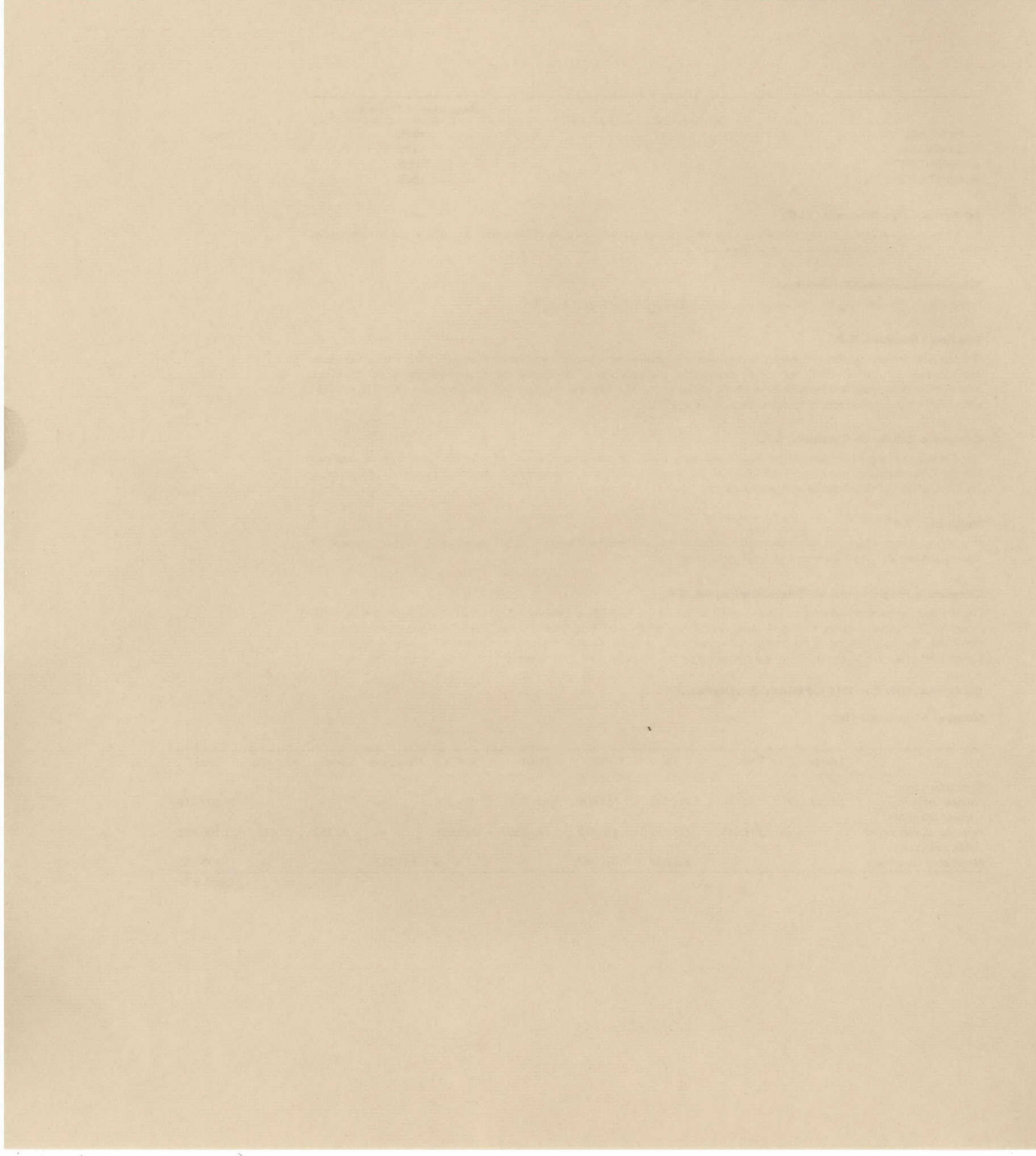
Companhia Riograndense de Telecomunicações, S.A.-

This Brazilian company provides telecommunications services in the State of Rio Grande do Sul in Brazil. As of December 31, 1996, it had 4,735 employees, operated 946,447 lines -781,789 of which were in service- and had 168,479 cellular mobile telephone customers. The total holding in this company's capital stock is 10.3% through the Group companies' various holdings in the Consortium which was awarded 35% of the company's common shares in the call for tenders held in December 1996.

INFORMATION ON THE OPERATOR COMPANIES

Number of lines installed-

[illegible]



Throughout 1996, Telefonica developed extensive activities, aimed both at maintaining its position of leadership in the telecommunications marketplace in Spain within the environment of the steady liberalization of telephony services, and the strengthening of its international presence, widening its geographical area of activity, and extending its operations in new business lines with high growth potential, especially in the multimedia sector (cable TV). All these activities have had one objective in common, that of offering our customer the ideal solutions for their communications needs.

The Telefónica Group has continued to broaden the scope of the products and services offered by the Group's companies, both through the launching of publicity campaigns aimed at increasing penetration and usage, and through more personal contact with our customers, a consequence of the introduction of our new distribution service «TeleSpaclo», where our customers can, in person, purchase, subscribe to, or obtain information on our services or; these services can be obtained through the TeleSpaclo's direct freephone service.

Continuing this objective of improving and diversifying the services on offer to our customers, along with increasing the competitiveness of our products, the Board of Directors approved the new organizational structure, as a result of which the Telefónica Group has been divided into three basic parts:

- The Corporate Centre, guaranteeing the Group's strategic orientation, and made up of Planning and Management Control, Institutional Relations, Corporate Finance, Regulatory Issues and General and Board Secretary.

- The Business Units, focusing on the marketplace, customers and products, and made up of Corporate Customers, Retail clients, Telefónica Internacional, Telefónica Móviles and International.

- Two Common Resources Units, Infrastructures and Resources, supporting the Business Units and providing the services common to the latter.

Throughout the year, a series of agreements and alliances with different entities, from both domestic and international viewpoints, have permitted the consolidation and expansion of Telefónica's position in the telecommunications marketplace.

In January 1996, Telefónica and Iberdrola formed a strategic telecommunications alliance to create a company to promote and manage the provision of value-added services to the energy sector; develop joint activities in local operators in which Telefónica participates, and establish agreements to optimize the usage of the telecommunications infrastructures of both companies and extend this collaboration to the Latin American market.

In February, Telefónica signed an agreement with the Fomento de Construcciones y Contratas group (FCC), which establishes the possibility for the latter to acquire the minimum of a 20% stake in the share capital of Cabiltel, the Telefónica Group company responsible for the marketing of the public telephony service.

In this same month, Telefónica Internacional formalized its participation in Multicanal's share capital, the Argentinian cable TV operator; through the acquisition of a 25% stake for a total value of \$US 168.5 million. The company's other partners are: the Clarin Group (the leading communications group in Argentina) and Citicorp Equity Investments, who hold 52.5% and 22.5%, respectively.

Regarding the cable TV market, the leading Peruvian telecommunications group, El Comercio, acquired a 15% stake in the share capital of our subsidiary Telefónica Multimedia del Perú.

These agreements further strengthen the Telefónica Group's expansion strategy in the field of multimedia in Latin America, as we now operate cable TV in Argentina, Chile and Peru, through the main local communications groups.

Within the framework of the Telefónica Group's policy, in recent years, of the divestiture of its participations in non-strategic companies, on April 30th, the sale of the Telefónica de España subsidiary, Sistemas e Instalaciones de Telecomunicación, S.A. (SINTEL) to MasTec International Inc. was completed for an amount of 4,900 million pesetas. SINTEL specializes in the installation and laying of lines and cables in the telecommunications field.

In May, Telefónica de España became an official partner of the European telecommunications consortium Unisource, through an exchange of shares, 100% of the shares corresponding to both the data transmission operator, Telefónica Transmisión de Datos, S.A. and Telefónica VSAT, S.A., the operator responsible for the transmission of telecommunications via the Paneuropean satellite VSAT.

These shares were exchanged for a 25% stake in Unisource N.V., with no cash outlay whatsoever on the part of Telefónica.

In November, Telefónica de España, Telecartera, the Sociedad General de Cablevisión and Sogecable signed an agreement which dissolved the cable TV agreement undertaken in July 1995. The result of the November agreement has been that Sogecable has acquired the shares held by Telefónica in Cablevisión, and Telefónica has acquired the shares held by both Sogecable and Cablevisión in the local Telefónica operators, with the exception of the Canary Islands. The aforementioned operators are now wholly-owned by Telefónica.

Likewise, Telefónica, Radio Televisión Española, Antena 3 de Televisión, Televisa, Televisió de Catalunya, Telemadrid, Canal 9 (Valencian television) and Televisión de Galicia signed an agreement through which they undertook to create, before December 16th 1996, a limited company for the broadcasting of digital television, via satellite, throughout the whole of Spain. Due to changes in the initial project, made by some of the partners (Antena 3), the structure and deadlines for the launching of the project are being reconsidered.

The consortium led by Telefónica Internacional, and in which the local Brazilian operator RBS participates (Participações Rede Brasil Sul), along with Telefónica de Argentina and the Chilean CTC won the bidding process for 35% of the voting shares of the Companhia Riograndense de Telecomunicações (CRT) in the state of Rio Grande do Sul, Brazil. This followed an international bidding process which commenced on December 17th, 1996, for the amount of 681 million reales. The strategic presence of Telefónica Internacional in Brazil, will allow this company to complement its existing investments in Latin America and to therefore strengthen its position of leadership both in the telecommunications sector in Latin America and in the area of Mercosur.

Telefónica Internacional has also pre-qualified for the granting of 35% of the share capital of Empresa Ecuatoriana de Telecomunicaciones (EMETEL).

Regarding financial matters, in the month of November, Telefónica launched its EMTN programme (Euro Medium Term Notes) through which successive debt note issues will be made on the EMTN market, with a maximum limit of \$US 1,500 million.

In order to launch the aforementioned programme it was necessary to gain a long-term rating. The Company therefore solicited this rating from Standard and Poor's and IBCA who subsequently gave Telefónica an AA- rating.

In December, the Cabinet authorized the Dirección General del Patrimonio del Estado to transfer the State-owned participation in Telefónica to the Sociedad Estatal de Participaciones Patrimoni-

ales (SEPPa) to be sold on domestic and international markets by way of a Public Offering, to take place on February 18th, 1997.

As a result of this Offering, the State now holds a 0.65% participation in Telefónica's share capital. This 0.65% stake is purely to cover the fidelity shares to be given to retail investors who maintain their investment for a year.

The previously mentioned operation has resulted in the State no longer being present on Telefónica's Board of Directors, which has adopted new internal rules regulating the organization and workings of the Board which is now made up of 18 members.

ECONOMIC RESULTS

The Telefónica Group recorded favourable results for fiscal 1996, reflecting growth in all the operating margins. This favourable performance resulted in consolidated net income reaching 160,282 million pesetas, having grown 20.3% over the figure for 1995. The principal contributors to this performance were:

Operating income rose 14.5%, favoured by the 9.5% increase in usage per line, the revenue from leased circuits which rose 146.0%, the steady introduction of new basic telephony services rising 53.3% and the growing contribution from Telefónica Servicios Móviles and our international businesses which are both areas of high growth and registered respective increases of 129.9% and 18.0%.

