

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

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

Risks Relating to Our Business

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

At December 31, 2009, approximately 35.7% of our assets were located in Latin America. In addition, approximately 40.6% of our revenues for 2009 were derived from our Latin American operations. Our operations and investments in Latin America (including the revenues generated by these operations, their market value and the dividends and management fees expected to be received therefrom) are subject to various risks linked to the economic, political and social conditions of these countries, including risks related to the following:

- government regulation or administrative policies may change unexpectedly and negatively affect our interests in such countries;
- currencies may be devalued or may depreciate or currency restrictions and other restraints on transfer of funds may be imposed;
- the effects of inflation or currency depreciation may result in certain of our subsidiaries having negative equity, which would require them to undertake a mandatory recapitalization or commence dissolution proceedings;
- governments may expropriate or nationalize assets or increase their participation in the economy and companies;
- governments may impose burdensome taxes or tariffs;
- political changes may lead to changes in the economic conditions and business environment in which we operate; and
- economic downturns, political instability and civil disturbances may negatively affect our operations.

For instance, throughout 2009 and in the early part of 2010, certain factors affecting the Venezuelan economy have had an impact on the accounting treatment applied with respect to our subsidiaries in that country, notably the level of inflation reached in 2009, the cumulative inflation rate over the last three years, restrictions placed on the official foreign exchange market and the devaluation of the Venezuelan Bolivar fuerte on January 8, 2010. As a result, in accordance with IFRS, Venezuela was considered a hyperinflationary economy in 2009, which has had a series of effects on our consolidated financial statements as of and for the year ended December 31, 2009 and will have additional effects on our consolidated financial statements as of and for the year ended December 31, 2010. A more detailed description of these effects is included in “Item 5. Operating and Financial Review and Prospects—A. Operating Results—Significant Factors Affecting the Comparability of our Results of Operations in the Periods Under Review—Classification of Venezuela as a hyperinflationary economy” and Note 2 to our Consolidated Financial Statements.

In addition, our operations are dependent, in many cases, on concessions and other agreements with existing governments in the countries in which we operate. These concessions and agreements, including their renewal,

could be directly affected by economic and political instability, altering the terms and conditions under which we operate.

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

We are exposed to various types of market risk in the normal course of our business, including the impact of changes in foreign currency exchange rates and the impact of changes in interest rates, as well as the impact of changes of credit risk in our treasury investments (in cash and cash equivalents) or in some of our financial transactions. We employ risk management strategies to manage this exposure, in part through the use of financial derivatives such as foreign currency forwards, currency swap agreements and interest rate swap agreements. If the financial derivatives market is not sufficiently liquid for our risk management purposes, or if we cannot enter into arrangements of the type and for the amounts necessary to limit our exposure to currency exchange rate fluctuations and interest rate fluctuations or if our counterparties fail to deliver on their commitments due to lack of solvency or otherwise, such failure could adversely affect our financial condition, results of operations and cash flow. Also, our other risk management strategies may not be successful, which could adversely affect our financial condition, results of operations and cash flow. Finally, if the rating of our counterparties in treasury investments or in our structured financial transactions deteriorates significantly or if any of such counterparties were to fail in its obligations to us, we may suffer a loss of value in our investments, incur unexpected losses and assume additional financial obligations under these transactions, and such failure could adversely affect our business, financial condition, results of operations and cash flow.

For a more detailed description of our financial derivatives transactions, see “Item 11. Quantitative and Qualitative Disclosures about Market Risk” and Note 16 to our Consolidated Financial Statements.

Adverse economic conditions could reduce purchases of our products and services.

Our business is impacted by general economic conditions and other similar factors in each of the countries in which we operate. The current adverse global economic environment and uncertainty about an economic recovery may negatively affect the level of demand of existing and prospective customers, as our services may not be deemed critical for these customers. Other factors that could influence customer demand include access to credit, unemployment rates, consumer confidence and other general macroeconomic factors. Spanish gross domestic product, or GDP, contracted by 3.6% in 2009 and, according to the Stability Program 2009-2013 forecasts from the Spanish Ministry of Economy, the Spanish economy is expected to remain in recession in 2010, which could have a material adverse effect on our business, financial condition, results of operations and cash flow.

