Press release

Telefónica O2 Czech Republic – 2010 Nine Months Financial Results

November 10, 2010

Telefónica O2 Czech Republic, a.s. announces its unaudited financial results for the first nine months of 2010. These results are consolidated and prepared according to International Financial Reporting Standards and fully include the results of Telefónica O2 Slovakia, Telefónica O2 Business Solutions and other smaller operating companies.

Operational Highlights

- Solid mobile customer growth in the Czech Republic in 3Q 2010 driven by 37 thousand contract net additions.
- ADSL accesses grew by 11.3% year-on-year, with 20 thousand net additions in the quarter, best figure year to date.
- Consolidated business revenues went down 7.0% year-on-year in 9M 2010, with a 7.8% decline in 3Q 2010 due to additional MTR cuts and lower ICT revenues.
- OIBDA increased by 5.6% year-on-year in 9M 2010 due to an impairment reversal booked in 3Q 2010, confirming Company's positive view of the fixed business. On fully comparable basis[1], OIBDA declined by 6.1% year-on-year in 9M 2010.
- Continuous OpEx savings and MTR cuts allowed the Group to decrease the operating expenses by 6.7% year-on-year (excl. T-Mobile settlement in 2Q 2009) and to improve comparable OIBDA margin[2] by 0.1 p.p. year-on-year to 44.0% in 9M 2010.
- Telefónica O2 Slovakia maintained its healthy commercial momentum (73 thousand net adds in the quarter) and improved its financial performance, reaching positive OIBDA in 3Q 2010
- Full year guidance[3] confirmed for OIBDA and CAPEX.

"I am pleased that our continuous focus on the valuable customer proposition allowed us to maintain solid commercial momentum in our focused areas. Customers' interest in our NEON tariffs resulted in further growth of mobile contract base and improvement in customer mix, while broadband centric proposition still helps to improve number of ADSL lines and to decelerate fixed accesses' disconnections. In Slovakia we kept healthy customer growth and recorded positive OIBDA in the third quarter. Our revenues have been impacted by additional MTR cuts and lower ICT revenues in the quarter. Nevertheless, we maintained the comparable OIBDA margin flat year-on-year reaching robust 44% in the first nine months of 2010 on the back of strict cost control, while improving quality of services. Additionally, our net profit improved by 16.5% year-on-year helped by non-recurring impairment reversal confirming our positive outlook for the fixed business, " says Jesús Pérez de Uriguen, the Chief Financial Officer and the First Vice-Chairman of the Board of Directors of Telefónica O2 Czech Republic when commenting on the operator's financial results.

[1] OIBDA excluding brand fees and non-recurring items (9M 2009: universal service, gain from real estate and settlement agreement with T-Mobile totaling CZK 1,536 million; 9M 2010: universal service, restructuring costs and impairment reversal totaling CZK 3,937 million).
[2] Comparable OIBDA over Comparable business revenues (business revenues excluding universal service: CZK 345 million in 9M 2009 and CZK 34 million in 9M 2010).
[3] OIBDA decline of -5% to -9%, CapEx around CZK 6 billion. In terms of 2010 guidance calculation, OIBDA excludes brand fees (CZK 754 million in 2009). In addition, 2009 OIBDA base excludes non-recurring items (settlement with T-Mobile, universal service and gain from real estate sale) totaling CZK 1,548 million; 2010 guidance excludes changes in consolidation, assuming constant FX rates of 2009.

