

TELEFONICA MOBILE INC
Form 20-F
June 23, 2005
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As filed with the Securities and Exchange Commission on June 23, 2005.

SECURITIES AND EXCHANGE COMMISSION

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2004

Commission file number: 1-15158

TELEFÓNICA MÓVILES, S.A.

(Exact name of registrant as specified in its charter)

TELEFONICA MOBILE

(Translation of registrant's name into English)

KINGDOM OF SPAIN

(Jurisdiction of incorporation or organization)

Goya, 24

28001 Madrid, Spain

(Address of principal executive offices)

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

Title of each class	Name of each exchange on which registered
Ordinary Shares, nominal value 0.50 per share* American Depositary Shares, each representing one Ordinary Share	New York Stock Exchange New York Stock Exchange

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

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

None

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

None

The number of outstanding shares of each class of stock of Telefónica Móviles, S.A. as of the close of the period covered by this annual report was:

Ordinary Shares, nominal value 0.50 per share: 4,309,104,934

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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PRESENTATION OF FINANCIAL INFORMATION

In this annual report, references to dollars, US\$ or \$ are to United States dollars. References herein to euro or are to the single currency of participating member states in the Third Stage of the European and Economic Monetary Union, including Spain, pursuant to the treaty establishing the European Community, as amended from time to time. Our consolidated and combined financial statements and the notes to our consolidated and combined financial statements are presented in euro. The Telefónica Móviles Group previously reported some of this information in Spanish pesetas.

FORWARD-LOOKING STATEMENTS

This annual report contains statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, Section 21E of the Securities Exchange Act of 1934 and the Safe Harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. These statements appear in a number of places in this annual report and include statements regarding our intent, belief or current expectations with respect to, among other things, trends affecting our business, financial condition and results of operations.

Such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and actual results may differ materially from those in the forward-looking statements as a result of various factors. The accompanying information contained in this annual report, including, without limitation, the information discussed in:

Item 3.D Risk Factors ,

Item 4. Information on the Company ,

Item 5. Operating and Financial Review and Prospects , and

Item 11. Quantitative and Qualitative Disclosures About Market Risk

identify important factors that could cause such differences. Readers are cautioned not to place undue reliance on those forward-looking statements, which speak only as of the date hereof. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

CERTAIN TERMS AND CONVENTIONS

When we use first person, personal pronouns in this report, such as we, us, or our, or the term Group, we mean Telefónica Móviles, S.A. and its consolidated operating companies, unless otherwise indicated or the context otherwise requires.

PART I

Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

Table of Contents**Item 3. KEY INFORMATION****A. SELECTED FINANCIAL DATA**

The following summary selected financial data should be read together with the Item 5. Operating and Financial Review and Prospects and our consolidated and combined financial statements included in this annual report. Our consolidated financial statements for the years ended and at December 31, 2003 and 2004 and our combined financial statements for the year ended at December 31, 2002 have been prepared in accordance with Spanish GAAP, which differs in certain significant respects from U.S. GAAP. See note 21 to our consolidated and combined financial statements. The principles of consolidation are described in note 2(c) to our consolidated and combined financial statements.

Summary Selected Financial Data

	Year ended December 31,				
	2000	2001	2002	2003	2004
(euro in thousands, except per share and ADS data)					
Statement of Operations Data					
<i>Spanish GAAP</i>					
Net revenues from operations	6,377,249	8,411,064	9,139,835	10,070,284	11,827,591
Other revenues	110,622	147,747	91,070	152,403	217,270
Services and goods purchased	(1,559,181)	(1,862,117)	(2,406,039)	(2,592,541)	(3,676,302)
External services and local taxes	(2,277,186)	(2,603,758)	(2,412,370)	(2,581,995)	(3,040,952)
Personnel expenses	(270,696)	(533,831)	(546,381)	(485,993)	(539,917)
Depreciation and amortization	(871,137)	(1,258,159)	(1,316,406)	(1,420,648)	(1,611,003)
Change in operating provisions	(129,284)	(225,416)	(130,245)	(99,274)	(86,723)
Total operating expenses	(5,107,484)	(6,483,281)	(6,811,441)	(7,180,451)	(8,954,897)
Operating income	1,380,387	2,075,530	2,419,464	3,042,236	3,089,964
Amortization of goodwill	(26,420)	(53,802)	(87,096)	(101,703)	(94,708)
Income (losses) of associated companies	(94,701)	(119,193)	(159,477)	(80,656)	(38,232)
Financial expense	(304,471)	(714,869)	(921,983)	(1,288,474)	(925,718)
Financial income	109,607	386,810	605,787	910,337	571,950
Income from ordinary activities	1,064,402	1,574,476	1,856,695	2,481,740	2,603,256
Extraordinary income (expense)	(51,241)	(100,705)	(12,075,902)	(4,536)	(92,949)
Corporate income tax	(347,872)	(628,768)	2,130,821	(890,493)	(898,117)
Minority interests	(20,518)	48,352	4,363,987	21,127	21,720
Net income (loss)	644,771	893,355	(3,724,399)	1,607,838	1,633,910
Earnings (loss) per share	0.18	0.22	(0.87)	0.37	0.38
Average outstanding common shares	3,560,966,298	4,141,432,815	4,290,372,979	4,309,104,934	4,309,104,934
<i>U.S. GAAP</i>					
Net income (loss)(1)	683,982	301,249	(3,644,742)	1,818,096	1,621,681
Earnings (loss) per share	0.19	0.07	(0.85)	0.42	0.38

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Average outstanding common shares 3,560,966,298 4,141,432,815 4,290,372,979 4,309,104,934 4,309,104,934

At December 31,

	2000	2001	2002	2003	2004
(euro in thousands)					
Balance Sheet Data					
<i>Spanish GAAP</i>					
Property, plant and equipment, net	3,820,869	5,244,414	4,661,729	4,384,354	5,639,994
Total assets	21,260,624	24,914,086	16,231,714	15,664,065	23,570,914
Short-term debt(2)	4,707,849	6,615,828	991,596	1,776,063	2,676,040
Long-term debt(3)	3,007,622	5,279,338	7,213,809	5,368,594	8,448,088
Total liabilities	15,941,284	17,425,434	12,984,131	11,623,630	18,851,021
Shareholders' equity	5,319,340	7,488,652	3,247,583	4,040,435	4,719,893
<i>U.S. GAAP</i>					
Total assets(4)	20,297,852	27,909,248	16,460,021	14,923,924	22,221,036
Long-term debt(4)	2,414,881	5,593,197	6,867,368	5,115,572	8,124,892
Shareholders' equity(4)	8,053,329	9,580,469	4,114,534	4,709,053	5,001,850

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	At December 31,				
	2000	2001	2002	2003	2004
Other Financial Data					
<i>Spanish GAAP</i>					
Cash flow from operating activities	5,594,426	1,332,485	2,156,756	3,681,481	3,931,355
Cash flow from investing activities	(12,057,634)	(4,038,059)	(1,756,219)	(1,155,113)	(5,968,007)
Cash flow from financing activities	6,455,915	281,834	(314,348)	(2,612,128)	2,217,288
Capital expenditures	13,620,172	2,141,210	1,046,596	834,879	1,397,317
Cash dividends	851,616			767,760	795,955

Operating Data

	(in millions)				
Population in licensed service territories	285	372	353	389	509
Total customers ⁽⁵⁾	19.2	28.0	39.4	49.6	74.4
Proportionate customers ⁽⁶⁾	16.7	24.6	28.6	32.9	53.6
Pre-paid customers ⁽⁷⁾	64%	69%	71%	72%	74%

- (1) Net income under U.S. GAAP as of December 31, 2003, 2002, 2001 and 2000 has been restated as a consequence of the effect of the acquisition of Telefónica Móvil de Chile from an entity under common control with us on July 23, 2004. See Note 21-6(g) to our consolidated financial statements.
- (2) Consists of short-term debt payable to banks and other financial institutions, short-term marketable debt securities and short-term debt payable to Telefónica Group companies. Short-term debt excludes interest payable and trade payables.
- (3) Consists of long-term debt payable to banks and other institutions, long-term debt payable to Telefónica Group companies and as of December 31, 2001 long-term debt incurred in connection with the acquisition of UMTS licenses included under Other liabilities on our consolidated and combined balance sheet.
- (4) Shareholders' equity, total assets and long-term debt under U.S. GAAP as of December 31, 2003, 2002, 2001 and 2000 has been restated as a consequence of the effect of the acquisition of Telefónica Móvil de Chile from an entity under common control with us on July 23, 2004. See Note 21-6(g) to our consolidated financial statements.
- (5) Represents total number of customers of all companies in which we have an interest, including subsidiaries, companies carried by the equity method and other companies carried as an investment. As of December 2002 we also include Brasilcel's customers. As of December 2003, we also include TCO's customers. For the year ended December 31, 2004, we also include Telefónica Móviles Chile's customers and those of the companies acquired from BellSouth during 2004.
- (6) Represents total number of customers of all companies in which we have an interest multiplied by our economic ownership interest in those companies.
- (7) Represents total pre-paid customers as a percentage of total customers at period-end.

Exchange Rate Information

Effective January 1, 1999, the following 11 European Union member states adopted the euro as a common currency: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Portugal and Spain. They also established fixed conversion rates between their respective sovereign currencies and the euro. On January 1, 2001, Greece joined the European Economic and Monetary Union. The exchange rate at which the Spanish peseta has been irrevocably fixed against the euro is 166.386 = 1.00. On January 1, 2002, the participating member states began issuing new euro-denominated bills and coins for use in cash transactions. As of March 1, 2002, the participating member states have withdrawn the bills and coins denominated in their respective currencies from circulation, and they are no longer legal tender for any transactions.

The Noon Buying Rate for the euro on June 20, 2005 was \$1.00 = 1.2140.