In addition, there could be other possible follow-on effects from the financial crisis on our business, including insolvency of key suppliers or customers. A loss of customers or a reduction in purchases by our current customers could have a material adverse effect on our business, financial condition, results of operations and cash flow and may therefore negatively affect our ability to meet our growth targets.

Existing or worsening conditions in the international financial markets may limit our ability to carry out our business plan.

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

If our ability to generate cash flow were to decrease, whether due to the current worldwide financial and economic crisis or otherwise, we may need to incur additional debt or raise other forms of capital to support our liquidity and capital resource requirements for the ongoing development and expansion of our business.

The current state of the financial markets in terms of liquidity, cost of credit and volatility has improved—compared to the situation in the second half of 2008 and during most of 2009. Nevertheless, there remain several factors that could affect the ordinary performance of financial markets, such as uncertainty about an economic recovery, reorganization of the international banking system, and growing concern over increases in government deficits, among other factors. Worsening conditions in the international credit markets due to any of these factors may make it more difficult and more expensive to refinance our financial debt (of which €8,647 million matures in 2010) or to incur additional debt.

In addition, our capacity to raise capital in the international capital markets would be impaired if our credit ratings were downgraded, whether due to decreases in our cash flow or otherwise. Further, current market conditions may make it more difficult to renew our unused bilateral credit facilities scheduled to expire prior to December 31, 2010 (for an aggregate amount of €2,779 million). The current financial situation may also make it more difficult and costly for us to launch a rights issue to our current shareholders or to raise additional equity capital if further funds were needed for pursuing our business plans.

The successful implementation of our strategy for our mobile operations in Brazil depends on the development of our joint venture company with Portugal Telecom, SGPS, S.A.

Our mobile business in Brazil is conducted through a 50/50 joint venture company, Brasilcel, N.V., or Brasilcel, which is jointly controlled by us and Portugal Telecom SGPS, S.A., or Portugal Telecom. As a result of our less than controlling interest in this joint venture, we do not have absolute control over the operations of the venture. As a result, there is an inherent risk for management or operational disruptions whenever a disagreement between us and our partner arises. Therefore, we must cooperate with Portugal Telecom in order to implement and expand upon our business strategies and to finance and manage the operations of the joint venture. If we do not manage to obtain the cooperation of Portugal Telecom or if a disagreement or deadlock arises we may not achieve the expected benefits from this joint venture, including economies of scale and opportunities to achieve potential synergies and cost savings.

Risks Relating to Our Industry

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

We face significant competition in all of the markets in which we operate, and we are therefore subject to the effects of actions by our competitors in these markets. Our competitors could:

- offer lower prices, more attractive discount plans or better services and features;
- develop and deploy more rapidly new or improved technologies, services and products;
- launch bundle offerings of one type of service with others;
- in the case of the mobile industry, subsidize handset procurement; or
- expand and enhance their networks more rapidly.

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

- greater brand name recognition;
- greater financial, technical, marketing and other resources;
- dominant position or significant market power;
- better strategic alliances;

- larger customer bases; and
- well-established relationships with current and potential customers.

To compete effectively with our competitors, we need to successfully market our products and services and to anticipate and respond to various competitive factors affecting the relevant markets, such as the introduction of new products and services by our competitors, pricing strategies adopted by our competitors and changes in consumer preferences and in general economic, political and social conditions. If we are unable to effectively compete, it could result in price reductions, lower revenues, under-utilization of our services, reduced operating margins and loss of market share, any of which could have a material adverse effect on our business, financial condition, results of operations and cash flow.

We operate in a highly regulated industry, which could adversely affect our businesses.