Operating expenses grew 20.5% compared with 5.3% the previous year. The restraint on personnel expenses, which rose 2.0%, was contrasted by the considerable increase in those expenses related with the revenue derived from marketing and promotion activities, with the overall figure for supplies and subcontracts rising by 55.8%.

The 7.7% decrease in financial expenses came as a consequence of the fall off in interest rates. Also outstanding is the contribution to the growth in profit derived from the 14.8% decrease in non-depreciated dismantled plant.

At year-end 1996, the Telefónica Group participated in the management of more than 26.4 million lines in service, of which 16.2 pertain to the Spanish market and the remaining number to Latin America. Likewise, the Group had 1.1 million cable TV customers, while the cellular mobile telephony business reached the figure of 3.3 million customers recording 142.0% growth.

Operating revenue

Consolidated operating revenue amounted to 2,171,135 million pesetas, having risen 14.5%. Operating revenue was the principal contributor to this performance, having grown 15.3% to reach

2,006,058 million pesetas, compared with the 10.2% increase the previous year.

Telefónica's operating revenue totalled 1,473,045 million pesetas, reflecting a 7.3% rise. Of this figure 83.1% derives from domestic basic telephony, 9.2% from international communications and the remaining amount from public telephony services, data transmission and special projects.

Revenue from basic telephony rose 17.3% to reach 1,223,496 million pesetas. This significant growth contrasts with the 5.6% increase registered in 1995. This performance is due to a series of factors, namely: the variation in the revenue generated from subscriber charges, the connection fees and domestic traffic originating from the fixed network was also contributed to by the 2.8% increase in billable plant and the 8.1% rise in domestic usage in minutes per line. In addition to this factor, new revenues were also generated by the segregation of businesses, the leasing of circuits to other operators (TSM, TTD and Airtel), the interconnection with other operators of mobile-fixed traffic and contracts with other businesses.

Besides Telefónica's contribution to the Group's operating revenue, that of mobile telephony and the international businesses also stands out.

Mobile telephony, totally managed by Telefónica Servicios Móviles, registered revenue amounting to 256,384 million pesetas, reflecting 129.9% growth. At year-end 1996, this subsidiary's customer portfolio had risen 152.5% to total 2,345,645, of which 1,037,716 subscribed to the Movistar GSM service. Therefore, combining the customers from the two services, GSM and analog, Telefónica Móviles now has a market share of 78%.

The Group's overseas activities, which from the outset have been managed by Telefónica Internacional, registered revenue totalling 331,598 million pesetas, having risen 18.0%.

Operating expenses

The Group's operating expenses rose 20.5% to 1,023,065 million pesetas, when compared with 1995. Throughout the year, the restraint on personnel expenses continued, rising 2.0% to total 554,682 million pesetas, contributed to by the average 7.1% fall off in workforce, to close the year with an average of 92,148 employees.

At year-end 1996, Telefónica de España recorded personnel expenses amounting to 442,562 million pesetas, and a workforce of 67,217 employees, 2,326 employees fewer than at the close of 1995. Due to this, the productivity indicator of lines per employee continued to improve, going from 226.8 in 1995, to 243.1 in 1996. Regarding the other Group companies, the 7.6% increase in per-

sonnel expenses registered by the Telefónica Internacional Group is particularly noteworthy. This growth is due, to a large extent, to the fact that in 1995 CTC recorded its capitalized personnel expenses under «Personnel Expenses» instead of as internal expenditure capitalized in fixed assets.

In contrast with the restraint on personnel expenses, the expenses derived from supplies and subcontracts grew 55.8%, as a consequence of the increased marketing activity carried out by some of the Group's companies, especially Telefónica Servicios Móviles, Telyco and Telefónica de España. The main reason for the growth in these expenses can be found in the expansion of cellular mobile telephony in Spain, reflected by the expenses derived from advertising and promotion campaigns, the distribution commissions paid to Telefónica Servicios Móviles' distributors, and the expense of procuring Telyco terminals.

Depreciation amounted to 526,229 million pesetas, having grown 4.9% over the year, principally due to the 64,289 million peseta contribution made by Telefónica Internacional, which reflected 21.3% growth. This performance by the Telefónica Internacional Group has come about due to the growing investment in CTC and Telefónica del Perú, combined with the accounting adjustments made for the inflation on intangible assets in Chile and Peru.

Operating profit

The combination of the growth in revenue and the performance registered by operating expenses, resulted in consolidated operating profit climbing 13.0% to reach 575,965 million pesetas.

Profit before extraordinary items

Profit before extraordinary items stood at 390,399 million pesetas, 22.2% higher than the figure for 1995, principally due to the decrease witnessed in financial expenses.

Financial expenses continue to play an important role in the growth in income, as over 1996 they fell 7.7%, continuing their downward trend, to stand at 206,425 million pesetas, with 10.3% weight over operating revenue (this figure was 12.8% in 1995). The reduction in interest rates made a particularly favourable contribution to this performance.

Telefónica's 25% participation in Unisource has meant the integration of the latter's results in the Group's profit and loss accounts using the equity method, as also occurs with companies such as Telefónica de Argentina and CANTV-Venezuela. Therefore, the companies that consolidate using the equity method recorded net income amounting to 7,811 million pesetas, 10.8% down on the 1995-figure, principally due to the registering of Telefónica's participation in Unisource losses over the period.

Pre-tax income

The Telefónica Group's pre-tax income rose 23.3% to total 275,881 million pesetas.

Within the item extraordinary results, the performance of extraordinary income must be mentioned as this reached 31,941 million pesetas, 6.9% up on the figure for 1995. This figure principally comprises of the extraordinary income contributed by Telefónica Internacional which amounted to 13,543 million pesetas, principally due to the extraordinary income registered by CTC (6,597 million pesetas), deriving from the merger of its mobile subsidiary, Compañía de Telecomunicaciones de Chile, with VTR Celular, and from the sale of the non-strategic participation in Telefónica de Argentina, which took place in the first quarter of the year. The remaining amount is principally from capital grants and compensation.

On the other hand, extraordinary expenses totalled 146,459 million pesetas, having risen 16.6%. The main reason for this increase has been the payments and provisions for early retirement and the release scheme, which rose 6.8% to reach 58,519 million pesetas. The 14.8% decrease in non-depreciated dismantled plant amounted to 47,918 million pesetas, partly offsetting this increase.

Net income

The provision for corporate tax amounted to 56,921 million pesetas, therefore setting the effective rate for the Group at 20.6%, compared with the 17.6% applied the previous year. This provision is 44.6% higher than that of 1995 due to the performance of income and the resulting higher effective tax rates. In the case of the Telefónica Internacional Group, the overall taxes for this sub-group rose 38.2%, increasing the effective rate from 21.3% to 24.6%.

Minority interests grew 14.7% to 58,678 million pesetas, due to the increases in the results of the companies in which Telefónica Internacional participates.

The favourable performances reflected by the different margins in the profit and loss accounts, when compared with 1995, permitted a 20.3% increase in consolidated net income which stood at 160,282 million pesetas.

RESEARCH AND DEVELOPMENT

Throughout 1996, the investment in research and development grew 8.4% to total 21,170 million pesetas. This figure makes up 46.6% of the Group's total investment in intangible assets.

Following the consolidation of the new operating framework, Telefónica I+D continued its aim of ensuring that the Telefónica Group is able to offer a range of services and solutions to the customer's needs that are increasingly extensive and different to those offered by the competition.

This activity has borne the following results: regarding the development of services, InfoVia has been consolidated having been implanted in Peru and Chile, along with the developments in mobile services, multimedia and public telephony. On the other hand, in terms of the activities aimed at improving the efficiency and quality in the operating of networks, attention must be drawn to the new versions of the Structure of Operating and Monitoring, the MORE system aimed at the modernizing of analog exchanges and the new tools for network planning.

Treasury Stock

Throughout 1996, no treasury stock was acquired.

FINANCIAL REVIEW AND EXHIBITS

SELECTED FINANCIAL DATA. CONSOLIDATED (Million pesetas)

	1992	1993	1994	1995	1996	1996 \$ (3)
Revenue from operations	1,208,938	1,297,437	1,578,850	1,740,557	2,006,058	15,281.3
Operating expenses	613,788	656,655	806,400	849,258	1,023,065	7,793.3
Financial expenses	220,912	242,342	236,101	223,656	206,425	1,572.5
Depreciation and amortization (1)	385,152	413,261	515,116	567,992	594,536	4,528.9
Net income	80,761	96,367	112,608	133,214	160,282	1,221.0
Cash flow	465,250	502,882	644,750	750,357	811,235	6,179.7
Share capital	463,480	469,735	469,735	469,735	469,735	3,578.3
Shareholders' equity	1,392,005	1,437,055	1,512,031	1,546,472	1,863,760	14,197.4
Long-term debt	1,610,878	1,569,568	1,773,321	1,665,508	1,603,896	12,217.8
Financial debt	1,887,687	1,824,654	2,032,020	1,941,908	1,995,940	15,204.3
Investment (2)	459,279	380,634	489,606	632,893	724,253	5,517.1

(1) Including amortization of goodwill.

(2) Fixed and intangible.

(3) Figures in million dollars. 30-12-96 exchange rate: \$ 1 = ptas. 131.275

TELEFONICA GROUP: OPERATING REVENUE (Million pesetas)

	1993	1994	1995	1996	Increase (%) Over 1995	1996 \$ (1)
Parent company						
Basic telephony	955,580	988,649	1,042,985	1,223,496	17.3	9,320.1
Telephone service	767,899	802,545	843,748	947,748	12.3	7,219.5
Leased circuits	40,685	34,103	29,809	73,317	146.0	558.5
Ibercom	48,399	54,769	58,517	69,290	18.4	527.8
Digital exchanges, intelligent network, ISDN and other	3,791	6,728	19,493	49,898	156.0	380.1
Equipment	79,949	75,154	75,983	71,696	(5.6)	546.2
Advertising	14,857	15,350	15,435	11,547	(25.2)	88.0
International communication services	132,040	139,349	145,222	136,124	(6.3)	1,036.9
Telephone service	121,048	128,228	134,145	123,120	(8.2)	937.9
Leased circuits	5,517	5,693	7,367	9,833	33.5	74.9
Retransmissions	5,475	5,428	3,710	3,171	(14.5)	24.1
Public telephony	52,511	62,941	65,452	64,655	(1.2)	492.5
Data transmission	45,522	43,735	38,642	44,645	15.5	340.1
Mobile services	34,431	46,471	76,494	0	—	—
Other	—	2,391	3,879	4,125	6.3	31.4
Total revenue from operations for Telefónica	1,220,084	1,283,536	1,372,674	1,473,045	7.3	11,221.0
Group						
Telefónica Internacional	18,338	221,451	281,050	331,598	18.0	2,526.0
Telefónica Servicios Móviles	4,108	7,179	35,028	256,384	631.9	1,953.0
Cabitel	16,267	21,373	33,187	40,482	22.0	308.4
Other subsidiaries	140,731	157,894	179,740	211,872	17.9	1,614.0
Sales among group companies	(102,091)	(112,583)	(161,122)	(307,323)	90.7	(2,341.1)
Total revenue from operations for Group Companies	77,353	295,314	367,883	533,013	44.9	4,060.3
Total revenue from operations for Telefónica Group	1,297,437	1,578,850	1,740,557	2,006,058	15.3	15,281.3