Consolidated Financial Statements

Consolidated **business revenues** went down 7.0% year-on-year to CZK 41,597 million in 9M 2010 with a 7.8% year-on-year decline to CZK 13,832 million in 3Q alone. The financial performance of the Group in 3Q 2010 was impacted by additional MTR cuts, lower number of ICT projects for public office sector and USO booked in 3Q 2009. Excluding the impact of USO[4], Group business revenues would have declined 6.4% year-on-year in 9M 2010 and 6.8% year-on-year in the quarter. Fixed business revenues in the Czech Republic declined by 8.9% year-on-year to CZK 18,255 million in 9M 2010 (-7.5% year-on-year excluding the USO impact) and by 11.7% to 5,982 million in 3Q 2010 (-9.6% year-on-year excluding the USO impact). Mobile revenues in the Czech Republic declined by 8.4% to CZK 21,444 million in 9M 2010 (-4.3 % year-on-year excluding the impact of MTR cuts) and by 8.2% to CZK 7,134 million in 3Q 2010, (-4.5 % year-on-year excluding the impact of MTR cuts). On the other hand, revenues in Slovakia confirmed sound growth and recorded a 54.1% year-on-year increase to reach EUR 78.9 million in 9M 2010 (+59.3% in 3Q 2010). Moreover, in 3Q 2010 Telefónica O2 Slovakia recorded a positive OIBDA.

The Company continued in its effort to realize savings in operating costs which have been reported already in previous quarters, to compensate for drop in revenues. As a result, consolidated **operating costs** reached CZK 24,499 million in 9M 2010, down 2.9% year-on-year and CZK 7,947 million in 3Q 2010, down 5.6% year-on-year. The year on year comparison year-to-date has been impacted by the settlement agreement with T-Mobile (CZK 1,027 million) booked in 2Q 2009. Excluding this item, consolidated costs would have declined by 6.7% in 9M 2010. It is worth highlighting a 12.9% reduction in personnel expenses in 3Q 2010, which confirms a positive impact of restructuring program announced in 1Q 2010. The Group headcount declined by 13.7% year-on-year to reach 7,716 as at 30 September 2010. In 3Q 2010 alone, the Group headcount has been reduced by 582 employees.

An impairment loss related to fixed cash generating unit (CGU) of CZK 9,909 million was booked by CESKY TELECOM (predecessor of Telefónica O2 Czech Republic) in 2003 as a reaction on unclear and potentially negative development of the telecommunication market and regulatory environment. Since that time, regular impairment tests were performed annually. Recent impairment test, while considering Company's fixed broadband and data focused strategy, enhanced fixed network performance as well as continuous synergies from integration with mobile segment, resulted into the impairment loss reversal reaching CZK 4,343 million in 3Q 2010, thus positively impacting OIBDA in that amount.

In addition impairment reversal increased depreciation and amortization (CZK 142 million in 3Q 2010) and income tax (CZK 798 million in 3Q 2010). Consequently, the positive impact of impairment reversal on net income amounted to CZK 3,402 million in 3Q 2010 as well as year-to-date.

Group **Operating income before depreciation and amortization (OIBDA)** improved by 5.6% year-on-year reaching CZK 21,610 million in 9M 2010 and by 53.4% to CZK 10,401 million in the quarter. Excluding the impact of impairment reversal, OIBDA would have dropped by 15.6% year-on-year to CZK 17,267 million in 9M 2010 (-10.6% to CZK 6,058 million in 3Q 2010) largely due to revenues decline, non-recurring gain from real estate sale booked in 1Q 2009 (CZK 341 million), settlement agreement with T-Mobile in 2Q 2009 (CZK 1,027 million) and negative impact of restructuring costs (CZK 428 million) booked in 1H 2010. **OIBDA margin** increased by 6.2 p.p. year-on-year to reach 52.0% in 9M 2010 and by 30.0 p.p. to reach 75.2% in 3Q 2010. **Comparable OIBDA**[5] decreased by 6.1% year-on-year to CZK 18,307 million in 9M 2010 (-9.1% year-on-year to 6,261 million in 3Q 2010), while **comparable OIBDA margin**[6] improved by 0.1 p.p. to reach 44.0% in 9M 2010 (-1.1 p.p. year-on-year to 45.3% in 3Q 2010).

Consolidated **net income** amounted to CZK 10,367 million in 9M 2010, up by 16.5% year-on-year, largely due to the impairment reversal. Excluding the impact of impairment reversal, consolidated net income would have

[4] CZK 345 million in 9M 2009 and CZK 34 million in 9M 2010

[5] OIBDA excluding brand fees and non-recurring items (9M 2009: universal service, gain from real estate and settlement agreement with T-Mobile totaling CZK 1,536 million; 9M 2010: universal service, restructuring costs and impairment reversal totaling CZK 3,937 million).