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

Year ended December 31,	Noon Buying Rate			
	Period End	Average(1)	High	Low
2000	0.9388	0.9207	1.0335	0.8270
2001	0.8901	0.8909	0.9535	0.8370
2002	1.0485	0.9495	1.0485	0.8594
2003	1.2597	1.1411	1.2597	1.0361
2004	1.3538	1.2478	1.3625	1.1801

Source: Federal Reserve Bank of New York.

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

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Month ended	High	Low
November 30, 2004	1.3288	1.2703
December 31, 2004	1.3538	1.3224
January 31, 2005	1.3476	1.2954
February 28, 2005	1.3274	1.2773
March 31, 2005	1.3465	1.2877
April 30, 2005	1.3093	1.2819
May 31, 2005	1.2936	1.2349
June 20, 2005	1.2320	1.2035

Source: Federal Reserve Bank of New York.

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

Our ordinary shares are quoted on the Spanish stock exchanges in euro. Currency fluctuations may affect the dollar equivalent of the euro price of our shares listed on the Spanish stock exchanges and, as a result, the market price of our ADSs, which are listed on the New York Stock Exchange. Currency fluctuations may also affect the dollar amounts received by holders of ADSs on conversion by the Depositary of any cash dividends paid in euro on the underlying shares.

Our consolidated results are affected by fluctuations between the euro and the currencies in which the revenues and expenses of our consolidated subsidiaries are denominated, principally the Brazilian real, the Argentine peso and the Mexican peso. See Item 11. Quantitative and Qualitative Disclosures About Market Risk.

B. CAPITALIZATION AND INDEBTEDNESS

Not applicable.

C. REASONS FOR THE OFFER AND USE OF PROCEEDS

Not applicable.

D. RISK FACTORS**Risks Related to Our Business**

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 our markets, typically from at least two other wireless providers, and increasingly from multiple providers, including some of the leading global wireless operators. Governmental authorities in some countries also continue to auction or sell additional bands of spectrum for wireless use and to grant licenses and concessions to new entrants, which will create new competitors in some of our markets.

In addition to other wireless providers, we experience competition from fixed-line telephone companies and, to an increasing extent, from the cable, utility, paging, internet and satellite industries. We expect that competition will continue to intensify in all of our existing markets, both from existing competitors and new entrants. These competitors could:

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

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provide increased handset subsidies;

bundle offerings of fixed-line telephone services with other services;

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

expand and enhance their networks faster.

The wireless communications industry has been experiencing significant consolidation, and we expect that this consolidation trend will continue. Acquisitions, mergers or joint ventures have created large, well-capitalized competitors with substantial financial, technical, marketing and other resources to compete with our service and product offerings.

We expect competition among wireless providers, including new entrants, to continue to drive prices for services and handsets lower. In addition, portability requirements, which enable customers to switch wireless providers without changing their wireless telephone numbers, have been introduced in some of the markets in which we operate and may be introduced in other markets in the future. All of these developments could lead to greater movement of customers among competitors, known as customer churn, which could increase our marketing, distribution and administrative costs, slow growth in customers and reduce revenues. Our market position will also depend on effective marketing initiatives and on our ability to anticipate and respond to various competitive factors affecting the industry, including new services, pricing strategies by competitors, changes in consumer preferences and economic, political and social conditions. Any material failure by us to compete effectively or any aggressive competitive behavior by our competitors in pricing their services or acquiring new customers would have a material adverse effect on our revenues and overall results of operations.

Our acquisition of BellSouth's wireless operations in Latin America and Telefónica Móvil de Chile, may require us to increase our capital resources and financing requirements.

On March 5, 2004 we entered into a stock purchase agreement with BellSouth Corporation, or BellSouth, to acquire 100% of BellSouth's interests in its wireless operations in Argentina, Chile, Peru, Venezuela, Colombia, Ecuador, Uruguay, Guatemala, Nicaragua and Panama. The acquisitions were completed in October 2004 and January 2005. The total acquisition cost for our interest in the companies purchased from BellSouth and minority shareholders in 2004, adjusted by the net debt of the companies purchased at closing and following certain additional post-closing adjustments, amounted to \$3,248.6 million. The total acquisition cost for the companies purchased from BellSouth in 2005, adjusted by the net debt of the companies purchased, amounted to \$836.6 million. In addition, on May 18, 2004, the board of directors of Telefónica CTC Chile, S.A. accepted our binding offer for the purchase of 100% of the shares of its subsidiary, Telefónica Móvil de Chile, S.A., which was completed on July 23, 2004 for a total acquisition cost of \$869.9 million.

We financed these acquisitions through cash generated by our operating activities and loans from Telefónica S.A., our controlling shareholder. In addition to the financing required for these acquisitions, our capital resource requirements may increase as a result of the upgrades (including, in some cases, significant technological upgrades) to and the integration of the networks of these newly acquired operators. We may be required to further increase our debt or divert funds from our existing operations to invest in our new acquisitions, which could have a material adverse effect on our revenues and overall results of operations.

The acquisition and integration of new operators may be costly, difficult and time consuming.

We may face technological, administrative and other challenges involved in integrating new operators that we acquire, including the operators we acquired as part of our acquisition of BellSouth's wireless operations in Latin America and Telefónica Móvil de Chile. In addition, we may face similar challenges in integrating new services and technologies into our existing networks and operations from operators we acquire. Any failure to expand and improve our service and product offerings in these operators may place us at a competitive disadvantage relative to other wireless communications providers. Customers may choose these competitors over us, which could adversely affect our ability to increase our revenues and leverage our cost base.

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We may require substantial capital resources in order to meet existing obligations under our licenses and continue to develop and expand our business.

The operation, expansion and upgrade of our networks, as well as the marketing and distribution of our services and products, require substantial financing. Achieving the minimum coverage requirements under our licenses could require additional financing. Any failure to satisfy our substantial liquidity and capital resource requirements would impede our ability to take advantage of promising but capital-intensive opportunities in our industry. In addition, our results of operations may be negatively affected if we are unable to upgrade our networks or respond to competitive initiatives of competitors that may be less capital-constrained.

We depend in large measure on the Telefónica Group for our liquidity and capital resource requirements.

Historically, we have relied, in large measure, on the Telefónica Group to satisfy our liquidity and capital resource requirements through loans and from time to time capital contributions. As of December 31, 2004, our total debt was 11,124 million, of which 9,615 million was owed to other members of the Telefónica Group. In the future, we may be required to incur additional indebtedness to support the ongoing development and expansion of our business. We plan to continue to rely upon Telefónica, S.A. and other Telefónica Group companies to satisfy most of these requirements. If Telefónica, S.A. or other members of the Telefónica Group are unable to provide us with funding, we may need to raise debt from other sources to support the ongoing development and expansion of our business.

Increased levels of debt could have negative effects on our company, including:

higher debt-service costs that adversely affect our results of operations;

allocation of increasing amounts of cash flow for debt service;

increased difficulty in obtaining future financing;

reduction of any credit ratings issued by rating agencies in respect of any debt we may issue in the future;

restrictions on our company's capital resources or operations imposed by lenders; and

reduced flexibility to take advantage of, or pursue, other business opportunities.

There may be insufficient demand for the new products and services we have invested in and developed.

As an element of our strategy, we have invested in and developed new wireless services, such as wireless internet and data services. In order for our customers to better access these services, we will need to upgrade our customer base with new handsets compatible for UMTS services in

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some countries and enabled with MMS, cameras, color screens, and other capabilities. The handsets needed to support these services may increase our cost base while demand for these data services and products may not materialize. We cannot assure you that demand for these services will be as high as expected, or that these initiatives will be profitable. If they are not, our growth could be impaired and we could lose our capital investments in these new services. These initiatives could fail for a number of reasons, such as technological developments or competitive factors. Our ability to introduce new services also depends on whether and on what terms new services are permitted by applicable regulations.

Our ability to deploy and deliver some of the new services is dependent upon new technologies. These technologies may not be developed in a timely manner or, if developed, may not perform as expected or favorably in comparison to competing technologies, which could negatively affect customer demand. In addition, we may not be able to deliver these services on an economic basis, particularly in comparison to competing technologies.

We could lose customers and revenues if we fail to upgrade our existing networks.

We must continue to upgrade our existing wireless networks on a timely and satisfactory basis in order to retain and expand our customer base and to provide an adequate and updated portfolio of products and services in each of our markets. Among other things, we must:

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

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fill in coverage gaps and increase capacity in some of our markets;

expand and maintain customer care, network management and administrative systems; and

upgrade our systems to maintain our competitiveness and adapt them to new technologies which become available.

We cannot assure you that we will be able to execute successfully all of these tasks, many of which are not entirely under our control, on a timely basis or at all. If we fail to successfully execute these tasks, we also may be less attractive to new customers and lose existing customers to our competitors, which would adversely affect our revenues and overall results of operations.

Our business could be adversely affected if major suppliers fail to provide us with needed equipment and services on a timely basis.

Although we have not been materially affected by supply problems in the past, handsets and network infrastructure suppliers may, among other things, extend delivery times, raise prices and limit supply due to their own shortages and business requirements. If these suppliers fail to deliver products and services on a timely basis, or fail to develop and deliver to us handsets that satisfy our customers' demands, we could be negatively affected. Similarly, interruptions in the supply of telecommunications equipment for our networks could impede network development and expansion.

The development of our business could be hindered if we fail to maintain satisfactory working relationships with our partners, especially Portugal Telecom, our joint venture partner in Brasilcel.

Some of our operations, such as Brasilcel, our co-managed joint venture with Portugal Telecom in Brazil, are conducted through joint ventures in which we do not have absolute control over the operations of the venture.