(1) Figures in million dollars. 30-12-96 exchange rate: \$ 1 = ptas. 131.275

RESULTS - PROFIT MARGINS. CONSOLIDATED (Million pesetas)

DESCRIPTION	1992	1993	1994	1995	1996	Increase %		1996 \$ (1)
						Over 95	Average accumulated 92-96	
+ Operating revenue	1,208,938	1,297,437	1,578,850	1,740,557	2,006,058	15.3	13.5	15,281.3
- Operating expenses								
Personnel expenses	429,626	448,402	520,918	543,547	554,682	2.0	6.6	4,225.4
Taxes	22,976	23,981	25,826	27,667	35,106	26.9	11.2	267.4
Subcontracts	161,186	184,272	259,656	278,044	433,277	55.8	28.0	3,300.5
+ Internal expenditure capitalized in fixed assets	103,929	109,103	121,391	121,548	127,319	4.7	5.2	969.9
= Operating margin	699,079	749,885	893,841	1,012,847	1,110,312	9.6	12.3	8,457.9
+ Other operating revenue	23,618	33,068	30,226	33,402	37,758	13.0	12.4	287.7
- Depreciation of fixed assets	343,179	374,259	454,530	501,480	526,229	4.9	11.3	4,008.6
- Other operating expenses	13,766	13,152	9,854	9,728	19,307	98.5	8.8	147.1
- Other provisions and charges	18,787	25,816	27,286	25,159	26,569	5.6	9.1	202.4
= Operating profit	346,965	369,726	432,397	509,882	575,965	13.0	13.5	4,387.5
+ Financial income	4,318	7,837	17,358	18,802	19,156	1.9	45.1	145.9
+ Exchange income	363	2,695	4,780	12,685	10,678	(15.8)	132.9	81.3
- Interest expenses	202,300	208,757	205,978	201,151	182,370	(9.3)	(2.6)	1,389.2
- Exchange losses	12,802	28,631	24,642	19,188	20,452	6.6	12.4	155.8
- Amortization of deferred charges	5,810	4,954	5,481	3,317	3,603	8.6	(11.3)	27.4
+ Revenue from associated companies	9,391	20,176	18,513	8,754	7,811	(10.8)	(4.5)	59.5
- Amortization of goodwill	808	4,798	6,191	6,985	16,786	140.3	113.5	127.9
= Profit from ordinary activities	139,317	153,294	230,756	319,482	390,399	22.2	29.4	2,973.9
+ Extraordinary income	10,804	14,904	40,206	29,874	31,941	6.9	31.1	243.4
- Extraordinary expenses	53,201	41,405	99,311	125,645	146,459	16.6	28.8	1,115.7
= Income before tax	96,920	126,793	171,651	223,711	275,881	23.3	29.9	2,101.6
- Corporate tax	13,698	24,845	30,589	39,358	56,921	44.6	42.8	433.6
= Net income	83,222	101,948	141,062	184,353	218,960	18.8	27.4	1,668.0
- Minority interest	2,461	5,581	28,454	51,139	58,678	14.7	121.0	447.0
= Net income attributed to Telefónica	80,761	96,367	112,608	133,214	160,282	20.3	18.7	1,221.0
Net income	83,222	101,948	141,062	184,353	218,960	18.8	27.4	1,668.0
+ Amortization of deferred charges	5,810	4,954	5,481	3,317	3,603	8.6	(11.3)	27.4
+ Depreciation of fixed assets	343,179	374,259	454,530	501,480	526,229	4.9	11.3	4,008.6
+ Dismantled plant pending depreciation	35,355	29,250	48,914	56,210	47,918	(14.8)	7.9	365.0
+ Amortization of goodwill	808	4,798	6,191	6,985	16,786	140.3	113.5	127.9
- Revenue from associated companies	9,391	20,176	18,513	8,754	7,811	(10.8)	(4.5)	59.5
+ Dividends of associated companies	6,267	7,849	7,085	6,766	5,550	(18.0)	(3.0)	42.3
= Cash flow	465,250	502,882	644,750	750,357	811,235	8.1	14.9	6,179.7

(1) Figures in million dollars. 30-12-96 exchange rate: \$ 1 = ptas. 131.275

BALANCE SHEET. CONSOLIDATED (Million pesetas)

ITEMS	1992	1993	1994	1995	1996	1996 \$ (1)
Subscribed shares not paid-in	1	0	23	174	0	0
Fixed assets	3,409,276	3,436,855	3,992,550	4,064,356	4,585,143	34,927.8
Capital increase expenses	503	226	349	714	577	4.4
Net intangible assets	50,778	63,207	300,207	317,239	337,825	2,573.4
Property, plant and equipment	5,303,671	5,483,037	6,311,527	6,538,507	7,024,676	53,511.1
Depreciation of fixed assets	(2,092,440)	(2,310,927)	(2,751,943)	(2,941,081)	(3,050,806)	(23,239.8)
Net fixed assets	3,211,231	3,172,110	3,559,584	3,597,426	3,973,870	30,271.3
Investments	146,764	201,312	132,410	148,977	272,871	2,078.7
Goodwill on consolidation	13,226	48,236	53,741	47,687	49,798	379.3
Deferred expenses	205,811	225,589	186,473	141,310	130,294	992.5
Long-term prepaid taxes	0	14,109	31,230	50,336	70,007	533.3
Current assets	378,838	377,094	495,203	514,395	600,373	4,573.4
Subscribed shares not paid-in	0	22	0	4	0	0
Inventories	18,552	16,505	25,362	29,036	33,834	257.7
Accounts receivable	337,400	332,841	369,798	398,837	505,653	3,851.9
Short-term investments, cash and banks	13,024	19,800	91,007	80,180	48,490	369.4
Prepayments	9,862	7,926	9,036	6,338	12,396	94.4
Assets= liabilities and shareholders' equity	4,007,152	4,101,883	4,759,220	4,818,258	5,435,615	41,406.3
Shareholders' equity (1)	1,392,005	1,437,055	1,512,031	1,546,472	1,863,760	14,197.4
Paid-in share capital	463,480	469,735	469,735	469,735	469,735	3,578.3
Reserves	847,764	894,140	929,688	971,707	1,266,624	9,648.6
Net income for year	80,761	96,367	112,608	133,214	160,282	1,221.0
Interim dividend	0	(23,187)	0	(28,184)	(32,881)	(250.5)
Minority interests (2)	31,044	41,798	292,293	313,753	374,693	2,854.3
Deferred income (3)	58,732	55,326	75,029	91,258	87,486	666.4
Provisions for liabilities and charges (4)	215,796	231,775	270,876	287,996	336,615	2,564.2
Long-term deferred taxes (5)	56,016	57,131	74,447	71,013	83,743	637.9
Long-term debt (6)	1,610,878	1,569,568	1,773,321	1,665,508	1,603,896	12,217.8
Debentures, bonds and promissory notes issued	722,284	708,440	721,323	643,938	654,378	4,984.7
Debt with credit institutions	690,728	681,881	917,607	901,885	843,349	6,424.3
Debt with group and associated companies	18,565	0	217	0	271	2.1
Other creditors	179,301	179,247	134,174	119,685	105,898	806.7
Permanent capital (1+ 2+ 3+ 4+ 5+ 6)	3,364,471	3,392,653	3,997,997	3,976,000	4,350,193	33,138.0
Short-term debt	642,681	709,230	761,223	842,258	1,085,422	8,268.3
Debentures, bonds and promissory notes issued	122,991	167,271	126,360	108,154	147,427	1,123.0
Debt with credit institutions	153,818	87,815	132,339	168,246	244,617	1,863.4
Other creditors	344,153	435,996	469,591	537,275	667,242	5,082.8
Prepayments	21,719	18,148	32,933	28,583	26,136	199.1
Unused credit facilities	136,936	230,639	245,740	334,676	470,513	3,584.2

(1) Figures in million dollars. 30-12-96 exchange rate: \$ 1 = ptas. 131.275

ECONOMIC / FINANCIAL INDICATORS. CONSOLIDATED (Figures in %, unless otherwise indicated)

	1992	1993	1994	1995	1996
Operating margin/Revenue from operations (1)	57.8	57.8	56.6	58.2	55.3
Financial expenses/Revenue from operations (2)	18.3	18.7	15.0	12.8	10.3
Operating margin/Average net plant (3)	22.0	23.5	26.5	28.3	29.3
Fixed asset coverage (4)	91.2	90.1	92.3	91.4	88.9
Self-financing ratio (5)	87.5	115.4	115.9	104.1	96.4
Financial debt ratio (6)	58.4	57.6	54.5	51.6	47.5
Debt repayment capacity(years) (7)	5.1	4.5	3.8	3.1	2.9
Financial expenses coverage (times) (8)	1.0	1.1	1.2	1.5	1.7

(1) Operating revenue - Operating expenses + Internal expenditure capitalized in fixed assets /Operating revenue.

(2) Financial expenses + Exchange losses + Amortization of deferred charges /Operating revenue.

(3) Operating margin /Average net fixed assets.

(4) Shareholders' equity + Outside shareholders' interests + Deferred income + Provisions + Long-term deferred taxes + Long-term debt /Fixed assets + Goodwill on consolidation + Deferred expenses + Long-term prepaid taxes.

(5) Net income - Telefónica Dividends + Minority Interests Dividends + Depreciation of plant and equipment + Intangible depreciation + Dismantled plant pending depreciation + Amortization of goodwill - Revenue from associated companies + Dividend from associated companies/Capital expenditure in fixed assets + Capital expenditure in intangible assets.

(6) Interest bearing debt /Shareholders' equity + Outside shareholders' interests + Deferred income + Long-term deferred taxes + Financial debt - Capital increase expenses - Goodwill on consolidation - Deferred expenses (except promissory note interest).
Interest bearing debt: Long-term creditors - Payments pending on shares + Short-term issue + Short-term debts with credit institutions - Promissory note interest.

(7) Interest bearing debt / Net income + Amortization of deferred expenses + Depreciation of fixed assets + Dismantled plant pending depreciation + Amortization of goodwill - Revenue from associated companies + Dividends from associated companies - Internal expenditure capitalized in fixed assets.

(8) Income before tax + Financial expenses + Exchange losses + Amortization of deferred charges - Internal expenditure capitalized in fixed assets /Financial expenses + Exchange losses + Amortization of deferred charges.