As a multinational telecommunications company that operates in regulated markets, we are subject to different laws and regulations in each of the jurisdictions in which we provide services. Such laws and regulations are promulgated and enforced to varying degrees by supranational regulators such as the European Union and national, state, regional and local authorities. Regulation may be especially strict in the markets of those countries in which we hold a significant market position. In this respect, regulatory authorities regularly intervene in the retail and wholesale offering and pricing of our products and services. Furthermore, such authorities may also adopt further regulations or take additional actions that could adversely affect us, including revocation of or failure to renew any of our licenses, authorizations or concessions, implementation of changes to the spectrum allocated to us or the granting or new licenses, authorizations or concessions to our competitors to offer services in the relevant markets. Furthermore, regulations could require us to reduce roaming prices and termination rates in mobile and fixed line networks, require us to offer access to our network to other operators, and result in the imposition of fines if we fail to fulfill our service commitments. Such regulations and regulatory actions could place significant competitive and pricing pressure on our operations, and could have a material adverse effect on our business, financial condition, results of operations and cash flow.

In addition, since we hold a leading market share in many of the counties where we operate, we could face regulatory actions by antitrust or competition authorities designed to enhance competition in the relevant markets. These authorities could prohibit us from taking further actions such as making further acquisitions or continuing to engage in particular practices or impose fines or other penalties on us, which, if significant, could result in loss of market share and harm to our financial performance and future growth.

The regulatory landscape in the European Union will change as a consequence of the recent passage of a new common regulatory framework that is to be implemented by Member States before June 2011. We believe based on the principles set forth in such regulatory framework that the regulations adopted by Member States may result in an increased focus on the development and maintenance of competitive markets. This regulatory framework proposes the adoption of measures, under exceptional circumstances and in specific situations, by national authorities to establish functional separation between the retail and wholesale operations of vertically integrated operators with significant market power, by requiring them to offer equal wholesale conditions to related and third party operators. The adoption of such regulatory framework in Spain and the other European Union Members States where we operate could result in requirements to modify our internal organization in the relevant markets, which could result in additional costs to us. Additionally, our industry may face new regulatory initiatives regarding lowering mobile termination rates and the provision of data and audiovisual services.

In addition, we may also face pressure from regulatory initiatives in some European countries in order to reallocate spectrum rights of use and to modify spectrum allocation policies that may result, among other matters, in new tender processes for spectrum allocation in the European Union.

Finally, the recommendation that is being drafted by the European Commission on the implementation of European regulation of new generation broadband networks may reduce the incentives for operators to invest in broadband networks over the short and medium term because operators that invest in broadband networks could be required to provide access to such networks to third parties. This could affect competition and business performance and future growth in such services.

For further information regarding the matters discussed above and other aspects of the regulatory environments in which our businesses operate, see “Item 4. Information on the Company–Business Overview–Regulation”.

We operate under licenses, authorizations and concessions granted by government authorities.

Most of our operating companies require licenses, authorizations or concessions from the governmental authorities of the countries in which they operate. These licenses, authorizations and concessions specify the types of services permitted to be offered by the operating company holding such license, authorization or concession. The continued existence and terms of our licenses, authorizations and concessions are subject to review by regulatory authorities in each country and to interpretation, modification or termination by these authorities. Moreover, authorizations, licenses and concessions as well as their renewal terms and conditions may be affected by political and regulatory factors.

The terms of these licenses, authorizations and concessions granted to our operating companies and conditions of the renewals of such licenses, authorizations and concessions vary from country to country. Although license, authorization and concession renewal is not usually guaranteed, most licenses, authorizations and concessions do address the renewal process and terms, which is usually related to the fulfillment of the commitments that were assumed by the grantee. As licenses, authorizations and concessions approach the end of their terms, we intend to pursue their renewal to the extent provided by the relevant licenses, authorizations or concessions and, under certain circumstances, we will operate under technically expired licenses, authorizations or concessions under preexisting terms during the renewal process. Failure to complete the renewal process successfully could adversely affect our business, financial condition, results of operations and cash flow.

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

For further information regarding the licenses and concessions of our operating companies, see “Item 4. Information on the Company–Business Overview–Regulation”.