Neither Portugal Telecom nor we exercise full control over the Board of Directors or executive team. Each of the shareholders has equal ownership and jointly controls the joint venture, each appointing half of the members of the Brasilcel Board of Directors. Significant financial and operating decisions require Board approval, and all strategic decisions need to be approved by the Board of Directors. Furthermore, Portugal Telecom is entitled to appoint the Vice-Chairman of the Board and nominate the Chief Executive Officer of the joint venture while we are entitled to appoint the Chairman of the Board and nominate the Chief Financial Officer.

In other cases where we own a majority of a venture, we may still be subject to provisions in shareholders' agreements restricting our control over the venture. The particular corporate governance provisions affecting our company vary from venture to venture, and often depend upon the size of our investment relative to that of other investors, our experience as a wireless operator compared to that of other investors and the preferences or requirements of foreign governments that local owners hold an interest in licensed telecommunications operators.

We face risks associated with litigation.

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We are party to lawsuits and other legal proceedings in the ordinary course of our business. An adverse outcome in, or any settlement of, these or other lawsuits could result in significant costs to us. In addition, we may be required to devote substantial time to these lawsuits, time which we could otherwise devote to our business. For a more detailed description of these lawsuits, see Item 8.A Consolidated Statements and Other Financial Information Legal Proceedings.

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Risks Related to Our Organizational Structure

We have recently undertaken a series of major initiatives and actions which will materially affect comparability of historical and future financial performance and which may not be fully captured in our historical financial statements included in this annual report.

In order to achieve our overall strategy of enhancing our position as one of the leading global wireless operators and achieving superior growth and profitability, we took several major initiatives during 2002, 2003, 2004 and early 2005. These initiatives and actions include, among others, the following:

the acquisition of BellSouth's wireless operations in Latin America (2004-2005);

the acquisition of 100% of Telefónica Móvil de Chile (2004);

the increase in our ownership interest in our Brazilian operations (2000-2005);

the acquisition by Brasilcel of a controlling interest in Tele Centro Oeste Participações (2003);

the consummation of Brasilcel N.V., our joint venture with Portugal Telecom in Brazil (2002);

the increase in our ownership interest in our Central American operations (2002); and

the acquisition by us of four wireless operators in Mexico (2001) and the acquisition by us of a 65% interest in the Mexican wireless operator Pegaso Telecomunicaciones, S.A. de C.V. and its integration with our Northern Mexican operations (2002).

The transactions that had not been consummated by December 31, 2004 are not reflected in our consolidated financial statements at all. All of these items will affect the comparability of our historical and future results of operations and financial condition. For further information on the items described above please see Item 5A. Operating Results Basis of Presentation Events Affecting Comparability of Historical and Future Results of Operations and Financial Condition. We anticipate that future results of operations and financial condition will be different from our results of operations and financial condition reflected in our consolidated financial statements, after taking into account these developments and any other future material developments.

We are controlled by Telefónica, S.A., whose interests may conflict with those of our company.

Telefónica, S.A. currently owns, directly or indirectly, approximately 92.5% of our shares and controls our company. As a result, Telefónica, S.A. has the power to determine the composition of our board of directors and to influence major business and corporate decisions, including, for example, extraordinary corporate transactions, strategic initiatives and dividend policy. Telefónica, S.A. also is able to direct our day-to-day management and operations.

The Telefónica Group could have conflicts of interest in business transactions with us, or take advantage of business opportunities otherwise available to us, which could reduce our revenues or increase our costs.

We regularly enter into business transactions and contractual arrangements with companies in the Telefónica Group and plan to continue to do so. Although we believe that prior and existing transactions and arrangements have been fair to us in all material respects and that their terms have reflected market conditions, it is possible that in some instances we could have obtained better terms from third parties. We could also face competition from other companies within the Telefónica Group that are not part of our company. Consequently, we could be impeded from pursuing some future business opportunities or obligated to pursue them in conjunction with other companies in the Telefónica Group. Because Telefónica, S.A. is a party to business transactions and contractual arrangements with our company and companies of the Telefónica Group are active in businesses that overlap with ours, there is potential for conflicts of interest between Telefónica, S.A. and its affiliates, on the one hand, and our company and subsidiaries, on the other, in circumstances where our interests and those of Telefónica, S.A. are not aligned.

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

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

Applying these standards to our financial statements will imply a change in the presentation of our financial information, since the financial statements will include more components and additional disclosure will be required. Additionally, there will be a change in the valuation of certain items. Regarding the former, at this moment it is not possible to determine the exact impact that this new regulation will entail compared to Spanish GAAP, since new pronouncements from the International Accounting Standards Board (IASB), or pronouncements that are not endorsed by the European Union (EU) prior to the preparation of our December 31, 2005 consolidated financial statements, may have an impact on our financial statements. Regarding the latter, we have performed a preliminary analysis of how the adoption of IFRS will impact our financial condition and results of operations. Based on this analysis, we estimate that the principal adjustments to our total shareholders' equity at December 31, 2004 under IFRS would result in a decline in our shareholders' equity of approximately 1,284.5 million from 4,719.9 million at that date under Spanish GAAP. For additional information concerning significant differences identified between IFRS and Spanish GAAP, see Item 5 Operating and Financial Review and Prospects Preliminary Guidance on Differences Between IFRS and Spanish GAAP .

Risks Related to Our Industry

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

The licensing, construction, operation and interconnection arrangements of wireless communications systems are regulated to varying degrees by national, state, regional or local and supra-national authorities, such as the European Union. These authorities could adopt regulations or take other actions that could adversely affect us and our companies. Our operating companies require licenses or concessions from the governmental authorities of the countries in which they operate. These licenses and concessions specify the types of services permitted to be offered by our operating companies and the spectrum that may be utilized for these purposes. The continued existence and terms of our licenses and concessions are subject to review by regulatory authorities in each country and to interpretation, modification or termination by these authorities. The terms of our licenses and concessions generally range from 15 to 25 years. Although these licenses and concessions generally are renewable upon expiration, we cannot assure you that they will be renewed or that any renewal will be on acceptable terms.

The rules of some of the government regulatory authorities having jurisdiction over our operating companies require us to meet specified network build-out requirements and schedules. In addition, our wireless licenses and concessions typically also require satisfaction of various obligations, including minimum specified quality, service, coverage criteria and capital investment. Failure to comply with these obligations in a given license area could result in the imposition of fines or the revocation or forfeiture of the license for that area. In addition, the need to meet scheduled deadlines may cause our company to expend more resources than otherwise budgeted for a particular network build-out. We cannot assure you that our operating companies will be able to fully comply with the terms and conditions of these licenses and concessions.

Increased or significant changes in the regulation of the activities of our operating companies, including the regulation of rates that may be charged to customers for services or termination fees, could have a material adverse effect on our company. New regulations could also increase the costs of regulatory compliance.

Our operating companies also typically require governmental permits, including permits for the construction and operation of cell sites. We do not believe that compliance with these permit requirements should have a material adverse effect on our company. However, if we fail to comply with these permit requirements, we could become subject to claims or regulatory actions.

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Our results may be affected in the medium or long term as a result of the new SMP rules in Brazil.

In 2002, Anatel, the Brazilian telecommunications regulator, introduced a new mobile services licensing regime, or SMP, encouraging companies operating under the personal cellular services, or SMC system, to migrate to the SMP system. Under the SMP regime, Brasilcel's subsidiaries will no longer receive payment from its customers for outbound long distance traffic, but will receive payment for the use of its network, in accordance with the network usage remuneration plan. Although the new regime has not had a significant impact on Brasilcel's subsidiaries, we cannot assure that in the future the interconnection fees that we will receive from long distance operators will compensate Brasilcel for the revenues that it would have received from its customers for outbound long distance traffic.

Until June 30, 2004, SMP service providers could choose to establish a price cap or freely negotiate their interconnection charges. After that date, free negotiation has been the rule, subject to Anatel regulations.

In addition, under the SMP regime, an SMP mobile operator must pay for the use of another SMP mobile operator's network in the same registration area only if the traffic carried from the first operator to the second exceeds 55% of the total traffic exchanged between them. In that case, only those calls that have surpassed the 55% level will be subject to payment for network usage. This rule will remain in effect until June 30, 2005, after which date no payments will be due for network usage between SMP networks, regardless of the amount of traffic. As a result, if the traffic Brasilcel's subsidiaries terminate for other SMP mobile operators exceeds the traffic such other SMP mobile operators terminate for Brasilcel's subsidiaries, Brasilcel's revenues and results of operations may be adversely affected.

Anatel submitted its proposed new regulations on interconnection for public comment. The public comment period ended on October 18, 2004 and Brasilcel subsidiaries presented their arguments against some of the proposals that may have adverse effects on their results. Anatel has not yet decided whether to modify its proposed new regulations. If these regulations take effect, they may negatively affect our revenues and results of operations.

We are subject to evolving regulatory policies which favor increased competition and which could expose us to additional competition in our markets.

Regulatory policies of many of the countries in which we operate generally favor increasing competition in the wireless services industry, including by granting new licenses in existing licensed territories in order to permit the entry of new competitors. In Spain the National Regulatory Authority (NRA) is currently analyzing, in accordance with the principles of the European Telecom Regulation Framework, the market of access and call originated on public mobile telephone networks. On the basis of this market analysis, the NRA will determine whether this market is effectively competitive or not, and subsequently impose, amend or withdraw regulatory obligations accordingly. Should the NRA conclude that the market of access and call origination on public mobile telephone networks is not effectively competitive, it may impose on network operators more stringent regulatory obligations, which may include, among others, to provide access to the mobile virtual network operator MVNOs (being mobile operator that do not own a network and instead buys mobile minutes wholesale from those network operators with physical networks and sells them to its clients).

In addition, because we hold leading market shares in many of the countries in which we have operations, we could face regulatory actions by national or, in the case of Europe, EU antitrust or competition authorities if it is determined that we have prevented, restricted or distorted competition.