TELEFÓNICA IN THE SPANISH ECONOMY (Telefónica as a % of national total) (Revised series)

	1992	1993	1994	1995	1996
Gross value added	1.97	2.03	2.01	1.97	1.92
Gross operating profit	2.59	2.55	2.36	2.29	2.17
Gross savings	4.26	3.82	4.30	3.58	3.50
Gross capital formation	3.40	3.15	3.18	3.01	2.61
Prices (1)					
GDP deflator	6.8	4.3	4.0	4.9	3.8
Consumer prices (annual average)	5.9	4.6	4.8	4.6	3.6
Telefónica (2)	3.1	3.8	0.0	(1.7)	(1.8)

(1) Growth rates.

(2) Price index variation of basic telephony tariffs.

Sources: I.N.E and Telefónica

GROSS VALUE ADDED (Real growth rates in %)

	1992	1993	1994	1995	1996
National economy	0.4	(0.2)	1.8	3.0	2.2
Services sector	2.4	0.8	2.0	2.5	2.3
Telefónica	9.1	2.9	4.9	7.8	5.2

Sources: I.N.E and Telefónica.

SELECTED FINANCIAL DATA. TELEFONICA DE ESPAÑA (Million pesetas)

	1992	1993	1994	1995	1996	1996 \$ (2)
Revenue from operations	1,154,696	1,220,084	1,283,536	1,372,674	1,473,045	11,221.1
Operating expenses	536,149	547,156	568,199	604,606	719,862	5,483.6
Financial expenses	217,434	235,319	212,639	191,397	165,263	1,258.9
Depreciation and amortization	382,466	406,603	467,274	505,644	474,403	3,613.8
Net income	83,899	84,837	91,734	106,183	120,414	917.3
Cash flow	466,365	491,440	559,008	611,827	594,817	4,531.1
Share capital	463,480	469,735	469,735	469,735	469,735	3,578.3
Shareholders' equity	1,376,751	1,397,712	1,454,684	1,470,679	1,734,072	13,209.5
Long-term debt	1,593,504	1,529,151	1,450,726	1,318,972	1,196,103	9,111.4
Financial debt	1,851,480	1,755,615	1,663,934	1,554,388	1,415,544	10,783.0
Investment (1)	439,391	381,507	406,882	436,720	395,198	3,010.5

(1) Fixed and intangible

(2) Figures in million dollars. 30-12-96 exchange rate: \$ 1 = ptas 131.275

RESULTS - PROFIT MARGINS. TELEFÓNICA DE ESPAÑA (Million pesetas)

DESCRIPTION	1992	1993	1994	1995	1996	Increase %		1996 \$ (1)
						Over year 95	Average accumulated 92-96	
+ Operating revenue	1,154,696	1,220,084	1,283,536	1,372,674	1,473,045	7.3	6.3	11,221.1
- Operating expenses								
Personal expenses	392,736	408,103	421,624	433,655	442,562	2.1	3.0	3,371.3
Taxes	22,260	23,871	25,569	27,055	29,183	7.9	7.0	222.3
Subcontracts	121,153	115,182	121,006	143,896	248,117	72.4	19.6	1,890.1
+ Internal expenditure capitalized in fixed assets	68,920	75,742	73,766	72,154	69,926	(3.1)	0.4	532.7
= Operating margin	687,467	748,670	789,103	840,222	823,109	(2.0)	4.6	6,270.1
+ Other operating revenue	23,346	23,632	24,992	29,610	37,620	27.1	12.7	286.5
- Depreciation of fixed assets	341,903	372,401	413,134	446,480	423,736	(5.1)	5.5	3,227.8
- Other operating expenses	13,252	10,507	11,450	12,550	20,551	63.8	11.6	156.5
- Other provisions and charges	16,769	24,115	22,573	20,383	10,699	(47.5)	(10.6)	81.5
= Operating profit	338,889	365,279	366,938	390,419	405,743	3.9	4.6	3,090.8
+ Financial income	23,074	10,191	14,388	15,693	27,190	73.3	4.2	207.1
+ Exchange income	0	0	0	5,381	4,434	(17.6)	—	33.8
- Interest expenses	199,561	203,124	182,880	171,540	149,295	(13.0)	(7.0)	1,137.3
- Exchange losses	12,411	27,243	24,533	16,903	13,219	(21.8)	1.6	100.7
- Amortization of deferred charges	5,462	4,952	5,226	2,954	2,749	(6.9)	(15.8)	20.9
= Profit from ordinary activities	144,529	140,151	168,687	220,096	272,104	23.6	17.1	2,072.8
+ Extraordinary income	8,148	8,392	29,673	16,262	16,007	(1.6)	18.4	121.9
- Extraordinary expenses	52,953	41,075	88,756	115,229	148,232	28.6	29.3	1,129.2
= Income before tax	99,724	107,468	109,604	121,129	139,879	15.5	8.8	1,065.5
- Corporate tax	15,825	22,631	17,870	14,946	19,465	30.2	5.3	148.2
= Net income	83,899	84,837	91,734	106,183	120,414	13.4	9.5	917.3
+ Amortization of deferred charges	5,462	4,952	5,226	2,954	2,749	(6.9)	(15.8)	20.9
+ Depreciation of fixed assets	341,903	372,401	413,134	446,480	423,736	(5.1)	5.5	3,227.8
+ Dismantled plant pending depreciation	35,101	29,250	48,914	56,210	47,918	(14.8)	8.1	365.1
= Cash flow	466,365	491,440	559,008	611,827	594,817	(2.8)	6.3	4,531.1

(1) Figures in million dollars. 30-12-96 exchange rate: \$ 1 = ptas. 131.275

BALANCE SHEET. TELEFONICA DE ESPAÑA (Million pesetas)

ITEMS	1992	1993	1994	1995	1996	1996 \$ (1)
Fixed assets	3,365,365	3,343,388	3,382,127	3,313,073	3,478,645	26,498.9
Capital increase expenses	359	162	157	117	76	0.6
Net intangible assets	41,609	55,520	70,831	89,426	110,822	844.2
Property, plant and equipment	5,306,956	5,489,734	5,592,518	5,491,583	5,588,247	42,569.0
Depreciation of fixed assets	(2,090,267)	(2,308,229)	(2,483,296)	(2,600,010)	(2,595,993)	(19,775.2)
Net fixed assets	3,216,689	3,181,505	3,109,222	2,891,573	2,992,254	22,793.8
Investments	106,708	106,201	201,917	331,957	375,493	2,860.3
Deferred expenses	203,486	224,113	181,307	135,572	122,554	933.6
Long-term prepaid taxes	0	13,616	30,764	49,699	66,854	509.3
Current assets	348,316	328,977	302,822	336,301	397,612	3,028.8
Inventories	5,019	3,832	4,292	4,303	4,634	35.3
Accounts receivable	329,144	317,323	288,428	313,562	371,257	2,828.1
Short-term investments	6,449	1,201	3,358	11,019	14,615	111.3
Cash and banks	3,789	5,031	4,699	5,375	5,240	39.9
Prepayments	3,915	1,590	2,045	2,042	1,866	14.2
Assets= liabilities and shareholders' equity	3,917,167	3,910,094	3,897,020	3,834,645	4,065,665	30,970.6
Shareholders' equity (1)	1,376,751	1,397,712	1,454,684	1,470,679	1,734,072	13,209.5
Paid-in share capital	463,480	469,735	469,735	469,735	469,735	3,578.3
Reserves	829,372	866,327	893,215	922,945	1,176,804	8,964.4
Net income for year	83,899	84,837	91,734	106,183	120,414	917.3
Interim dividend	0	(23,187)	0	(28,184)	(32,881)	(250.5)
Deferred income (2)	58,723	54,765	67,531	78,933	80,428	612.6
Provisions for liabilities and charges (3)	211,813	216,094	232,412	240,995	272,141	2,073.1
Long-term deferred taxes (4)	52,904	53,003	52,273	44,145	53,084	404.4
Long-term debt (5)	1,593,504	1,529,151	1,450,726	1,318,972	1,196,103	9,111.4
Debentures, bonds and promissory notes issued	696,811	685,614	636,533	571,271	563,464	4,292.2
Debt with credit institutions	602,800	540,494	558,700	496,269	419,505	3,195.6
Debt with group and associated companies	103,586	122,403	140,447	149,319	126,615	964.5
Other creditors	190,307	180,640	115,046	102,113	86,519	659.1
Permanent capital (1+ 2+ 3+ 4+ 5)	3,293,695	3,250,725	3,257,626	3,153,724	3,335,828	25,411.0
Short-term debt	623,472	659,369	639,394	680,921	729,837	5,559.6
Debentures, bonds and promissory notes issued	130,225	167,267	125,094	104,670	117,000	891.3
Debt with credit institutions	127,751	59,197	88,114	130,746	102,441	780.4
Other creditors	344,799	416,078	400,825	420,173	487,483	3,713.4
Prepayments	20,697	16,827	25,361	25,332	22,913	174.5
Unused credit facilities	38,498	126,044	146,991	175,466	274,628	2,092.0

(1) Figures in million dollars. 30-12-95 exchange rate: \$ 1 = ptas. 131.275

ECONOMIC/FINANCIAL INDICATORS. TELEFÓNICA DE ESPAÑA (Figures in % unless otherwise indicated)

	1992	1993	1994	1995	1996
Operating margin/Revenue from operations (1)	59.5	61.4	61.5	61.2	55.9
Financial expenses/Revenue from operations (2)	18.8	19.3	16.6	13.9	11.2
Operating margin/Average net plant (3)	21.5	23.4	25.1	28.0	28.0
Fixed assets coverage (4)	90.7	89.8	88.9	88.9	89.6
Self-financing ratio (5)	91.8	112.2	120.9	123.1	128.6
Financial debt ratio (6)	58.4	57.1	54.7	51.7	45.0
Debt repayment capacity (years) (7)	4.5	4.1	3.4	2.8	2.7
Financial expenses coverage (times) (8)	1.1	1.1	1.2	1.3	1.4

(1) Operating revenue - Operating expenses + Internal expenditure capitalized in fixed assets / Operating revenue.

(2) Financial expenses + Exchange losses + Amortization of deferred charges / Operating revenue.

(3) Operating margin / Average net fixed assets.

(4) Shareholders' equity + Deferred income + Provisions + Long-term deferred taxes + Long-term debt / Fixed assets + Deferred expenses + Long-term prepaid taxes.

(5) Net income - Telefónica Dividends + Depreciation of plant and equipment + Intangible depreciation + Dismantled plant pending depreciation / Capital expenditure in fixed assets + Capital expenditure in intangible assets.

(6) Interest bearing debt / Shareholders' equity + Deferred income + Long-term deferred taxes + Financial debt - Capital increase expenses - Deferred expenses (except promissory note interest). Interest bearing debt: Long-term creditors - Payments pending on shares + Short-term issue + Short-term debts with credit institutions - Promissory note interest.

(7) Interest bearing debt / Net income + Amortization of deferred expenses + Depreciation of fixed assets + Dismantled plant pending depreciation - Internal expenditure capitalized in fixed assets.