[6] Comparable OIBDA over Comparable business revenues (business revenues excluding universal service: CZK 345 million in 9M 2009 and CZK 34 million in 9M 2010).

declined 21.7% in 9M 2010 and 17.7% in 3Q 2010 on the back of decrease in OIBDA, which has not been fully compensated by lower depreciation and amortization and lower income tax expense.

Consolidated **CAPEX** reached CZK 3,728 million in 9M 2010, down by 17.8% year-on-year (-17.3% year-on-year in 3Q). Similarly to the previous quarters, the Company continued to invest in expansion of its mobile broadband networks (EDGE and UMTS), enhancement of fixed broadband network as well as development of IT systems in 3Q 2010. At the end of October 2010, the mobile 3G network was available in 74 towns and their urban areas, which represents 40% of the Czech population. At the same time, investment in EDGE network expansion also advanced to reach 98% of the population coverage.

Group **free cash flows** increased by 31.4% year-on-year to reach CZK 11,619 million in 9M 2010, largely due to lower income tax payments and less CAPEX related cash payments.

The consolidated **financial debt** amounted to CZK 2,976 million at 30 September 2010 resulting into 4.9% decline compared to the end of 2009 on the back of appreciation of the Czech currency. **Cash and cash equivalents** and short term financial investments reached CZK 12,892 million at the end of September 2010, up from CZK 1,378 million at the end of 2009. In 3Q 2010, the Company continued in accumulating cash for a dividend payment (CZK 12,884 million) which was made on 6 October 2010, i.e. in 4Q.

CZ Mobile Business Overview[7]

Mobile business continued to maintain solid commercial performance in mobile contract segment leveraging on successful customer proposition around O_2 NEON tariffs. Overall financial performance in 3Q 2010 has been impacted by additional MTR cut from CZK 1.96 to CZK 1.66 effective from 1st July 2010, while underlining mobile revenues performance excluding incoming voice (MTR impact) shows continuous improving trends seen already in previous quarter.

Total **mobile customer base** reached 4,856 thousand at the end of September 2010, a 1.4% decline year-on-year, impacted by the disconnection of 111 thousand inactive contract customers in 2Q 2010. Excluding the disconnection, the customer base would increase by 0.9% year-on-year. Number of **contract customers** went up 2.6% year-on-year reaching 2,819 thousand at the end of 3Q 2010 (+6.7% year-on-year excluding cleanup adjustment made in 2Q) with 36.7 thousand net adds in the quarter (115.2 thousand net adds in 9M 2010 excluding the impact of disconnection in 2Q 2010). This performance was driven by continuous uptake of O_2 NEON tariffs and by customers migrating from the prepaid to the contract segment. Number of **prepaid active customers** reached 2,038 thousand at the end of 3Q 2010, down by 6.4% year-on-year. It is worth to highlighting further improvement in prepaid customer base development. In 3Q 2010, number of prepaid customers declined by 22.8 thousand compared to net losses of 34.5 thousand and 35.4 thousand in 2Q and 1Q respectively. At the end of 3Q 2010, contract customers represented 58.0% of the base (+2.3 p.p. year-on-year).

The blended monthly average **churn rate** totaled 2.4% in 9M 2010 posting a 0.5 p.p. year-on-year increase mainly due to the cleanup disconnections made in the contract base in 2Q 2010.

In terms of usage, **mobile traffic**[8] carried by the customers in the Czech Republic grew by 7.9% year-on-year to 6,558 million minutes in 9M 2010.

In 9M 2010, **blended ARPU**[9] reached CZK 469.9, down 8.8% year-on-year, also due to MTR cuts. However, the year-on-year decrease in ARPU decelerated from -7.9% year-on-year in 2Q to -7.4% year-on-year in 3Q 2010 as a result of stabilization in customer spend. **Contract ARPU** reached CZK 665.8 in 9M 2010, down by 12.3% year-on-year, while in 3Q its decline slowed down to -10.1% year-on-year to reach CZK 669.5. This improvement was largely the result of stabilization in spend seen already in 2Q. In addition, customer migration from prepaid to the contract tariffs and MTR cuts continued to contribute to contract ARPU dilution. **Prepaid ARPU** decreased by 8.6% year-on-year to reach CZK 203.8 in 9M 2010 with a 7.5% decline to CZK 205.1 in 3Q.