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The provision of wireless internet-based content and m-commerce may become subject to increased regulation, which could increase our costs or delay growth in demand for our wireless data and internet services.

The provision of internet-based content and m-commerce has not to date been materially restricted by regulation in the markets in which we operate or intend to operate. The legal and regulatory environment relating to internet content and m-commerce is uncertain, however, and may change. New laws and regulations may be adopted for internet service offerings. Existing laws may be applied to the forms of m-commerce in which we expect to engage. Uncertainty and new regulations could increase our costs and could also slow the growth of m-commerce. New and existing laws could delay growth in demand for our wireless data and internet services and thereby limit the growth of our revenues.

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Our company's technology could fail to be competitive with other technologies or compatible with the next generation technology.

Our operating companies offer both analog and digital cellular services in their markets. Our digital networks in different countries use different standards. Although there is some ability to roam on analog networks, the digital transmission standards are not fully compatible with one another. Our use of these multiple technologies may limit some of our anticipated economies of scale as we seek to further integrate the businesses of our multiple operating companies and we could be required to make significant additional capital investments. Significant capital investments may not be recouped and revenues could decline as current and potential customers select alternative providers and technologies. In addition, alternative technologies may develop for the provision of wireless services to customers that may prove superior to those currently projected. We cannot assure you that unforeseen technological developments will not render our services obsolete or unpopular with customers.

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

Media and other reports have suggested that radio frequency emissions from wireless handsets and base stations may cause health problems. If consumers harbor health-related concerns, they may be discouraged from using wireless handsets. These concerns could have an adverse effect on the wireless communications industry and, possibly, expose wireless providers, including us, to litigation. Even if the authorized health institutions confirm there is no scientific evidence of adverse health effects, we cannot assure you that further medical research and studies will refute a link between the radio frequency emissions of wireless handsets and base stations and these health concerns. Government authorities could increase regulation of wireless handsets and base stations as a result of these health concerns or wireless companies, including us, could be held liable for costs or damages associated with these concerns, which could have an adverse effect on our business. In Spain, for example, we have been required by law to test and certify the emissions of all our base stations in or close to populated areas. For the year ended December 31, 2004, all the tests we were obliged to do have again confirmed lower emission levels than those required by regulations. If in the future we fail to comply fully with these standards, we could be subject to claims or regulatory actions.

Risks Related to Latin America

Adverse Latin American economic, political and social conditions could affect our financial performance.

The portion of our revenues and profits deriving from Latin American operations will be increasing due mainly to the development of our operations in Brazil, Mexico and other Latin American countries, including the operations recently acquired from CTC (a subsidiary of Telefónica) and BellSouth. Our financial performance in the region is affected by economic, political and social conditions in Latin America. These conditions are volatile due to, among other factors, the following:

significant governmental influence over local economies;

substantial fluctuations in economic growth;

historically high levels of inflation;

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devaluation or depreciation, or over-valuation of local currencies;

exchange controls or restrictions on expatriation of earnings;

high domestic interest rates;

wage and price controls;

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changes in governmental economic or tax policies;

imposition of trade barriers;

unexpected changes in governmental regulation;

social unrest; and

overall political and economic instability.

Many or all of these factors have occurred at various times in the last two decades in most Latin American markets. Adverse economic, political and social conditions in Latin America may have a material adverse effect on our results of operations and the market price for our ordinary shares or ADSs.

For example, our operations in Argentina were affected by the devaluation of the Argentine peso, the adverse macroeconomic conditions in Argentina and the related legislative measures adopted by the Argentine Government in past years.

Additionally, Telefónica Comunicaciones Personales is currently in a negative net worth position. Although current Argentine law (Decree 214/2002, as extended) allows companies to maintain this negative net worth position until December 2005 without the need to establish a positive net worth position, it is uncertain whether the government of Argentina will once again extend this exception beyond December 2005. Should this exception fail to be extended and if Telefónica Comunicaciones Personales is not capitalized by Telefónica Móviles, either through increased capital or partial capitalization of intercompany loans, Telefónica Comunicaciones Personales could be subject to a dissolution proceeding by the Argentine authorities and could lose its license.

Latin American currencies have been subject to fluctuations, which could adversely affect revenues and expenses for our operations in this geographic region.

Although our reporting currency is the euro, most of our revenues and expenses relating to our Latin American operations are denominated in local currencies. The currencies of many Latin American countries, have experienced substantial devaluations and volatility in recent years, and our revenues from customers will decline in value if the local currencies depreciate relative to the euro.

Our business, financial condition and results of operations may be adversely affected by declines in the value of the currencies of the Latin American countries where we operate. Our hedging strategies may not prove effective to address the effects of foreign currency exchange movements on our financial condition or performance. In addition, our exposure to foreign currency exchange losses may be increased if we become subject to exchange control regulations that restrict our ability to convert local currencies into euro or U.S. dollars. Because our strategy involves increasing our revenues from our Latin American operations and because of the increasing importance of Latin American markets to our operations, our exposure to foreign currency movements is likely to increase over time.

Item 4. INFORMATION ON THE COMPANY

A. HISTORY AND DEVELOPMENT OF THE COMPANY

Background of Our Company

We are a limited liability company duly organized and existing under the laws of the Kingdom of Spain. We were incorporated on February 14, 2000. Our principal executive offices are located at Goya 24, 28001 Madrid, Spain and our telephone number is +(34) 91 423-4004.

We are a holding company that conducts its wireless operations through subsidiaries and investments in Spain, Morocco, and Latin America. We manage all of the wireless assets of the Telefónica Group, a diversified

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telecommunications group that provides a comprehensive range of services in Spain and Latin America. As of December 31, 2004 Telefónica, S.A., the parent company of the Telefónica Group, holds, directly and indirectly, 92.46% of our shares.

The following is a brief summary of key steps in the development of our company:

Spain: The Telefónica Group commenced wireless operations in Spain in 1982. In 2000, Telefónica, S.A. transferred to our company all of the shares of its wireless subsidiary in Spain, Telefónica Móviles España, in exchange for 84,445,927 ordinary shares of our company. Telefónica Móviles España is a direct wholly-owned subsidiary of our company and constitutes our most significant subsidiary in terms of its contribution to our revenues and profitability.

Brazil: The Telefónica Group commenced wireless operations in Brazil in 1996. In 2002, we and Portugal Telecom created Brasilcel, N.V., or Brasilcel, a joint venture which combined our respective wireless operations in Brazil. The joint venture is 50%-owned by each group and consolidated by the proportional method in our financial statements. Our holdings and those of Portugal Telecom in the following operations were combined in the Brasilcel joint venture:

Tele Sudeste Celular Participações S.A.;

Celular CRT Participações S.A.;

Tele Leste Celular Participações S.A.; and

Telesp Celular Participações S.A.

The value of our contribution to Brasilcel of the wireless assets owned by us was 1,898 million. Subsequently, in 2003, Telesp Celular Participações S.A. acquired 86.6% of the voting capital stock (representing approximately 28.9% of the total capital stock) of Tele Centro Oeste Participações S.A., a wireless operator that provides wireless services in Brazil's Federal District and 11 Brazilian states.

In June 2004, Brasilcel completed its acquisition of the interests of NTT DoCoMo, Inc. and Itochu Corporation in Sudestecel Participações, S.A., the holding company of Tele Sudeste Celular Participações, S.A. This acquisition brings Brasilcel's control of Sudestecel to 100%. In October 2004, Brasilcel completed voluntary tender offers for outstanding public holdings of Tele Sudeste Celular Participações, S.A., Tele Leste Celular Participações, S.A. and Celular CRT Participações, S.A., bringing Brasilcel's holdings in these companies to 90.9%, 50.6% and 67.0%, respectively. Additionally during 2005 Sudestecel increased its participation in Tele Sudeste Celular Participações, S.A. to 24.52% bringing Brasilcel's participation to 91.14%. Additionally, in October 2004, Telesp Celular Participações, S.A. (TCP), a company controlled by Brasilcel, increased its participation in Tele Centro Oeste Celular Participações, S.A. (TCO) to 50.6% through the acquisition of a 32.8% interest in TCO's preferred shares. In addition, TCP's Board of Directors approved an increase in its share capital of approximately R\$2.1 billion, which was effected in January 2005. The proceeds raised were used in part to finance TCP's increased stake in TCO and the remainder has been used to partially repay short-term debt and improve TCP's capital structure. Through this transaction Brasilcel's stake in TCP's share capital increased to 65.7%.

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Peru: The Telefónica Group commenced wireless operations in Peru in 1991. Its subsidiary, Telefónica del Perú S.A.A., spun off in June 2001 its wireless operations in the form of shares of Telefónica Móviles S.A.C. Following this spin-off and later share exchanges and additional share purchases, as of June 23, 2005, we indirectly hold a 97.97% interest in Telefónica Móviles S.A.C. Following our acquisition of BellSouth's interest in its Peruvian operations in October 2004, as of June 23, 2005, we hold, directly and indirectly, a 99.85% interest in Comunicaciones Móviles del Perú, S.A. (formerly BellSouth Perú, S.A.). On April 26, 2005, we launched a tender offer for the acquisition of the outstanding minority interest (0.15%) in Comunicaciones Móviles del Perú, S.A. which ended on May 23, 2005, with the acquisition of 0.04% of the share capital for US\$9,239.80, bringing our interest in Comunicaciones Móviles del Perú, S.A. to 99.89%.

We have merged Telefonica Moviles, S.A.C. and Comunicaciones Móviles del Perú, S.A. Currently, we hold, directly and indirectly, 98.04% of the resulting entity.