The industry in which we operate is subject to rapid technological changes, which requires us to continuously adapt to such changes and to upgrade our existing networks. If we are unable to adapt to such changes, our ability to provide competitive services could be materially adversely affected.

Our future success depends, in part, on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge on a continuous basis and that existing products and technologies will further develop. These new products and technologies may reduce the prices for our existing services or may be superior to, and render obsolete, the products and services we offer and the technologies we use and may consequently reduce the revenues generated by our products and services and require investment in new technology. In addition, we may be subject to competition in the future from other companies that are not subject to regulation as a result of the convergence of telecommunications technologies. As a result, it may be very expensive for us to upgrade our products and technology in order to continue to compete effectively with new or existing competitors. Such increased costs could adversely affect our business, financial condition, results of operations and cash flow.

In particular, we must continue to upgrade our existing mobile and fixed line telephony networks in a timely and satisfactory manner in order to retain and expand our customer base in each of our markets, to enhance our financial performance and to satisfy regulatory requirements. Among other things, we could be required to upgrade the functionality of our networks to accommodate increased customization of services, to increase coverage in some of our markets, or to expand and maintain customer service, network management and administrative systems.

Many of these tasks are not entirely under our control and may be affected by applicable regulations. If we fail to execute these tasks successfully, our services and products may be less attractive to new customers and we may lose existing customers to our competitors, which would adversely affect our business, financial condition, results of operations and cash flow.

Spectrum capacity may become a limiting factor.

Our mobile operations in a number of countries may rely on spectrum availability. Failure to obtain sufficient or adequate spectrum coverage and, to a lesser extent, the costs related to obtaining this capacity could have a material adverse impact on the quality of our services and on our ability to provide new services, adversely affecting our business, financial condition, results of operations and cash flow.

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

We depend upon a small number of major suppliers for essential products and services, mainly network infrastructure and mobile handsets. These suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own shortages and business requirements. Furthermore, these suppliers may be adversely affected by current economic conditions. If these suppliers fail to deliver products and services on a timely basis, our business and results of operations could be adversely affected. Similarly, interruptions in the supply of telecommunications equipment for our networks could impede network development and expansion, which in some cases could adversely affect our ability to satisfy our license terms and requirements.

We may be adversely affected by unanticipated network interruptions.

Unanticipated network interruptions as a result of system failures whether accidental or otherwise, including due to network, hardware or software failures, which affect the quality of or cause an interruption in our service, could result in customer dissatisfaction, reduced revenues and traffic and costly repairs, penalties or other measures imposed by regulatory authorities, and could harm our reputation. We attempt to mitigate these risks through a number of measures, including backup systems and protective systems such as firewalls, virus scanners and building security. However, these measures are not effective under all circumstances and cannot avert every action or event that could damage or disrupt our technical infrastructure. Although we carry business interruption insurance, our insurance policy may not provide coverage in amounts sufficient to compensate us for any losses we may incur.

The mobile industry may be harmed by reports suggesting that radio frequency emissions cause health problems.

Over the last few years, the debate about the alleged potential effects of radio frequency emissions on human health has increased significantly. In many cases, this has hindered the deployment of the infrastructures necessary to ensure quality of service.

Institutions and organizations, such as the World Health Organization (WHO), have stated that exposure to radio frequency emissions generated by mobile telephony, within the limits established, has no adverse effects on health. In fact, a number of European countries, including Spain among others, have drawn up complete regulations reflecting the Recommendation of the Council of the European Union dated July 12, 1999. These add planning criteria for new networks, thus ensuring compliance with the limits on exposure to radio frequency emissions.

Whether or not other research or studies conclude there is a link between radio frequency emissions and health, popular concerns about radio frequency emissions may discourage the use of mobile communication devices and may result in significant restrictions on both the location and operation of cell sites, either or both of which could have a detrimental impact on our mobile companies and consequently on our financial condition, results of operations and cash flow. While we are not aware of any evidence confirming a link between radio frequency emissions and health problems and we continue to comply with good practices codes and relevant regulations, there can be no assurance of what future medical research may suggest.