[7] Figures are shown net of inter-segment charges between fixed and mobile businesses
[8] Inbound and outbound, including roaming abroad, excluding inbound roaming
[9] Including inter segment revenues

Total mobile **business revenues** in the Czech Republic declined by 8.4% to CZK 21,444 million in 9M 2010 with a 8.2% decline in 3Q 2010, while mobile service revenues went down by 8.4% year-on-year and only 8.1% year-on-year in 9M and 3Q respectively due to above mentioned MTR cuts and stabilizing spend. Mobile termination rate cuts diluted mobile service revenues by 4.2 p.p. and 3.8 p.p. in 9M and 3Q 2010. Despite 7.8% year-on-year growth in mobile outbound voice traffic in 9M 2010, traffic revenues decreased by 10.8% year-on-year to CZK 6,337 million (-11.4% in 3Q), due to higher number of customers opting for semi-flat rate tariffs (O_2 NEON). Interconnection revenues went down by 21.4% year-on-year to CZK 2,800 million in 9M (-25.3% in 3Q), largely impacted by MTR cuts and lower incoming traffic. Other revenues (including SMS & MMS, data and other business revues) declined by 5.1% year-on-year in 9M 2010 with a lower decline rate (-0.7%) in 3Q 2010 confirming lower customer optimization from 2Q.

CZ Fixed Business Overview[10]

The fixed business reported solid commercial performance in broadband customer base and fixed accesses. As expected and communicated earlier in the year, the financial performance in 3Q 2010 was negatively impacted by lower ICT revenues due to less projects for public office sector and already mentioned universal service.

Total number of **fixed accesses** declined by 5.8% year-on-year to reach 1,686 thousand at the end of September 2010, with 23 thousand net losses in the quarter (by 22.8% less compared to 2Q 2010 and by 31.8% less compared to 1Q 2010) helped by solid uptake of naked accesses following the introduction of new broadband centric proposition in 2009. The positive impact of the broadband strategy has been also proven by household access performance.

Voice traffic generated in the fixed network went down 13.2% in 9M 2010 to 1,318 million minutes as a result of continued fixed telephony lines losses and fixed to mobile substitution effect.

Number **of ADSL accesses** reached 777 thousand at the end of 3Q 2010, up 11.3% year-on-year with 20.1 thousand net additions in the quarter, while total number of **O_2 TV customers** reached 131 thousand.

Total fixed **business revenues** went down 8.9% year-on-year to CZK 18,255 million in 9M 2010 (-7.5% year-on-year excluding the USO impact), while they decreased by 11.7% to CZK 5,982 million in 3Q (-9.6% excluding the USO impact). **Revenues from traditional accesses** fell by 27.1% year-on-year to reach CZK 3,934 million in 9M 2010 (-15.4% in 3Q) due to continuous fixed telephony lines losses and introduction of broadband centric customer proposition in 2009, while **Internet & broadband revenues** increased in total by 22.3% year-on-year to CZK 4,476 million in 9M 2010. **IT services and business solutions revenues** increased by 2.1% year-on-year to reach CZK 1,525 million in 9M 2010, while dropping by 26.4% year-on-year in 3Q alone due to expected lower number of projects realized in public office sector.