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Argentina: The Telefónica Group commenced wireless operations in Argentina in 1993. Its subsidiary, Telefónica de Argentina S.A., spun off its wireless operations in the form of shares of Telefónica Comunicaciones Personales S.A. and its data operations in 2001. Following the spin-off and share exchanges, as of June 23, 2005, we indirectly hold a 97.93% interest in Telefónica Comunicaciones Personales S.A. We do not hold an interest in the data operations formerly owned by Telefónica de Argentina. Following our acquisition of BellSouth's interest in its Argentine operations in January 2005, as of June 23, 2005, we hold, directly and indirectly, a 100% interest in Compañía de Radiocomunicaciones Móviles, S.A.

Mexico: We hold 92.0% of Telefónica Móviles Mexico and the Burillo Group owns the remaining 8%. The companies making up Telefónica Móviles Mexico were acquired by us in two steps:

- 1) *Acquisitions of Northern operators.* We acquired four Northern wireless operators (Bajacel, Movitel, Norcel, and Cedetel) from Telefónica, S.A. in July 2001.
- 2) *Acquisition of Pegaso and formation of Telefónica Móviles Mexico.* On April 26, 2002, we signed agreements to purchase 65.23% of Pegaso Telecomunicaciones, S.A. de C.V. We also agreed to contribute our interests in Pegaso and our other Mexican operators and with Burillo Group's interest in Pegaso into a new holding company, Telefónica Móviles Mexico.

Chile: The Telefónica Group commenced wireless operations in Chile in 1990. In July 2004, we acquired 100% of Telefónica Móvil de Chile, S.A. from CTC (a subsidiary of Telefónica S.A.). We have been managing Telefónica Móvil de Chile's operations since 2000.

Guatemala and El Salvador: The Telefónica Group commenced wireless operations in El Salvador in 1998 and in Guatemala in 1999. In 2000, The Telefónica Group transferred to us its shares in TES Holdings, S.A. and TCG Holding, S.A., its holding companies in El Salvador and Guatemala, in exchange for 5,542,534 ordinary shares of our company. We acquired the remaining interests in TES Holdings, S.A. and TCG Holding, S.A. in 2002 for 14.5 million of our ordinary shares. Following our acquisition of BellSouth's interest in its Guatemalan operations, as of June 23, 2005, we hold, directly and indirectly, 100% of Telefónica Móviles Guatemala y Compañía. (formerly BellSouth Guatemala, S.A.).

On April 20, 2005, TES Holding acquired shares representing approximately 4.4% of Telefónica Móviles El Salvador, S.A.'s capital stock for approximately \$5.1 million. Following this acquisition, TES Holding owns 96.19% of Telefónica Móviles El Salvador, S.A.

Colombia, Ecuador, Uruguay, Panama, Nicaragua, Venezuela: In October 2004, we acquired BellSouth's interests in its operations in these countries. Additionally, in various countries we increased the acquired stakes by acquisition of minority shareholders. As of June 23, 2005, we hold, directly and indirectly, 100% of BellSouth Colombia, Otecel, S.A. (Ecuador), Abiatar (Uruguay), Telcel, S.A. (Venezuela), Telefónica Celular de Nicaragua, S.A., and 99.95% of Telefónica Móviles Panamá, S.A.

Morocco: The Telefónica Group commenced wireless operations in Morocco in 2000. In October 2000, Telefónica, S.A. transferred to our company a 30.5% interest in Medi Telecom. We increased our holding through capital increases of Medi Telecom in 2002 and 2003. As of June 23, 2005, we hold a 32.18% equity interest in Medi Telecom.

Europe: In 2000 and 2001, we obtained third-generation wireless telephony (UMTS) licenses in Germany, Italy, Austria and Switzerland. The financial, technological, competitive and regulatory changes that have taken place in the market since then resulted in our reviewing our

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European strategy. Accordingly, in July 2002 we decided to halt our commercial activities in Germany and updated the assumptions of the business plans of our subsidiaries in Austria, Germany, Italy and Switzerland. As a result, at December 31, 2002, a net loss of 5,049.8 million was recorded in our combined financial statements associated with the write-down of assets and the restructuring of operations in these four countries. In December 2003, we sold our Austrian subsidiary to Mobilkom Austria for a total sale price of 13.6 million.

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Puerto Rico: We entered into a management contract with NewComm Wireless, a Puerto Rican wireless operator, when it commenced operations. In September 2004, the management contract was terminated and Clearcomm took charge of the management of Newcomm Wireless. At the same time, we decided to write-off the value of convertible notes (46 million) issued by Newcomm Wireless to the Telefónica Group. In September 2003, the Telefónica Group transferred these convertible notes to us for an aggregate amount of \$60.9 million. On April 20, 2005, we converted these notes into 49.9% of the capital stock of NewComm Wireless and currently hold this interest through our 100%-owned subsidiary, Telefónica Móviles Puerto Rico Inc. Since we do not have a controlling interest in and we no longer manage the operations of Newcomm Wireless, we no longer count its customers in our total managed customer base.

Other strategic initiatives: We have also undertaken the following strategic initiatives and acquisitions that we believe are complementary to our core wireless communications activities.

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

The development of further joint technical projects and procurement initiatives are expected to deliver economic benefits, while the volume of devices jointly acquired is targeted to increase over time. Collective synergies will also help members to be the first to market new models and to potentially secure exclusivity periods on those models with manufacturers.

Acquisition of BellSouth's Latin America wireless operations: On March 5, 2004, we entered into a stock purchase agreement with BellSouth to acquire 100% of BellSouth's interests in its wireless operations in Argentina, Chile, Peru, Venezuela, Colombia, Ecuador, Uruguay, Guatemala, Nicaragua and Panama. The firm value of the wireless operators that we have acquired from BellSouth, including the interests of minority shareholders and the net debt of these wireless operators, was valued at US\$5,850 million, including BellSouth's wireless operations in Argentina and Chile, which we acquired in January 2005. The firm value of the wireless operators that we have acquired from BellSouth as of December 31, 2004, including the interests of minority shareholders and the net debt of these wireless operators, was US\$4,330 million.

The total amount paid for our interests in these wireless operators as of December 31, 2004, adjusted for the net debt of the acquired companies, was 3,248.6 million. The total acquisition cost for BellSouth's wireless operations in Argentina and Chile, which we acquired in January 2005, adjusted for the net debt of the acquired companies, was 836.6 million.

Acquisition of 100% of Telefónica Móvil de Chile in 2004: On May 18, 2004, the board of directors of Telefónica CTC Chile, S.A., or CTC, accepted our binding offer for the purchase of 100% of the shares of its subsidiary, Telefónica Móvil de Chile, S.A. Telefónica S.A. owns 43.6% of CTC Chile. We have been managing Telefónica Móvil de Chile's operations since 2000. We completed the acquisition on July 23, 2004. The purchase price was 869.9 million. In addition, we assumed approximately 168,000 million Chilean Pesos in debt owed by Telefónica Móvil de Chile to CTC.

The following tables provide information for our principal acquisitions completed in 2002, 2003 and 2004.

Acquisitions in 2002

<u>Month</u>	<u>Company name</u>	<u>Initial%</u>	<u>Acquired%</u>	<u>Final%</u>	<u>Acquisition Price (thousands of euro)</u>
Jan	TES Holding, S.A. de C.V. (El Salvador)	51.00	16.30	67.30	32,106
Jan.	TCG Holdings, S.A. (Guatemala)	51.00	16.30	67.30	25,226
May	Iberoleste Participações, S.A. (1) (Brazil)	37.98	62.02	100.00	113,196

Table of Contents**Acquisitions in 2002**

Month	Company name	Initial%	Acquired%	Final%	Acquisition Price (thousands of euro)
May	TBS Participações, S.A. (1) (Brazil)	66.27	7.00	73.27	25,910
May	Tele Leste Celular Participações, S.A. (1) (Brazil)		3.38	3.38	13,593
May	Sudestecel Participações, S.A. (1) (Brazil)	82.50	7.00	89.50	64,062
May	TES Holding, S.A. de C.V. (1) (El Salvador)	67.37	32.70	100.00	14,934
May	TCG Holdings, S.A. (1) (Guatemala)	67.37	32.70	100.00	11,734
May	Telefónica de Centroamérica, S.L. (1) (Spain)	67.37	32.70	100.00	982
Sep.	Pegaso Telecomunicaciones, S.A. de C.V. (Mexico)		65.23	65.23	92,870
Sep.	Pegaso Telecomunicaciones, S.A. de C.V. (Mexico)	65.23	65.23	65.23	211,454
Oct.	CRT Celular Participações, S.A. (Brazil)	22.75	0.66	23.41	11,544
Oct.	Telesp Celular Participações, S.A. (Brazil)		14.68	14.68	200,306
Dec.	Medi Telecom. (Morocco)	30.5	0.84	31.34	17,390
Dec.	Telefónica Móviles Soluciones y Aplicaciones, S.A. (Chile)	100.00		100.00	9,215

(1) These acquisitions were performed through capital increases.