(8) Income before tax + Financial expenses + Exchange losses + Amortization of deferred charges - Internal expenditure capitalized in fixed assets / Financial expenses + Exchange losses + Amortization of deferred charges.

SHAREHOLDERS' INFORMATION

SHARE CAPITAL

	1992	1993	1994	1995	1996
Share Capital (Million Ptas.)	463,479.58	469,735.41	469,735.41	469,735.41	469,735.41
Earnings per share (Ptas.)	90.5	90.8	97.6	113.0	128.2
Price / earnings ratio	12.6	20.5	15.9	14.9	23.5
Payout (%)	67.4	68.3	67.6	67.2	69.4
Price / Cash flow per share	2.3	3.6	2.6	2.6	4.8

At December 31, 1996 Telefónica's share capital totalled 469,735,410,000 pesetas, divided into 939,470,820 shares with a nominal value of 500 pesetas each fully paid in.

Since 1990 the following capital increases have been made, all of which through the conversion of bonds.

	Number of shares issued (thousands)	Issue Price (Ptas.)	Amount issued Nominal (Million Ptas.)	Effective (Million Ptas.)
1990	1,994.6	858.435	997.3	1,712.3
1992	1.1	924.750	0.5	1.0
1993	12,511.7	1,267.230 (*)	6,255.8	15,855.2

(*) Average issue price

QUOTATION OF SHARES

Telefónica shares are quoted on the continuous markets of all Spanish Stock exchanges (Madrid, Barcelona, Bilbao and Valencia) and on the following foreign exchanges: London, París, Frankfurt, Tokyo, New York (*) and the London Stock Exchange's SEAQ International.

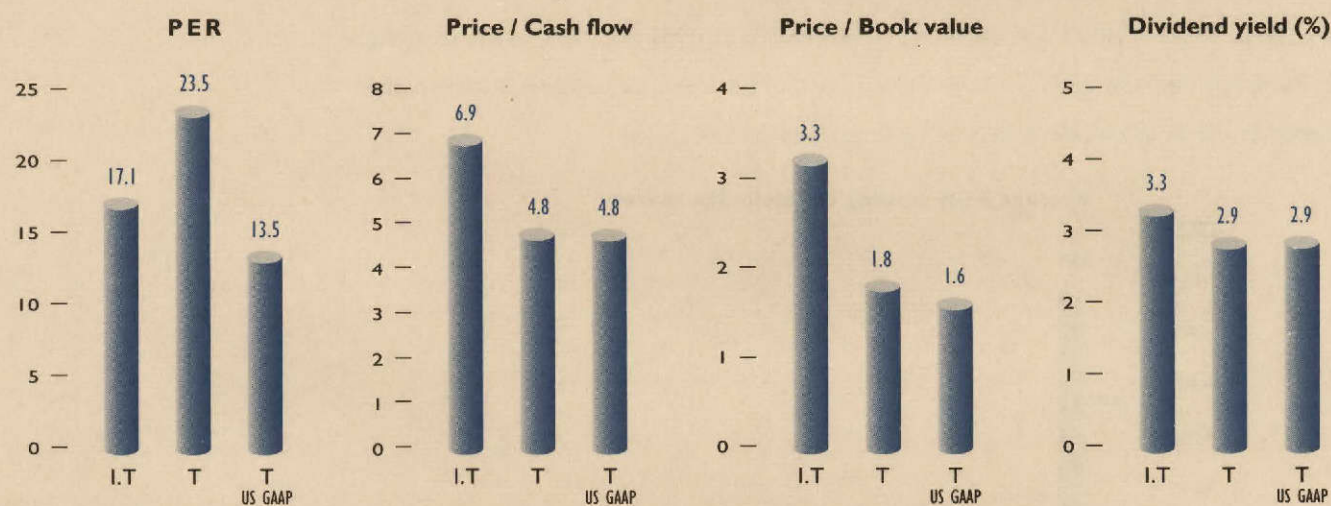
Option contracts on Telefónica shares are carried out on the Spanish Financial Futures Market (MEFF-RV) and on the American Stock Exchange (AMEX) (*)

(*) Quotes American Depositary Receipts (ADR) 1 ADR = 3 shares

QUOTATION OF TELEFÓNICA SHARES

The table below reflects maximum, minimum and closing prices, in pesetas on the continuous Spanish market.

	Maximum	Minimum	Closing
1992	1,300	750	1,140
1993	1,880	1,135	1,865
1994	2,185	1,450	1,555
1995	1,795	1,470	1,680
1996 1 st quarter	2,050	1,690	1,970
1996 2 nd quarter	2,505	1,960	2,360
1996 3 rd quarter	2,445	2,075	2,385
1996 4 th quarter	3,060	2,385	3,015



I.T.: International Telecommunications Index (Source: "Capital International Perspective")

T.: Telefónica (Information in accordance with Spanish accounting principles)

T (U.S. GAAP): Telefónica (Information in accordance with US accounting principles)

International Comparisons at 31-12-96

DIVIDEND POLICY

Telefónica normally pays an interim dividend at year-end and a final dividend once the total dividend for the year has been approved by the Annual General Shareholders' Meeting, following the proposal made by the Board of Directors.

RECENT DIVIDENDS HAVE BEEN:

	1994	1995	1996
Interim	27 ptas.	30 ptas.	35 ptas.
Final	39 ptas.	46 ptas.	54 ptas. (*)
Total	66 ptas.	76 ptas.	89 ptas.

(*) Pending approval by the Annual General Shareholders' Meeting in accordance with the proposed distribution of net income.

STATE PARTICIPATION IN TELEFÓNICA DE ESPAÑA, S.A.

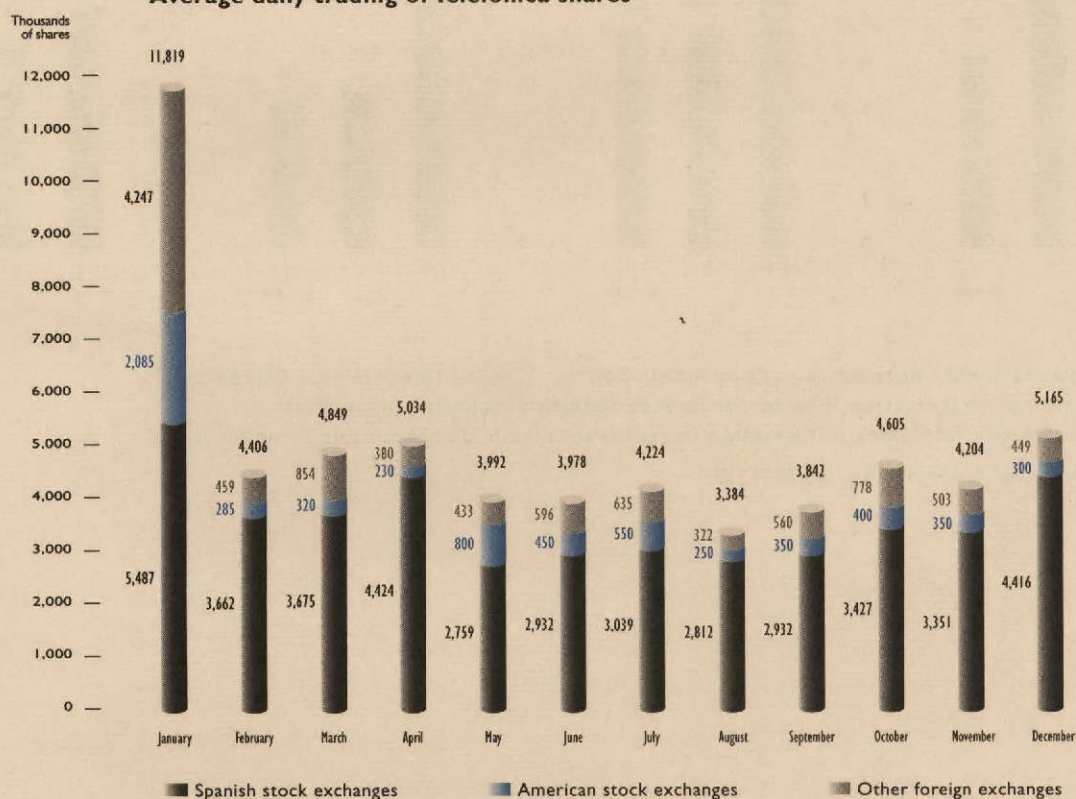
Under the stipulations of the Royal Decree 116/14/2/92, since December 14, 1995, Telefónica's shares are represented as book entries and therefore the official shareholder list has ceased to exist.

The state participation after the Public Offering on February 18, 1997 was stated as the following:

Sociedad Estatal de Participaciones Patrimoniales, S.A. (SEPPa): 0.55% participation in share capital

Sociedad Estatal de Patrimonio II, S.A.: 0.1% participation in share capital

Average daily trading of Telefónica shares



STOCK MARKET CAPITALIZATION

	1992	1993	1994	1995	1996	Average increase% 96/92
Telefónica (billion pesetas)	1,056.7	1,729.8	1,460.9	1,578.3	2,832.5	27.9
Total Madrid Stock Exchange (billion pesetas)	13,332	20,833	20,351	22,899	31,632	24.1
Telefónica's weighting on the Madrid Stock Exchange Index (%)	9.25	9.43	10.44	9.44	11.46	—

TELEFÓNICA GROUP SHARES

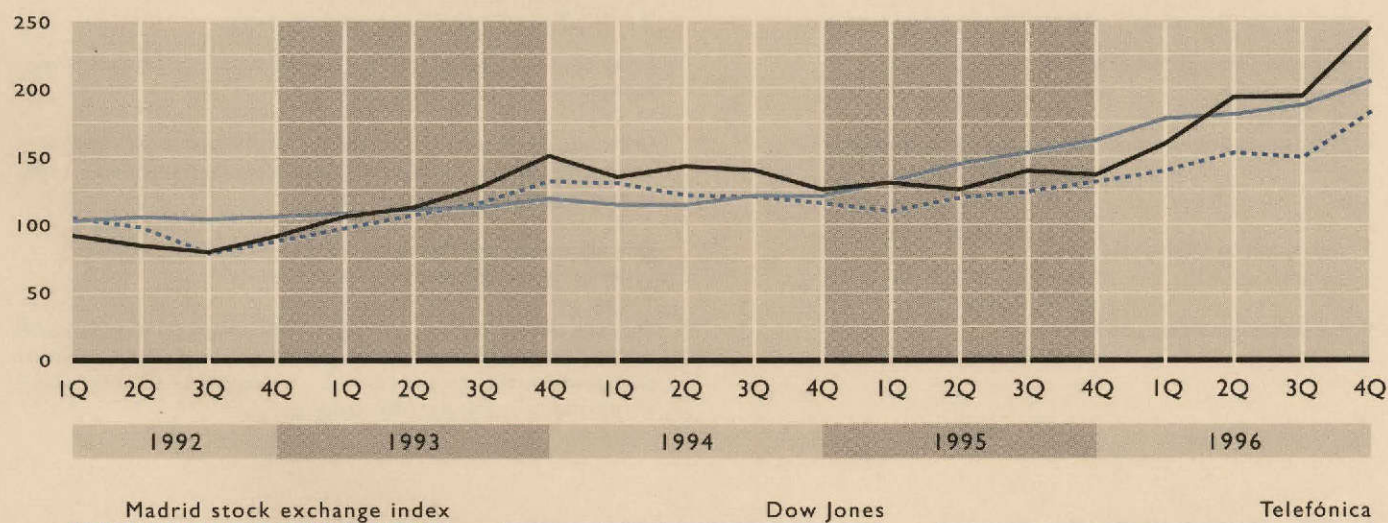
	CTC Chile		CPT Perú		Telefónica Argentina (*)		CANTV(**)	
	1995	1996	1995	1996	1995(I)	1996	1995	1996
Stock market capitalization (million \$US)	4,150	4,923	4,964	4,388	6,365	6,177	—	4,017
Closing price(\$US)	4.88	5.73	2.13	1.88	2.70	2.62	—	4.02
Price/earnings ratio	15.6	13.9	16.4	12.6	13.9	16.0	—	9.3
Price/Cash flow	8.4	7.6	13.7	9.0	6.4	5.8	—	4.4
Dividend yield (%)	3.5	3.2	2.8	3.6(***)	3.8	3.9	—	—

(*) The 1996 figures are based on the quotation of 31/12/1996 and the figures for the financial balance sheet were closed at 30/09/96.