Slovakia

In 3Q 2010, Telefónica O2 Slovakia continued in its sound commercial performance and delivered strong financial performance leveraging on successful customer proposition based on value and simplicity strategy (O_2 Fér). Total **number of active customers** reached 781 thousand at the end of September 2010, up by 68.7% year-on-year, with 72.5 thousand net adds in the third quarter. Number of **contract customers** grew by 82.2% year-on-year to reached 286 thousand, while number of **prepaid active customers** increased by 61.7% year-on-year to reach 495 thousand at the end 3Q 2010. Contract customers represented 36.7% of total customer base at the end of 3Q 2010, up 2.7 p.p. year-on-year. **Total revenues** of Telefónica O2 Slovakia in local currency increased by 54.1% year-on-year to reach EUR 78.9 million in 9M 2010, with a 59.3% year-on-year growth in 3Q alone to EUR 30.1 million. As expected and indicated in the previous quarters, Telefónica O2 Slovakia reported positive **OIBDA** in 3Q 2010. **Contract ARPU** reached EUR 19.15 and EUR 19.7 in 9M and 3Q respectively, while **prepaid ARPU** was at EUR 8.49 and EUR 8.8 in these periods.

[10] Figures are shown net of inter-segment charges between fixed and mobile businesses

Attachment:
The consolidated balance sheet and income statement of Telefónica O2 Czech Republic prepared in accordance with International Financial Reporting Standards (all figures in CZK million).

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About Telefónica O2 Czech Republic

Telefónica O2 Czech Republic is a major integrated operator in the Czech Republic. It is now operating more than six million lines, both fixed and mobile, making it one of the world's leading providers of fully converged services. The organization offers the most comprehensive portfolio of voice and data services in this country. It is paying special attention to the exploitation of the growth potential, particularly in the data and Internet sector. Telefónica O2 Czech Republic operates the largest fixed and mobile network including a 3rd generation network, CDMA (for data), and UMTS, enabling voice, data and video transmission. Telefónica O2 Czech Republic is also a notable provider of ICT services.

About Telefónica Europe

Telefónica Europe is a business division of Telefónica comprising mobile, fixed, and DSL operations in the UK, Ireland, the Isle of Man, Germany, the Czech Republic, and Slovakia. With the exception of Isle of Man, all the operating businesses use 'O2' as their consumer brand. Telefónica Europe also has 50% ownership of the UK and Irish Tesco Mobile and German Tchibo Mobilfunk joint venture businesses. Telefónica Europe is headquartered in Slough, UK, and has 49 million mobile and fixed customers.

INCOME STATEMENT	Jan – Sep 2010	Jan – Sep 2009
Business revenues	41,597	44,742
Other recurring revenues	144	66
Revenues	**41,742**	**44,808**
Internal expenses capitalized in fixed assets	460	565
Operating expenses	(24,499)	(25,238)
Other operating income/(expenses)	(422,1)	2
Gain on sale of fixed assets	2	358
Impairment of fixed assets	4,327	(23)
OIBDA	**21,610**	**20,471**
Depreciation and amortization	(8,610)	(9,014)
Operating Income	**13,000**	**11,457**
Net financial income (expense)	(155)	(142)
Income before tax	**12,845**	**11,315**
Income tax	(2,478)	(2,419)
Net Income	**10,366**	**8,896**

BALANCE SHEET	30.9.2010	31.12.2009
Non-current assets	**79,576**	**80,316**
- Intangible assets	8,304	9,029
- Goodwill	13,448	13,448
- Property, plant and equipment and investment property	57,649	57,545
- Long-term financial assets and other non-current assets	175	294
- Deferred tax assets	0	-
Current assets	**22,565**	**12,357**
- Inventories	515	618
- Trade and other receivables	8,920	9,664
- Current tax receivable	238	697
- Short-term financial investments	14	109
- Cash and cash equivalents	12,878	1,269
Non-current assets classified as held for sale	**35**	**95**
Total assets	**102,176**	**92,768**
Equity	**71,225**	**73,879**
Non-current Liabilities	**6,761**	**6,422**
- Long-term financial debt	2,831	3,044
- Deferred tax liabilities	3,884	3,333
- Long/Term Provisions	20	24
- Other long/term liabilities	26	21
Current Liabilities	**24,190**	**12,467**
- Short-term financial debt	145	87
- Trade and Other payables	8,848	9,384
- Current tax payable	4	(1)
- Short-term provisions and other liabilities	15,193	2,997
Liabilities assoc. with non-current assets classified as held for sale	**0**	**-**
Total Equity and Liabilities	**102,176**	**92,768**