Acquisitions in 2003

Date	Company name	Initial%	Acquired%	Final%	Acquisition Price (thousands of euro)
Apr.	Tele Centro Oeste Celular Participações, S.A. (Brazil)		20.37	20.37	206,285
Jul.	Medi Telecom. (Morocco)	31.34	0.84	32.18	21,234
Oct.	Tele Centro Oeste Celular Participações, S.A. (Brazil)	20.37	8.50	2.87	73,827
Dec.	TCG Holdings, S.A. (Guatemala)	100.00		100.00	3,746

Acquisitions in 2004

Date	Company name	Initial%	Acquired%	Final%	Acquisition Price (thousands of euro)
Jul.	Telefónica Móvil de Chile, S.A.		100.00	100.00	869,898
Oct.	Otecel, S.A. (Ecuador)		100.00	100.00	663,428
Oct.	Telefónica Móviles y Compañía, S.C.A. (Guatemala)		100.00	100.00	92,538
Oct.	BellSouth Panamá, S.A.		99.57	99.57	549,275
Oct.	Telcel, S.A. (Venezuela)		100.00	100.00	1,223,984
Oct.	Telefónica Móviles Colombia, S.A.		100.00	100.00	517,456
Oct.	Comunicaciones Móviles del Perú, S.A.		99.85	99.85	7,697
Oct.	Telefonía Celular de Nicaragua, S.A.		100.00	100.00	148,742
Oct.	Abiatar, S.A. (Uruguay)		100.00	100.00	49,419

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The following chart presents our corporate organization, including our principal operating companies and the companies in which we have non-controlling minority interests, as well as our ownership interests in these companies at December 31, 2004:

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- (1) Jointly managed with Portugal Telecom.
- (2) We acquired 100% of Telefónica Móvil de Chile's shares on July 23, 2004, and it was fully consolidated in our financial statements as from August 1, 2004.
- (3) Telefónica Móviles increased its stake in Telefónica Móviles El Salvador to 91.75% in 2004 after capitalizing certain loans to the subsidiary.
- (4) In October 2004, we purchased BellSouth's wireless operators in Colombia, Ecuador, Guatemala, Nicaragua, Panama, Peru, Uruguay and Venezuela. These companies were consolidated in our financial statements as from November 1, 2004.
- (5) Telefónica Móviles increased its stake in this company to 50% in June 2004.

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B. BUSINESS OVERVIEW

Overview

We are part of the Telefónica Group, whose parent company is Telefónica, S.A., estimated as one of the five largest diversified telecommunications companies in the world based upon stock market capitalization.

We are a leading provider of wireless communications services in Spain and Latin America in terms of managed customers. We estimate, based on annual reports and press releases made public by our competitors and information from regulatory authorities, that we are one of the five largest global providers of wireless communication services based upon total managed customers at December 31, 2004. Managed customers include all customers from all operators in which we hold an economic interest, including TCO in Brazil from 2003, Telefónica Móvil de Chile from August 2004 following its acquisition in July 2004, the operators acquired from BellSouth in Colombia, Ecuador, Guatemala, Nicaragua, Panama, Peru, Uruguay and Venezuela from October 2004. Managed customer figures for 2004 exclude Movistar Puerto Rico's customer base, following the termination of our management contract in September 2004. We offer a broad range of wireless services, including voice services, enhanced calling features, international roaming and wireless internet.

At December 31, 2004, we provided wireless services through our operating companies and joint ventures, to approximately 74.4 million managed customers in territories with a population of approximately 509 million. Telefónica Móviles has operations in Spain, Mexico, Peru, El Salvador, Guatemala, Venezuela, Colombia, Panama, Nicaragua, Ecuador, Uruguay, Argentina and Chile and, through its joint ventures with Portugal Telecom, it also provides wireless communication services in Brazil and Morocco.

Our strategy is to focus on increasing our profitability and cash flow in the medium term by consolidating our competitive positions in Spain and Latin America, introducing new services to promote usage, and optimizing our investments and operating efficiencies. We will continue to analyze the possibility of selective acquisitions and strategic agreements that complement our business. For example, we have acquired TCO in 2003, BellSouth's Latin American wireless operations in 2004 and 2005 and 100% of Telefónica Móvil de Chile in 2004. We believe that growth in our markets will be driven by (i) increased customer usage of our wireless services, including both voice and data services, (ii) the introduction of new wireless data and internet services, and (iii) increased penetration rates in our Latin American markets.

We also have licenses to provide UMTS services in Switzerland through our wholly-owned subsidiaries, in Germany through our 57.2% interest in the Group 3G UMTS Holding GmbH consortium, or Group 3G, and in Italy through our 45.59% interest in the IPSE 2000 consortium. We have, however, restructured our operations in these countries. For further information see Regulation Legal Framework of European Operations.

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The following table provides a summary overview of our principal operating companies and those companies in which we have non-controlling minority interests.

Year ended December 31, 2004

Country	Company	Service Territory	Ownership Interest at December 31, 2004	Population	Total customers at December 31, 2004	Net Revenue from Operations	Operating profit before depreciation and amortization (4)
				(in millions)	(in millions)	(millions of euro)	
Ecuador	Otecel, S.A.(7)	Nationwide	100%	12.9	1.1	43.8	(0.9)
Panama	BellSouth Panamá, S.A.(10)	Nationwide	99.95%	3.2	0.6	24.0	7.7
Venezuela	Telcel, S.A.(7)	Nationwide	100.0%	26.0	4.3	215.2	51.0
Colombia	Telefónica Móviles	Nationwide	100.0%	45.3	3.3	94.9	(0.4)
	Colombia, S.A.(7)						
Nicaragua	Telefónica Celular de	Nationwide	100.0%	5.6	0.3	8.3	1.0
	Nicaragua, S.A.(7)						
Uruguay	Abiatar, S.A.(7)	Nationwide	100.0%	3.4	0.2	5.6	0.9
Spain	Telefónica Móviles España	Nationwide	100.0%	44	19	8,190.0	4,202.0
Brazil	Brasilcel, N.V.(1)	Nationwide (2)	50.0%	131.5	26.5	1,522.0	500.0
Peru	Telefónica Móviles Peru	Nationwide	97.97%	27.6	2.1	248.0	70.0
	Comunicaciones Móviles del	Nationwide	99.85%	27.6	0.7	19.0	2.6
	Perú, S.A(7)						
Argentina	Telefónica Comunicaciones	Nationwide	97.93%	38.7	3.4	360.5	4.0
	Personales						
Mexico	Telefónica Móviles México,	Nationwide	92.0%	104.7	5.6	730.0	(145.0)
	S.A. de C.V.(3)						
El Salvador	Telefónica Móviles El	Nationwide	91.75%	6.7	0.4	104.0	12.4
	Salvador						
Guatemala	Telefónica Centroamérica	Nationwide	100.0%	12.7	0.4	79.0	8.5
	Guatemala						
	Telefónica Móviles y	Nationwide	100.0%	12.7	0.4	13.7	4.5
	Compañía, S.C.A.(7)						
Morocco	Medi Telecom(6)	Nationwide	32.18%	31	2.7	336.0	154.0
Chile	Telefónica Móvil de Chile(5)	Nationwide	100.0%	15.4	3.3	182.8	50.1

- (1) Jointly controlled and managed by Telefónica Móviles and Portugal Telecom. Through its 50% interest in Brasilcel, as of December 31, 2004, Telefónica Móviles indirectly holds 45.45% of Tele Sudeste, 26.42% of Celular CRT, 25.3% of Tele Leste Celular, 32.56% of Telesp Celular Participações, S.A. and 10.74% of Tele Centro Oeste Celular Participações, S.A. Brasilcel is proportionally consolidated in our financial statements. For information on our ownership interest in Brasilcel, and its operators, please refer to our organizational structure found in Item 5.A. Operating Results Overview.

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- (2) The service territory in Brazil is nationwide with the exception of region 4 (the state of Minas Gerais).
- (3) Telefónica Móviles México, S.A. de C.V. holds interests in 100% of Baja Celular Mexicano, 90.0% of Movitel del Noroeste, 100% of Telefónica Celular del Norte, 100% of Celular de Telefónica, S.A. de C.V. and 100% of Pegaso PCS. Through its 92.0% interest in Telefónica Móviles México, S.A. de C.V., as of December 31, 2004, Telefónica Móviles indirectly holds 92.0% of Baja Celular Mexicano, 82.8% of Movitel del Noroeste, 92.0% of Telefónica Celular del Norte, 92.0% of Celular de Telefónica, S.A. de C.V. and 92.0% of Pegaso PCS.
- (4) See Item 5.A. Operating Results Introduction to Results of Operations Non-GAAP Financial Information for a definition of operating profit before depreciation and amortization and a discussion concerning our use of, and limitations relating to, that measure.
- (5) In July 2004, we acquired 100% of the shares of Telefónica Móvil de Chile, S.A., and it has been consolidated in our financial statements as from July 1, 2004. Net revenue from operations and operating profit before depreciation and amortization are provided for the last six months of fiscal year 2004. Ownership interests, population and total customers are presented at December 31, 2004.
- (6) Jointly controlled and managed by Telefónica Móviles and Portugal Telecom. Portugal Telecom owns 32.18% of the share capital of Medi Telecom.
- (7) Acquired from BellSouth Corporation in October 2004 and consolidated in our financial statements as from November 1, 2004. Net revenue from operations and operating profit before depreciation and amortization are provided for the last two months of fiscal year 2004. Ownership interests, population and total customers are presented at December 31, 2004.

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Business Strategy

The key elements of our strategy consist of the following:

Maintain our market leadership position in Spain: As the Spanish market continues to mature and the competitive pressure increases, mainly in number portability and pricing for the corporate segment, we are focused on preserving our leading position in the market, particularly in terms of revenue share. As part of our strategy we are developing new products and pricing schemes targeted at different customer segments to stimulate usage, increase customer retention and attract new customers in segments with high growth potential. In addition, we are leading the deployment of the UMTS in Spain, offering superior coverage than our competitors, with 3,800 UMTS base stations as of December 2004. We will also continue to leverage our customer loyalty programs to increase customer retention.

Consolidate our competitive position in Latin America: We seek to consolidate our strong competitive position in the growing Latin American market through our extensive presence in the region and our integrated management of operations in the area, leveraging our extensive managerial and operational experience.

Our acquisition of BellSouth's wireless operators in Latin America and Telefónica Móvil de Chile has allowed us to further consolidate our leadership position and strengthen our growth profile in Latin America. At December 31, 2004, we had approximately 74.4 million managed customers in 13 Latin American countries.

Introduce new services to increase the usage of wireless services: We will continue leading innovation in our markets to capture the high growth potential of wireless data services. We will continue launching new data services and applications aimed at different customer needs, such as MMS, video message, content downloads, location-based services, corporate services, (such as the launch of Oficin@ Movistar UMTS,) and domotics. We aim to leverage our extensive experience and best practices to grow revenue from data services across our markets. The introduction of UMTS in Spain and 1XRTT EVDO in some of our markets in Latin America will enhance customer experience, while we will capitalize on our expertise in developing customize solutions to increase data usage in the corporate segment.