(**) CANTV shares have been quoted on the Caracas Stock Exchange and New York Stock Exchange since November 21, 1996.

(***) 1996 dividend estimated on Company's payout (45%).

Trading index : Telefónica shares



PRELIMINARY RECONCILIATION OF INCOME AND NET WORTH UNDER SPANISH GAAP TO U.S. GAAP

Telefónica's financial statements have been prepared in accordance with Spanish generally accepted accounting principles which differ, in certain respects, from U.S. generally accepted accounting principles (U.S. GAAP).

Since Telefónica has been listed on the New York Stock Exchange since the beginning of 1987, it must present its income and net worth in accordance with U.S. accounting principles. Below we list the main differences between U.S. and Spanish GAAP. The definitive figures, and the supplementary information required under U.S. GAAP, will be detailed in the 20F document to be published before June 30, 1997.

TREATMENT UNDER SPANISH GAAP

1. Property and equipment (see Note 4-e)
2. Intangible assets (see Note 4-d)
3. Deferred exchange differences
 - a) Exchange gains (see Note 4-j)
 - b) Exchange losses (see Note 4-j)
4. Differences in accruals for transactions
5. Capitalized interest (see Note 4-e)
6. Provision for preretirement and early retirement (see Note 4-l)
7. Adjustment for inflation and other
8. Corporate income tax (see Note 4-n)

TREATMENT UNDER U.S. GAAP

Asset restatements are not permitted. Property and equipment and accumulated depreciation must be stated at historical cost.

Research and development expenses are recorded when they arise and cannot be capitalized.

Exchange gains on unmatured transactions must be treated as period revenues.

In view of the foreseeable deregulation of the telecommunications industry in Spain from January 1, 1998, in accordance with Spanish principles, Telefónica wrote off in its financial statements as of December 31, 1995, the potential unrealized exchange losses relating to debts maturing after January 1, 1998. Accordingly, the deferred losses relating to 1997 continued to be recorded as assets as of December 31, 1996. Under U.S. GAAP, these exchange differences cannot be capitalized since Telefónica does not meet the requirements to be deemed to be a regulated entity.

Certain transactions are accrued for differently under Spanish GAAP and U.S. GAAP.

Under U.S. GAAP interest incurred until the start-up of fixed assets must be capitalized.

Under U.S. GAAP, provisions of this type require there to be individual agreements with the employees affected or their representatives in order to be recognized as a period expense.

Only adjustments for inflation at companies located in high-inflation countries can be considered in consolidation.

The taxes relating to timing differences in the recognition of revenues and expenses and the tax benefits relating to tax losses and unused tax credits are recorded in the year, and a provision is recorded for tax credits which are deemed to be unlikely to be recovered.

RECONCILIATION TO U.S. GAAP AS OF 12/31/96
RECONCILIATION OF CONSOLIDATED INCOME AND NET WORTH AS OF DECEMBER 31

	1996	1995
Income for the year under Spanish GAAP	160,282	133,214
Adjustments under U.S. GAAP		
Reversal of depreciation on restated portion of fixed assets	10,673	12,548
Reduction in amount of undepreciated retired plant, due to effect of tangible fixed asset restatements	972	1,159
Single tax on restatement pursuant to Royal Decree Law 7/1996	(6,776)	0
Research and development expenses	(12,054)	(8,387)
Deferred exchange differences	(12,669)	20,983
Transaction accruals	(23)	(505)
Adjustment for inclusion of capitalized interest	(8,469)	(6,351)
Provision for preretirements and early retirements	18,234	20,587
Adjustments for inflation and other	(2,724)	(3,379)
Corporate income tax	57,674	(12,829)
Approximate income for the year under U.S. GAAP	205,120	157,040
Net worth under Spanish GAAP	1,863,760	1,546,472
Adjustments under U.S. GAAP		
Reversal of net effect of restated fixed assets	(103,331)	(114,004)
Reduction in amount of undepreciated dismantled plant, due to effect of tangible fixed asset restatements	57,908	56,936
Effect of restatement pursuant to Royal Decree Law 7/1996	(225,852)	0
Research and development expenses	(62,820)	(50,766)
Deferred exchange differences	(4,124)	8,560
Transaction accruals	(4,069)	(4,046)
Adjustment for inclusion of capitalized interest	127,832	136,300
Provision for preretirements and early retirements	59,087	40,853
Adjustments for inflation and other	(9,065)	(6,068)
Deferred tax due to adjustments under U.S. GAAP	23,999	(33,675)
Approximate net worth under U.S. GAAP	1,723,325	1,580,563

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BOARD OF DIRECTORS

At 31 December, 1996

CHAIRMAN

Juan Villalonga Navarro

VICE-CHAIRMEN

José María Concejo Alvarez

Isidro Fainé Casas

Francisco de Asís Gómez Roldán

DIRECTORS

(representing shareholders)

Eduardo Abril Abadín

Carlos Aragonés Mendiguchía

José Javier Echenique Landiribar

Jorge Fernández Díaz

Pablo Isla Alvarez de Tejera

Antonio Massanell Lavilla

Ramón de Miguel Egea

Cristobal Ricardo Montoro Romero

Pedro Morenés Eulate

José Pedro Pérez-Llorca Rodrigo

Manuel Pimentel Siles

Juan Manuel Rebollo Castrillo

Elvira Rodríguez Herrer

Carles Vilarrubí Carrió

Miguel Zorita Lees

DIRECTORS

(representing government)

Fernando Díez Moreno

Víctor Calvo-Sotelo Ibáñez-Martín

Pedro Ferreras Díez

Víctor Agustín González Muñoz

Adolfo Menéndez Menéndez

SECRETARY GENERAL OF THE BOARD (non Director)

Javier Revuelta del Peral

ASSISTANT SECRETARY (non Director)

Mariano Aldama Magnet

Changes to the Board of Directors of Telefónica de España S. A. after the end of 1996.

During the month of January, 1997, important changes in the Board of Directors took place, as the directors named by the management of State Patrimony (Mssrs. Abril Abadín, Aragonés Mendiguchía, Fernández Díaz, Alvarez de Tejera, de Miguel Egea, Morenés Eulate, Montoro Romero, Perez-Llorca Rodrigo, Pimentel Siles, Rodríguez Herrer y Rebollo Castrillo) and the five Directors representing the government (Mssrs. Gonzalez Muñoz, Díez Moreno, Calvo-Sotelo Ibáñez-Martín, Ferreras Díez y Menéndez Menéndez). At the same time, the deputy secretary of the board, Mariano Aldama Magnet, resigned from his post.

The board members appointed to cover the majority of the vacancies on the Board of Directors were Mssrs. Alierta Izuel, Ariño Ortiz, Ballvé Lantero, Carpio García, Cortina de Alcocer, Larracoechea Jausoro, Perez Sáenz de Buruaga, Revuelta del Peral, Sagardoy Bengoechea and Velasco Gómez. Also, Diego L. Lozano Romeral was named deputy secretary of the Board of Directors.

The membership of the Board of Directors as of the 28th of February, 1997, was as follows:

CHAIRMAN

Juan Villalonga Navarro

VICE-CHAIRMEN

José María Concejo Alvarez

Isidro Fainé Casas

Francisco de Asís Gómez Roldán

MEMBERS

César Alierta Izuel

Gaspar Ariño Ortiz

Pedro Ballvé Lantero

Maximino Carpio García

Alberto Cortina de Alcocer

José Javier Echenique Landiribar

Ignacio Larracoechea Jausoro

Antonio Massanell Lavilla

Juan Perea Sáenz de Buruaga

Juan Antonio Sagardoy Bengoechea

Martín Velasco Gómez

Carles Vilarrubí Carrió

Miguel Zorita Lees

SECRETARY GENERAL OF THE BOARD

Javier Revuelta del Peral

DEPUTY SECRETARY (non Director)

Diego L. Lozano Romeral

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The Board of Directors, at a meeting held on the 29th of January, 1997, agreed to approve the Operating Rules of the Board of Directors of Telefónica de España S. A. . In accordance with these, the Directors of the company have been divided into the following three groups:

a) Directors With Executive Functions in the Company:

Juan Villalonga Navarro

Juan Perea Sáenz de Buruaga

Javier Revuelta del Peral

b) Directors proposed by owners of significant amounts of the company's share capital:

José María Concejo Alvarez

José Javier Echenique Landiribar

Isidro Fainé Casas

Francisco Gómez Roldán

Antonio Massanell Lavilla

Miguel Zorita Lees

c) Independent directors:

César Alierta Izuel

Gaspar Ariño Ortiz

Pedro Ballvé Lantero

Maximino Carpio García

Alberto Cortina de Alcocer

Ignacio Larracoechea Jausoro

Juan Antonio Sagardoy Bengoechea

Martín Velasco Gómez

Carles Vilarrubí Carrió

Executive Committee

At the abovementioned meeting of the Board of Directors on 29 January 1997, the executive committee was reorganized as the delegated governing organ of the Board, comprised of the chairman and seven members:

CHAIRMAN

Juan Villalonga Navarro

MEMBERS

José Javier Echenique Landiribar
Isidro Fainé Casas
Francisco Gómez Roldán
Ignacio Larracoechea Jausoro
Juan Perea Sáenz de Buruaga
Martín Velasco Gómez

SECRETARY

Javier Revuelta del Peral

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Management Committee

The Management Committee of Telefónica de España S.A. and its group of companies is comprised of the following members:

Juan Villalonga Navarro

Chairman of the Management Committee

Rafael Hernández García

General Manager, Retail Client Business

Juan Perea Sáenz de Buruaga

**General Manager of Planning
and Management Control**

Francisco Mochón Morcillo

**General Manager,
International Business**

Andrés Tejero Sala

**General Manager,
Institutional Relations**

Luis Lada Díaz

**Vice president and general manager,
Telefónica Servicios Móviles, S.A.**

Javier Revuelta del Peral

**Secretary General
of the Board of Directors**

Marcial Portela Alvarez

**Managing Director of Telefónica International
de España, S.A.**

Fernando Abril Hernández

General Manager, Corporate Finance

Ignacio de Benito Secades

General Manager, Resources

Guillermo Fernández Vidal

General Manager, Corporate Client Business

Carlos Díaz-Guerra Alvarez

General Manager, Infrastructure

1996 — *Highlights*

January

— Telefónica and the Institute for the small and medium-sized company (IMPI), part of the Ministry of Industry, sign an agreement to provide information to small and medium-sized companies (PYMES). At the same time, the hotel chain, the Paradores and the Education Institution SEK, sign agreements to update and equip these organisms with the most modern telecommunications infrastructures.