Optimize capital expenditures and increase operating efficiency: Our economies of scale allow us to better optimize our capital expenditure. In addition, the integrated management of our operations in Latin America and the promotion of our best practices among our operating companies will allow us to operate more efficiently, optimize investments and improve the time to market of our services.

Analyze new projects: We intend to evaluate the possibility of making selective acquisitions and forming selected strategic partnerships in order to improve our competitive position, such as our acquisition of TCO in 2003, our acquisition of 100% of BellSouth's interests in its Latin American wireless operations, our acquisition of 100% of Telefónica Móvil de Chile as well as our alliances with T-Mobile International, TIM (Telecom Italia Mobile) and Orange in Europe. In addition, on February 26, 2003 we announced our participation in the new MPESA association (Mobile Payment Services Association). The association, which is composed of Vodafone, Orange, T-Mobile and us will operate under the brand name Simpay. For further information see Wireless Internet and Data Initiatives M-Payment.

We believe that the following strengths will allow us to compete successfully against other wireless services providers in our existing and future markets: (i) market leadership in Spain and most Latin American markets; (ii) global and local scale; (iii) management control over our operations; (iv) proven track record of innovation; (v) strong distribution channels; (vi) extensive operational experience; (vii) financial strength and flexibility; and (viii) membership of the Telefónica Group.

Services and Products

Our operating companies offer a wide variety of wireless and related services and products to consumer and business customers. We believe that we have historically been leaders in the introduction of new products in our principal markets, and we plan to continue expanding our offerings as new services and products become commercially feasible. Although the products available vary from country to country, the following are our principal services and products:

Wireless Voice Services. Our principal service in all of our markets is wireless voice telephony, which has gained increased usage as a result of our increased customer base and increased market penetration rates. Accordingly, we are also able to offer new services such as those detailed below.

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

Wireless data and internet Services. Current data services offered include Short Messaging Services, or SMS, and Multimedia Messaging Services, or MMS, which allows customers to send messages with images, photographs and sounds. Customers may also receive selected information, such as news, sports scores and stock quotes. We also provide wireless connectivity for devices such as laptops and personal digital assistants. We offer internet access in an increasing number of areas, allowing our clients to access a wide range of mobile internet services through voice, WAP (wireless application protocol, a standard protocol allowing for wireless Internet access) or GPRS. Through wireless internet access, our customers are able to send and receive e-mail, browse web pages, download games, purchase goods and services in m-commerce transactions and use our other data services. Technological advances, which include the development of GPRS, CDMA 1XRTT (code division multiple access, a broadband transmission system for wireless networks allowing for speeds of up to 144 Kbits/s) and UMTS, facilitate the development of these services by increasing the speed at which data is transmitted, and making it possible to expand the offer of services and reduce their cost. Telefónica Móviles España launched its Oficin@ Movistar UMTS GPRS/UMTS data card, making it available to its corporate customers in February 2004, and to all residential and prepaid customers in May 2004, together with the launch of the first UMTS videophone services in the Spanish market. We also have the technology available to provide other wireless data services such as location-based services and telematics. Location-based services permit the precise location of the handset to be determined by our networks, which will permit users to receive and access information specific to such location. We believe that this technology will be widely used in fleet management, logistics and security monitoring. Telematics applications permit the delivery of data to machines, such as automobiles and vending machines.

Corporate Services. We provide business solutions, including wireless infrastructure in offices, private networking and portals for corporate customers that provide flexible on-line billing. Telefónica Móviles España offers corporate services through *MoviStar Corporativo 2000*, and other advanced solutions for data, developed for specific sectors. In addition, as of February 13, 2004, Telefónica Móviles España has offered its corporate customers Oficin@Movistar UMTS, the first third generation service offered in Spain by a mobile operator offering high-speed data transmission of up to 384 kbits/s.

Roaming. We have roaming agreements that allow our customers to use their handsets when they are outside of their service territories, including on an international basis. In 2002, we extended international roaming services to pre-paid customers. We have also implemented intelligent network technology using the CAMEL standard for our customers in Spain. This allows our customers to use their mobiles in European countries where a roaming agreement has been reached as if they were in their home country (for example, by not having to dial customary roaming prefixes). Through Telefónica Móviles España's FreeMove alliance with T-Mobile International, Telecom Italia Mobile and Orange, customers of the four partners now enjoy seamless roaming services when traveling abroad through the Virtual Home Environment. In Brazil, Mexico and Argentina, our roaming agreements allow our customers to make and receive calls throughout the national territories of these countries.

Trunking and Paging. In Spain and Guatemala, we provide digital wireless services for closed-user groups of clients and paging services.

M-payment. Through our subsidiary Telefónica Móviles España and together with Vodafone España, Amena and many other financial institutions and processing companies, we have an interest of 13.36% in Mobipay España, a company incorporated to develop micro-payments. We also have, together with BBVA, a 50%/50% interest in Mobipay International, aimed at expediting payments through mobile phones in an international setting. In addition, we participate in the new MPSA association (Mobile Payment Services Association). The association, which is composed of Vodafone, Orange, T-Mobile and us will operate under the brand name Simpay. For further information see Wireless Internet and Data Initiatives M-Payment.

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Our Operations

Our operations currently are conducted in three distinct geographic areas:

Spain

Morocco

Latin America

We have operations in Spain, Mexico, Peru, El Salvador, Guatemala, Venezuela, Colombia, Panama, Nicaragua, Ecuador, Uruguay, Argentina and Chile, all of which operate under the Movistar brand as of April 2005, and through our joint ventures with Portugal Telecom, we also provide wireless communication services in Brazil and Morocco. At December 31, 2004, we provided wireless services through our operating companies and joint ventures to approximately 74.4 million managed customers and our licenses and concessions covered markets with over 509 million people.

The following section provides a description of the markets in which we operate and includes information on our total revenues, customer churn and market share by geographic location.

We provide information on total revenues for our fully consolidated operations and equity investments such as Medi Telecom. In Brazil, we provide information on total net revenues for fiscal year 2002 (which reflect the total revenues of Tele Sudeste, Celular CRT and Tele Leste Celular). These companies were fully consolidated in our statement of operations until their transfer to Brasilcel on December 27, 2002. After their transfer, we ceased reporting revenues by the individual operating companies in the Brasilcel joint venture. Instead, we now report revenues at the Brasilcel joint venture level. As a result, the revenue figures for Brasilcel for fiscal years 2003 and 2004 are presented on a proportional basis to reflect the proportional consolidation of the joint venture in 2003.

We provide customer churn rates for each of our wireless operations described below. We calculate churn rates by determining the number of customers whose wireless service is discontinued during a period, whether voluntarily or involuntarily, divided by the average number of customers during the period. We determine when service is discontinued according to different criteria in the different countries in which we operate, and therefore calculate churn differently for our customers in Spain, Latin American countries and Morocco.

Customer information on the wireless markets in which we operate, including our market share, are estimates that we have based on annual reports and press releases made public by our competitors or information from local regulators in the respective markets. With respect to our operations in Morocco, this customer information is also based on data collected from interconnection fees charged and paid in this market.

Spain

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We offer wireless services in Spain through Telefónica Móviles España, the leading wireless operator in Spain in terms of total number of customers at December 31, 2004. Telefónica Móviles España had approximately 19.0 million customers at December 31, 2004, representing an estimated 48.5% market share. Telefónica Móviles España is a wholly owned subsidiary and is our most significant operating company, accounting for 69% of our consolidated net revenues from operations for 2004.

The following table presents, at the dates and for the periods indicated, total net revenues and other statistical data relating to the operations of Telefónica Móviles España:

	Year ended December 31,		
	2002	2003	2004
Total net revenues from operations (euro in millions)	6,770	7,496	8,190
Total customers (in millions at period end) (1)	18.4	19.7	19.0

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	Year ended December 31,		
	2002	2003	2004
Pre-paid customers (in millions at period end) (1)	11.9	11.7	9.7
Population in service territory (in millions at period end)	42	43	44

Source: Telefónica Móviles

- (1) In July 2004, we decided to stop counting 1.3 million inactive prepaid SIM cards in our reported customer base. This adjustment was made as of April 1, 2004 and all the operating metrics corresponding to 2004 have been calculated taking this adjustment into account.

The Telefónica Group has offered wireless services in Spain since 1982 with the launch of analog wireless services under the brand MoviLine. Digital wireless services, using GSM 900 MHz technology, were launched in 1995 under the MoviStar brand name, which has since become one of the most widely recognized brands in Spain. In 1997 Telefónica Móviles España launched the first pre-paid wireless service in Spain under the MoviStar Activa brand name, and in January 1999 Telefónica Móviles España launched the GSM 1800 MHz service. In March 2000, having achieved the highest rating in the award process, Telefónica Móviles España was awarded a third generation wireless, or UMTS, license covering the Spanish national territory for 131 million.

Market

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

The Spanish wireless market has shown growth as a result of a decline of wireless handset prices and per minute call rates, and the introduction of pre-paid tariffs. At December 31, 2004, Telefónica Móviles España had approximately 19.0 million customers. The number of contract customers totaled approximately 9.3 million, representing a 16.8% increase compared to 2003.

Telefónica Móviles España believes that, to date, it has been successful in preserving its advantage in terms of absolute numbers of customers and quality of average customer in terms of minutes of usage. Telefónica Móviles España estimates that its traffic market share is higher than its customer market share.

Network and Technology

Telefónica Móviles España's licenses and concessions in Spain permit it to operate digital networks and analog networks. Since December 31, 2003, Telefónica Móviles España has not operated an analog network, having moved its analog MoviLine subscribers to GSM Movistar services. Telefónica Móviles España also holds one of four nationwide licenses for UMTS services in the country.

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Telefónica Móviles España's digital network in Spain is based upon the GSM standard. The prevalence of the GSM standard, together with Telefónica Móviles España's international roaming agreements, enables its MoviStar customers to make and receive calls throughout Western Europe and in almost 200 countries worldwide. Telefónica Móviles España's GSM-based network provides its customers with access to many of the most advanced wireless handsets and a full panoply of services and products.

In 2002, 2003 and 2004, Telefónica Móviles España invested in the aggregate approximately 1,669 million in building out and enhancing its networks in Spain, developing its technological platforms and information systems. At December 31, 2004, Telefónica Móviles España's GSM/GPRS digital network in Spain, which consisted of 115 switching centers and more than 16,200 base stations, provided coverage to approximately 99% of the population. The amounts invested in 2002, 2003 and 2004 have been used to enhance the quality of its coverage of high-density areas, to permit more intensive use of its wireless services within buildings in an urban environment, further enhancing the appeal of wireless communications and to introduce new technologies. In addition, Telefónica Móviles España has continued to roll-out its UMTS network in 2004, complying with its obligations under its UMTS license. By the end of the year, Telefónica Móviles España's UMTS network provided coverage to 40% of the population, with 3,800 base stations in approximately 100 cities.

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The Spanish wireless market has been receptive to new wireless services, such as SMS and wireless internet. Telefónica Móviles España has offered GPRS services, with higher speed data transmission than existing GSM networks, since 2001. Multi-media messaging services, or MMS, which allow customers to send and receive messages combining color photographs and images with voice, sound, animation or text, have been offered by Telefónica Móviles España since 2002. Telefónica Móviles España remains committed to being a leader in technological innovation in Spain and to making the most innovative services available to its customers. The following new services and data applications were launched or developed in 2004:

GPRS technology continued developing significantly in 2004. Telefónica Móviles España estimates that close to 3.8 million of its customers were web browsing using GPRS technology during the month of December 2004, almost 2.4 million more compared to December 2003. During December 2004, following the launch of i-mode navigation services as part of its e-moción brand in June 2003 under a general collaboration agreement with NTT DoCoMo, almost 700 thousand of Telefónica Móviles España's web browsing customers were using the i-mode service.

Utilization of multimedia messaging services (MMS) continued to grow in 2004, with almost 1.5 million users during the month of December 2004 (compared to 0.5 million during December 2003). Almost one half of the handsets sold by Telefónica Móviles España in 2004 were equipped with MMS technology.

With regard to the corporate and professional segment, Telefónica Móviles España launched its *Oficin@ Movistar* UMTS GPRS/UMTS data card—the first 3G service offered by a mobile operator in Spain with high-speed data transmission up to 384 kbits/s to its corporate customers on February 13, 2004. This service was extended to all Telefónica Móviles España residential and prepaid customers on May 24, 2004, initially in Madrid and Barcelona, and is gradually being extended to the major urban areas in Spain. On May 24, 2004, Telefónica Móviles España also launched the first UMTS videophone service in the Spanish market.

Telefónica Móviles España has continued to compete for high-value customers and the corporate segment by developing new value-creating products, services and solutions. During the fourth quarter of fiscal year 2004, Telefónica Móviles España stepped up the commercialization of services such as *Movistar desktop* and *Blackberry Professional Mail* with attractive offers for its devices. Telefónica Móviles España also launched the TSM 520 handset, primarily targeted at these segments, with the Windows Mobile Smartphone 2003 system built in.

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

Sales and Marketing

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

Telefónica Móviles España utilizes all types of marketing channels, including television, radio, exterior signage, telemarketing, direct mail and internet advertising. Telefónica Móviles España also sponsors a leading motorcycle grand prix racing team and cultural and sporting events in order to increase its brand recognition.

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

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

Telefónica Móviles España offers several different pricing options for wireless services. At December 31, 2004, approximately 49% of Telefónica Móviles España's total customer base are contract customers, and the remainder are pre-paid (*MoviStar Activa*).

In 2004, Telefónica Móviles España continued to encourage customer migration from its pre-paid plans to its contract plans, in line with the process that started in March 2002, when the contract plans of Telefónica Móviles España shifted from a monthly fee to a minimum usage commitment. In 2004, prepaid to contract migrations stood at over a million, contributing to an improvement in the contract weight to the total customer mix by 8.5 percentage points as of December 31, 2004 compared to December 31, 2003.

The tariffs and quality of services provided by Telefónica Móviles España, along with its success in encouraging migration to its contract plans, have led to improvement in the usage and spending patterns of its customers. Total traffic increased to 30.4 billion minutes in 2004, a 12% increase compared to 2003. In addition, data and content services are becoming increasingly important methods by which wireless customers in Spain communicate.

Customer Care

One of Telefónica Móviles España's principal business objectives is to strengthen its relationship with its customers. As the Spanish market for wireless services continues to mature and competitive pressures increase, Telefónica Móviles España believes that it must enhance customer loyalty in order to maintain its customer base and to increase revenues. For this reason, its focus has been shifting from customer acquisition to quality of service and customer care.

We have developed loyalty programs implemented by Telefónica Móviles España for both our contract and pre-paid customers. The *MoviStar Plus* program, for example, offers contract customers the ability to exchange points earned based on monthly usage for new handsets. The *Estrena Plan* allows pre-paid customers to upgrade their handsets and benefit from special offers (attractive prices of handsets and free traffic). In 2004, there were over 3.6 million handset upgrades based on loyalty programs of Telefónica Móviles España.

At December 31, 2004, Telefónica Móviles España maintained 19 customer relations centers with real time access to its information systems. These call centers handled approximately 60.3 million calls in 2004.

In addition, Telefónica Móviles España has launched client attention services. The monthly invoices for the corporate customers can be personalized according to their needs. Pre-pay customers can view a detailed breakdown of their calls on the Telefónica Móviles España website, and the balance remaining on their pre-pay cards.

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Telefónica Móviles España provides e-business services designed for its large corporate customers including a portal with billing facilities that provides on-line billing customization to customers and distributors through the Hermes system, which provides up-to-date information on news, products and services catalogs, events and promotions. Telefónica Móviles España's average monthly customer churn rate was 1.6% for 2004.

Competition

Telefónica Móviles España currently has two competitors in the Spanish market for wireless communications service: Vodafone España, a subsidiary of Vodafone PLC, and Retevisión Móvil S.A., which operates under the trade name *Amena*.

Morocco

We provide wireless services in Morocco through Medi Telecom, S.A., in which we hold a 32.18% interest and share management responsibilities with Portugal Telecom, which holds a 32.18% interest in Medi Telecom as well. Medi Telecom is also owned by local minority shareholders. Medi Telecom S.A. is the second largest wireless

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

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

The following table presents, at the dates and for the periods indicated, total net revenues and other statistical data relating to our investment in Medi Telecom:

	Year ended December 31,		
	2002	2003	2004
Total net revenues from operations (euro in millions)(1)	230	274	336
Total wireless customers (in millions at period end)	1.6	2.06	2.73
Pre-paid customers (in millions at period end)	1.5	1.93	2.62
Population in service territory (in millions at period end)	30	30	31

Source: Telefónica Móviles, except population

Population: Pyramid Research

(1) Medi Telecom has been consolidated pursuant to the equity method for each of the years ended December 31, 2002, 2003 and 2004. We held 30.5%, 32.18% and 32.18 % of Medi Telecom at year end December 31, 2002, 2003 and 2004, respectively.

Market

With a population of approximately 31 million people, Morocco is an attractive wireless market with a high potential for growth. Morocco had 9.13 million wireless customers at December 31, 2004 representing a penetration rate of 29%. Medi Telecom estimates that the Moroccan market grew 25.5% in 2004 when compared to 2003.

Network and Technology

Medi Telecom's network in Morocco is based upon the GSM standard. In 2002, 2003 and 2004, Medi Telecom invested a total of approximately 252 million in building out and enhancing its digital network in Morocco. At December 31, 2004, Medi Telecom's digital network in Morocco consisted of 13 switching centers and 1,689 base stations providing coverage to over 96% of the population. Medi Telecom has been offering wireless internet since April 2001.

Sales and Marketing

Medi Telecom's sales and marketing strategy has been to generate rapid customer growth. At December 31, 2004, approximately 96% of Medi Telecom's customers used pre-paid plans with the remainder using contract service. Medi Telecom plans to target business customers and the more affluent segments of the consumer market in the short-term. Medi Telecom also intends to expand the range of services offered to its customers.

Customer Care

Medi Telecom believes that an emphasis on its customer service will enable it to distinguish itself from its competitor in Morocco. Medi Telecom maintains customer relations call centers with real time access to its information systems. The call centers in Morocco handled approximately 8.8 million calls in 2004. Medi Telecom's average monthly churn rate was 2.3% in 2004.

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Competition

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

Latin America

Latin America is an attractive telecommunications market with a population of approximately 512 million people and a combined gross domestic product of approximately \$1.9 trillion in 2004. Since the introduction of wireless services in Latin America in the late 1980s, they have experienced significant growth. The average penetration rate in Latin America as a whole was 30.3% at year-end 2004. The wireless services industry is focusing on increasing penetration and expanding the use of voice service, wireless internet services and wireless data transmission services, through the introduction of 2.5G technologies such as GSM/GPRS and CDMA/CDMA 1XRTT.

The Latin American wireless communications market has been shaped by several underlying trends that are likely to cause growth in this market to continue, including the following:

Market liberalization. Deregulation of the Latin American telecommunications markets, which has allowed for the entry of new competitors and the granting of new licenses, has resulted in increased competition for substantially all telecommunications services and products. Competition in these markets has increased the availability of advanced wireless services and reduced prices, which