— Telefónica and Iberdrola sign an important strategic telecommunications alliance. The agreement includes the creation of a joint venture to provide value-added services and develop diverse activities within the telecommunications sector. It also includes the optimum use of the infrastructure and its application in Latin America. This agreement will take advantage of both companies' customer bases, operating experience, geographic distribution of activities, management of infrastructures and company image.

— Telefónica Móviles' customer portfolio exceeds one million. Annual growth rate now stands



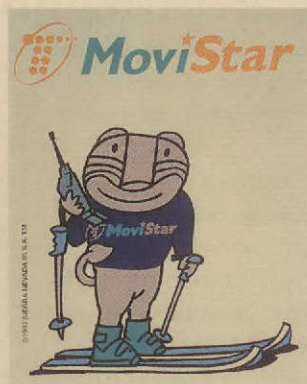
at 135% and penetration index surpasses 2.6%.

— Telefónica Sistemas exports its management system to Argentina. This system will monitor and control the 20,000 public modular telephones distributed throughout the country through Telefónica de Argentina.

February

— Telefónica agrees to provide the Medical Board access to information highways through InfoVía. Likewise Bancb de Santander's home banking system becomes the first interactive system, through InfoVía, to offer access to financial services from the comfort of one's own home. InfoVía currently has 150 Information Provider Centres that can be accessed through this service, making it a multiprovider access service to Internet.

— The Telefónica Group provides the Sierra Nevada 1996 Ski Championships a complete array of global telecommunications services:



voice and data communications, analog and digital GSM mobile telephony, radio-paging, public telephony, special services for journalists and a constant public attention service.

— Telefónica is made the exclusive global telecommunications provider for the intercontinental golf tournament, the «Ryder's Cup», therefore assuring the application of the most modern transmission technology for the coverage of the event.

— Telefónica announces that in the course of 1996 it will invest 71,000 million pesetas in Andalusia, therefore becoming the highest investor in the region.

— The Spanish Commercial Rating Association (AECOC), and Telefónica renew their agreement to operate the EDI AECOM service which is responsible for the development of the most significant technological advances in the increasing of transmission speeds and the development of new communications access routes such as ISDN and InfoVía. AECOM currently embodies the highest number of EDI service users in Spain, growing 300% over the figure for 1995.

— Telefónica Internacional finalizes its entrance into the Argentinian cable TV company MULTICANAL, thereby strengthening the Telefónica

Group's position in the Latin American multimedia sector and complementing its leadership as a telecommunications operator in the area.

March

— Telefónica and Microsoft sign an agreement for the joint development and marketing of their products and services throughout the world. The Company is also granted, through a bidding process, the right to provide the Ministry of Trade and Tourism with its communications network. The Royal Academy of Science agrees to collaborate with Telefónica on the compiling of an electronic edition of scientific and technical vocabulary through Internet and InfoVía.

— The Social Security's General Treasury and its Administrators form an agreement with Telefónica Servicios Avanzados de Información (TSAI) by which this company's electronic mail service Mensatex 400 will be introduced to cover their communications needs: the registering of contributors, TC2, labour related inquiries, etc.

— The new Telefónica Móviles service, Multiasistencia 2424, is created, consequence of the agreement with the European company Multiassistance. This service offers the convenience of a single number attention line through which MoviLine and MoviStar customers can make all types of inquiries.

— Telefónica names Arthur Andersen, Peat Marwick and Price Waterhouse as the external auditors for the Group's companies for the years 1996, 1997 and 1998. These companies have been responsible for the auditing over the past few years. Telefónica has divided its 23 principal subsidiaries into three sub-groups, in order to introduce a rotation system among the three auditing companies previously mentioned.

April

— Telefónica sells Sintel to the North American company Mastec for 4,900 million pesetas.

— The Recoletos Group joins Telefónica Sistemas and Proeinsa in the TeleLine project. TeleLine is an interactive on-line service that offers information, communication, entertainment, and Internet connection services, through the telephone network.

— The Telefónica subsidiary TEMASA is granted, following an open international bidding process, the installation contract for the cable-laying ship «Teneo» to lay the



underwater cable Adria I, that will link Croatia, Albania and Greece. TEMASA is also responsible for the laying of the Barcelona-Savona cable, conceded through an international bidding process.

— Telefónica Móviles presents its Automatic Location of Vehicles and Fleet Management Service, «MoviStar Flotas». This service is specially designed to cover the communication, information and location needs of the transport sector.

May

— Unisource and AT&T join forces in Europe through the creation of a Paneuropean communications and multimedia services company. Likewise, AT&T and Unisource will continue to carry out joint investments in other business ventures in order to enhance their service offer.

— The Peruvian daily newspaper «El Comercio» joins Telefónica Multimedia de Perú to develop cable TV.

— Standard & Poor's, the international rating company, concedes Telefónica an AA long-term rating. This comes as a result of the Company's strong position, combined with the Group's sound financial situation.

— Telefónica and the association for the blind, ONCE, agree to create, in a three-year period, 300 jobs for handicapped people and to

introduce joint projects regarding Tele-employment. This agreement forms part of the Telecommunications Access Plan for Disabled People.

— The Generalitat de Cataluña (the Catalan regional government) and Telefónica sign an agreement regarding the implantation of a corporate network for voice, data and image, integrated into a Network Management Centre. IBM also signs a cooperation agreement with Telefónica regarding InfoVía by which both companies will promote this service.

— The first «TeleSpacio» shop opens in Madrid forming part



of Telefónica's new marketing model by which the Company aims to bring their products and services closer to the customer. TeleSpacio is the first shop of its kind in the world, offering virtual television and remote control systems through InfoVía and Internet.

— Coinciding with the first European conference on Regions and Information Society, the pilot project of a «virtual municipality» is initiated in the town of Villena in Alicante. This project has been

developed by the Generalitat Valenciana (the Valencian regional government) and Telefónica, among others.

June

— Telefónica doubles its access capacity to Internet through a second trunk connection with the US. InfoVía is now the most popular access route through the services offered by more than 80 companies which use this application to maintain contact with their subscribers.

— At the extraordinary meeting held by Telefónica de España's Board of Directors, Juan Villalonga Navarro is named Chairman. Prior to this naming he was responsible for Bankers Trust's activities in Spain and Portugal. Whilst addressing the Board, Mr. Villalonga underlines, among other priorities, the strategies for the immediate future, particularly the intention to increase shareholder value, the high quality service to be provided to all our customers, and the support of the rapid introduction of competition, within an unbiased and transparent regulatory framework.

— Telefónica presents its new type of bill in braille «Validal '96» at an international conference. This bill has been developed with the collaboration of the ONCE, and will accompany the ordinary bill.

— At the XIth World Telecommunications

Conference, held in Seville, and attended by more than 500 telecommunications specialists



from all over the world, the Telefónica Group presents an array of multimedia services and applications through ATM networks, information highways, etc.

— Telefónica appoints the North American investment bank, Morgan Stanley, as the coordinator for its European Medium-Term Notes (EMTN) programme for the European market. CS First Boston, Deutsche Morgan Grenfell, Merrill Lynch and Salomon Brothers among others form part of the initial core dealers for the programme.

— Telefónica Móviles' customers exceed 1,500,000 (1,200,000 with MoviLine, and

310,000 with MoviStar), reflecting 50% growth in the customer portfolio. Telefónica Móviles, Hewlett-Packard and Nokia agree to develop the concept of a "Mobile Office" in Spain, through the marketing of a set considered to be the smallest «office» in the world.

— Lotus and Telefónica sign a strategic agreement to collaborate on the implantation of the «Notes Public Network» platform, aimed at the development of such trends as Tele-employment, Intranets, Webs, etc, within the framework of InfoVía.

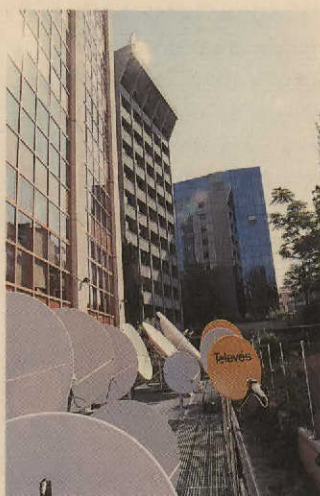
July

— Reuter's and Telefónica Móviles launch a financial information service for GSM customers.

— Telefónica, the Internet Users Association and SEDISI persuade the Internet connection providers to create a neutral domestic interconnection loop that will simplify communications and avoid Internet traffic from extreme ends of the country having to go through international trunks, which are often saturated with traffic and are more expensive for the customer.

— The Spanish Standardization Association (AENOR) approves Telefónica's billing process.

— Telefónica cuts the price of its international calls by an average 13.3%. This price



reduction, combined with that of year-end 1995, represents an overall price cut in international call tariffs of 25%.

— Telefónica and the Anaya group develop the INFOEDUCA service for school children and university students, through the provision of educational, cultural and entertainment-related information, aimed at the education community in general.

— The hotel chain NH and Telefónica sign an agreement



for the incorporation, in hotels, of the most technologically advanced products and services. Likewise, the Spanish

Savings Banks Confederation (CECA) signs a similar agreement with Telefónica, to install these products and services in their offices.

— Telefónica Internacional prepares its entrance into the Brazilian market, through its participation with RBS Participações and the Companhia de Telecomunicações de Chile (CTC) in a consortium that will bid for 35% of the ordinary shares of the Brazilian company Companhia Riograndense de Telecomunicações CRT.

— Telefónica Sistemas de Satélites (TSS) carries out its first commercial transmission in Spain, using a transportable digital ground station, in accordance with the corresponding international regulations.

August

— Telefónica del Perú begins to market the InfoVía service, becoming the second country after Spain, to introduce the information superhighway developed by Telefónica.

— Telefónica Móviles raises the number of countries and service operators through



which it is possible to use MoviStar. This figure now stands at 45 countries and 64 service operators. This has become possible due to open roaming agreements reached with Thailand, Indonesia, the Czech Republic and Taiwan.

September

— Telefónica choses Zaragoza to be the first province to incorporate nine digits in its dialling. This forms part of Telefónica's new Numbering Plan, as proposed to the Government by Telefónica, in accordance with European Union requirements.

— Telefónica, along with Hewlett-Packard, Microsoft and Banco Santander, organize, coinciding with the international cycling race «la Vuelta de España», the "Vuelta Mágica" (the Magic Tour), using a «magic» bus carrying software which enables the inhabitants of different towns and cities to see, for the first time, how to use the new tools to surf in Internet.

— Telefónica and Microsoft sign a joint distribution and promotion agreement to include InfoVía in the operating system of Microsoft Windows 95. The InfoVía user software will be included in the Spanish version of Windows 95 in pre-loaded PCs to be distributed in Spain and Latin America at the beginning of 1997.

— Telefónica Móviles initiates its promotion campaign to extend

the usage of mobile telephony. This campaign will be carried out over the next few months with the cutting of MoviStar Data prices and the night-time retrieving of voice and fax mail, which will now be included in the time band «Free time».

October

— The multimedia Yellow Pages Web site on Internet, produced by Telefónica Publicidad e Información (TPI) receives an award from the IXth Annual Convention of the US Editors of Yellow Pages (YPPA). TPI now has more than 1.5 million companies registered in its directories, both on InfoVía and Internet.

— Nestcape, a leading company in Internet products, signs an agreement with Telefónica Sistemas as the first systems distributor of Intranet applications in Spain and Latin America. Telefónica presents its technological platform for digital television via satellite to the media. Testing also begins through the Hispasat satellite.

— Telefónica Internacional pre-qualifies in the privatization process of Companhia Riograndense de Telecomunicações.

— Telefónica Móviles launches its «MoviStar Dual» service. This is the first time that GSM mobile telephony has offered the possibility for a company and an employee to share the usage of a mobile telephone and a MoviStar card, as the

card distinguishes between business and personal calls, through a code system. New MoviStar discounts are also launched, namely: the Maxisavings and 3-number contracts. The insurance company MAPFRE choses MoviStar for its «Automatic Vehicle Finding» service, Segurmóvil. This service is the first of its kind, combining advanced GPS positioning technology with data transmission using GSM.

— The Telefónica Móviles-owned company, RadioRed, responsible for the marketing of mobile land radiocommunications for closed user groups, is granted four new regional licences for the operating of trunking services, becoming the only operator to provide this public service in the existing twelve zones.

— Paul Smits, of Dutch nationality, takes over the presidency of Unisource from the Spaniard, Francisco Ros who becomes the president of AT&T-Unisource Services, the company which will market AT&T and Unisource's products and services in Europe.

November

— Sogecable and Telefónica agree to dissolve the Strategic Agreement signed in July 1995 regarding cable TV, and to terminate their joint venture in Cablevisión and the local operators. Cablevisión becomes wholly-owned by Sogecable, and the Telefónica Group acquire

the shares previously held by Sogecable and Cablevisión in the local operators.

— Telefónica once again doubles the Internet connection speed with the US, now reaching 16 Megabits. Telefónica Transmisión de Datos, this market's leading operator, provides more than 80% of the Internet connections provided by the 230 Internet Access Providers currently existing in Spain.

— Telefónica Romania, a company in which Telefónica Internacional participates, contests before the Rumanian authorities, the bidding process and subsequent granting of licences for the provision of the cellular telephony GSM service, due to the aforementioned company having been excluded.

— Telefónica and Planeta join forces with the Board of Architects in the launching of the first on-line service for the construction sector, to be provided through the joint company BuildNet S.A.

— The Generalitat Valenciana and the company Camerdata, incorporated by the Spanish Chamber of Commerce, sign strategic collaboration agreements for the implantation, in their different activities, of the most advanced telecommunications services.

— Telefónica Móviles cuts its MoviStar service prices by up to 11%, in the «office-hours»

time band, following an interconnection agreement between Telefónica and Movistar, cutting the prices of calls between mobile and fixed telephones. Movistar and Movistar receive the AENOR quality rating in accordance with international standards.

— Telefónica presents the remodelling of the Telefónica Group, whose Management Committee is made up of 12 members who head the Corporate Centre, five Business Units each with its own profit and loss accounts, and two Resources Units.

— Telefónica Publicidad e Información (TPI) and the Valencian Council, sponsor the El Almudín exhibition in Valencia. The exhibition includes 15 sculptures created by the Basque artist Eduardo Chillida, on loan from Telefónica's art collection, the artist himself and the National Art Museum, Reina Sofía.

December

— Telefónica Internacional wins the bidding process for the



privatization of the Companhia Riograndense de Telecomunicações (CRT). This

operation is of high strategic value for Telefónica Internacional as it completes its expansion in MERCOSUR's natural markets.

— The InfoVía service celebrates its first anniversary with record growth rates: more than 840 Service Information Providers, 215,000 users, 36 million calls received and 10 million connection hours. Telefónica is also pioneering the export of this service to two Latin American countries and is acting as the principal vehicle for the expansion of Internet in Spain.

— The Telefónica Group agrees to invest \$85 million in



the construction of Panamerican Underwater System, which will be operating by August 1998 and will represent the most important network in the linking of the South American countries, in the Pacific and Caribbean seas, with the US and Europe.

— Alcampo and Telefónica create the Virtual Hypermarket, which, through the InfoVía service, will offer a new 24-hour distribution centre, open

7-days a week and offering a delivery service.

— Microsoft and Telefónica announce the joint investment of 500 million pesetas in the expansion of computer-related services and telecommunications among small and medium-sized companies. This project will be based on a marketing strategy through which Spanish companies will be offered solutions in the form of the products, technology and services of both companies.

— Telefónica Móviles intensifies its marketing strategy through the launching of a «super» Christmas offer, consisting of a free gift of a basic Movistar handset and 5,000 pesetas worth of free calls included in the SIM Movistar cards purchased over the Christmas period. The 5,000 pesetas in free calls is deducted from subsequent bills.

— Telefónica receives the direct marketing «Echo Gold Mailbox Award» for InfoVía's launching campaign. This award, given by the Direct Marketing Association, is the most important of its kind worldwide.

Telefónica, Planeta and IBM present their joint launching of a computer «set» aimed at promoting the usage of Internet and InfoVía.

— Barcelona is the scenario for the first Telephone Telecard

International Fair to be held in Spain. This fair is sponsored by Cabitel (Telefónica Group) and the Asociación Coleccionistas Targetes Telefónicas. Cabitel's Card Collectors Club has 2,500 members throughout the world.

— The Spanish Quality Rating Association (AENOR) grades Telefónica's quality system in all the Spanish provinces, in accordance with the international UNE standard. The achieving of this grading forms part of the objectives laid down in the Total Quality Company project initiated by Telefónica in 1992, which includes the whole organization.

— On December 20th, the Cabinet grants authorization to the Dirección General del Patrimonio del Estado to transfer the State's share participation in Telefónica to the Sociedad Estatal de Participaciones Patrimoniales (SEPPA), and the subsequent divestiture of this participation (196,738,320 shares) through a Public Share Offering. This therefore means that the State will no longer participate in Telefónica's share capital nor will it be represented on the Board of Directors.

— On December 20th, the European Union approves Telefónica's incorporation into the Unisource Alliance.

Copies of this Annual Report are available to shareholders at the company's offices. They can also be requested by mail at the following address:

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28020 Madrid

The information required by law is also available to shareholders and to the general public.

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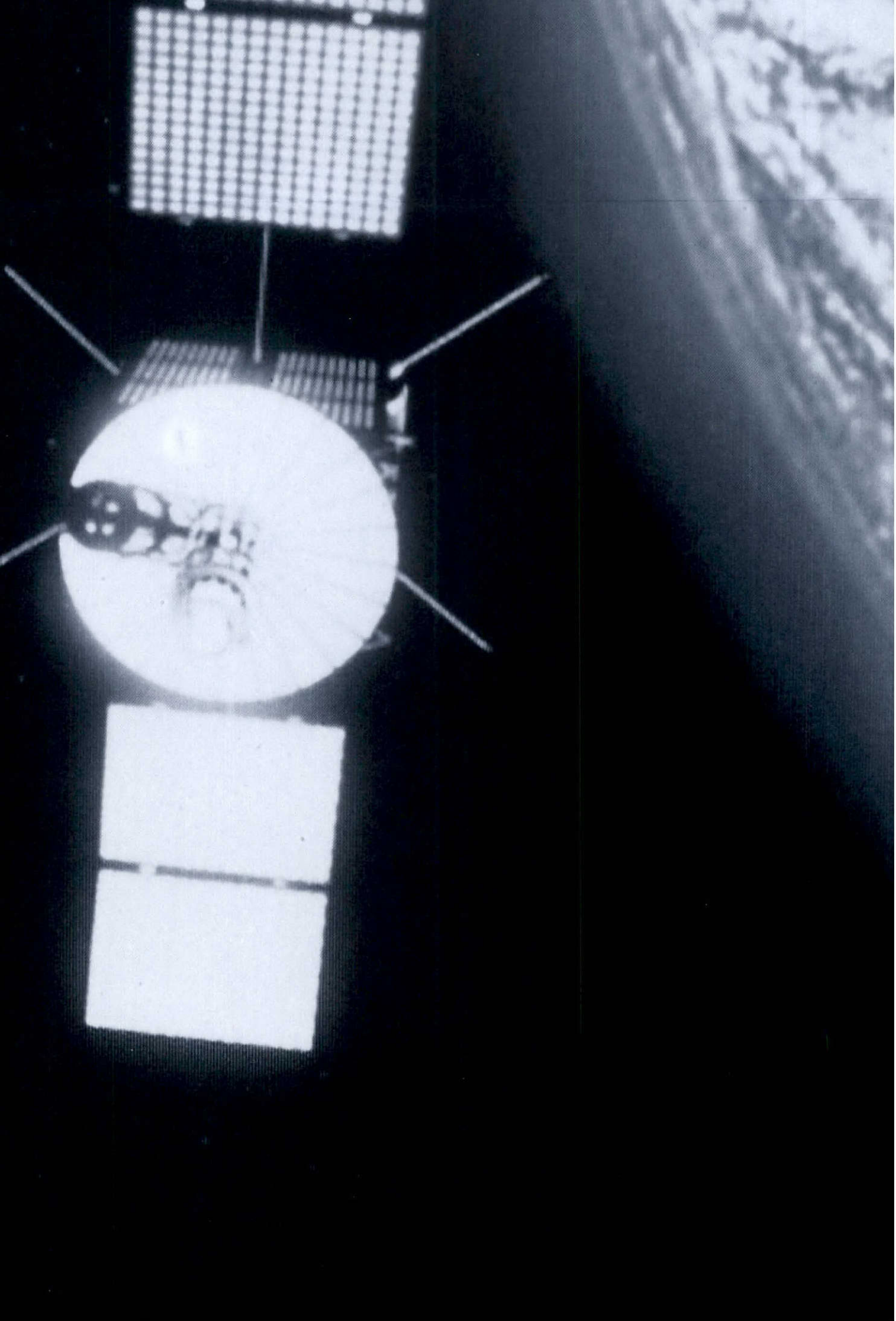
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