Half-Year report 2011

The financial figures and information stated in this Half-Year Report are not audited.

Telefónica Czech Republic, a.s. here and throughout the Report as well as Telefónica CR or the Company

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1. Letter from the Chairman of the Board of Directors

Dear Shareholders

Allow me to look back at the activities and results of the Telefónica Czech Republic Group in the first half of 2011.

Given the challenging external environment, I consider our results for the first six months of this year as satisfactory. We succeeded in maintaining a solid growth of our customer base in key areas, which include fixed and mobile broadband internet and mobile contract customers. It shows that our strategy – to offer services which respond to the customers' needs – is on the right track. Our simple and comprehensible market proposition helped us to maintain our customer adds momentum in Slovakia.

In the past half-year, the household spending continued to be weak which resulted in only a slow recovery of our customers' spend, while the demand in the government segment declined, which impacted mainly our revenues from ICT services. Our results were also influenced by the regulation, especially further cuts in mobile termination rates and lower roaming prices. In addition, we had to contend with strong competitive pressures in all areas of our business.

In the fixed access segment, the launch of VDSL-based broadband internet further improved the competitive position of our offer, which has been met with a lot of interest from our existing customers and which will help us maintain our Average Revenue Per User (ARPU) and reduce the churn rate. The popularity of our xDSL services helped to sustain a two-digit rate of growth of their user base and slow down the rate of decline in the number of fixed accesses. This, together with our measures focused on the reduction of the decline of traditional voice lines, succeeded in slowing down the rate of fixed accesses' decline by 6.2% year on year in the first half of 2011 to 58 thousand.

In the mobile segment we continued with the migration of our prepaid customers to contracts. The growth in the mobile internet contract customer base helped us achieve an increase of 93 thousand in the total mobile contract customer base in the first half year and out-perform the competition. Our small business and home office customers benefited from an improved access to our call centre operators and dedicated priority service desks staffed with qualified assistants which we set up in selected brand stores. In March, we cut the data roaming prices – both the base rates and the prices of the majority of bundles. Our pricing offer for surfing online within the EU was the most competitive on the market.

As regards mobile broadband internet, we continued to roll out our 3G network coverage. Early in the year we entered into an agreement with T-Mobile for the construction and sharing of 3G network infrastructure in areas which were not yet covered. This will assist us with accelerating the rate of network roll-out and bring the benefits of mobile broadband to even more customers. At the end of June, our 3G network was available to approximately 55% of the Czech population, confirming our market leadership. Together with the expansion of our mobile data networks we also improved our service proposition. We changed the way we bill for mobile data usage to customers who go online only occasionally and we paid a lot of attention to promoting the advantages of having internet in a mobile to customers, in order to increase the penetration of smartphones in our customer base. In relation to this we launched a marketing campaign by the name of Now I Know Why which guides customers through their first steps in the world of applications. Already after the first month of the campaign the rate of users of small-screen internet service more than doubled compared to the level before the campaign.

In Slovakia, we continued to offer our simple and comprehensible tariffs *O_2 Fér* and *O_2 Moja firma* for entrepreneurs. The new tariff *O_2 Filip* set out to satisfy the needs of the higher-value consumer customer. Despite the fact that the competition was trying hard to copy our market proposition, we succeeded in maintaining our strong rate of growth in our customer base, improve its structure and the loyalty of customers. The Customer Satisfaction Index in Slovakia has been hitting record marks for quite some time and we controlled our advantage over the rest of the field. At the end of the first half of the ear, the number of customers in Slovakia hit the one million mark. At the same time we strengthened our position in the Slovak mobile market, with our market share rising almost two percentage points since the start of the year to 16.6%. The growth in the customer base was accompanied by improved financial performance. Our revenues grew almost 50% year on year in the first half of the year and the company posted a positive operating profit OIBDA.

In the first half of 2011 we upheld our focus on operating efficiency in both commercial and non-commercial areas. Our goal is to maintain a high operating profitability in the time of significant pressures on our revenues, which will boost our competitiveness and maintain the value of the business. As in the last year, we carried on with the implementation of our restructuring programme which seeks to leverage our human capital and deliver personnel cost savings.

As I am reviewing our financial results and listing the factors that have impacted on them and on the trends of the first half of the year, I have to mention again the adverse macroeconomic climate, the effect of the regulation and the competition, which was fierce especially in some customer segments. Our consolidated business revenues went down 6.7% to CZK 25.9 billion in the first half year. Revenues from the mobile segment in the Czech Republic recorded a 9.7% year-on-year decline, down to CZK 12.9 billion, which was caused by a slow recovery in the customer spend and the mobile termination rate cuts, while the revenues from the fixed access segment were down 7.9% year-on-year, reaching CZK 11.3 billion. In this instance, the incremental revenues from broadband internet failed to offset the decline of revenues from voice and ICT services. Revenues in Slovakia were up 50% to EUR 73.1 million. In the first half of 2011, OIBDA reached CZK 10.3 billion, which is a year-on-year decline of 8.3%. OIBDA margin, excluding brand and management fees, remained, with 42%, at about the level of the previous year, which is the result of our dedicated campaign for efficient expenditure in both the commercial and non-commercial areas. Net profit was down 17.1% to CZK 3.6 billion; the decline was driven by the lower OIBDA, and a slight increase of depreciation and amortization, which was not fully compensated for by the lower tax.

Despite the fact that our first-half results do not meet our full-year expectation, I confirm, on behalf of the Company, our 2011 year-end guidance for OIBDA, which is a decline within the range of 1-5%, and capital expenditure, which should reach approximately CZK 5.7 billion.

I am confident that the second half of the year will see some recovery in the mobile market where we aspire to maintain our leadership position. We will continue with our investments in the expansion of our 3G network coverage, driving for higher average revenue per user of mobile services. The continued growth in our customer base and revenues from the Slovak market will positively impact on our profitability. In the Czech Republic we plan to focus on strict cost control with a view to compensate for as much as possible of the revenue decline, and we want to maintain a high level of operating efficiency.

Luis Antonio Malvido
Chairman of the Board of Directors

2. Calendar of key events of 2011

January

Telefónica CR went live with its new website www.o2.cz, and at the same time introduced the e-bill for mobile services.

February

Telefónica CR its audited consolidated financial results prepared under International Financial Reporting Standards for the fiscal year 2010. Consolidated business revenues reached CZK 55.7 billion; the net profit rose to CZK 12.3 billion.

Vladimír Dlouhý was co-opted as member of the Supervisory Board to step in for Jaime Smith Basterra who had resigned from office.

Telefónica CR and T-Mobile Czech Republic a.s., signed a 3G network sharing agreement. The sharing arrangement concerned areas not yet covered with proprietary networks. The joint process helped to accelerate network roll-out and significantly enhanced 3G coverage of both operators. Telefónica CR took over more than 11,000 consumer ADSL accounts from VOLNÝ, a.s.

Telefónica CR joined Think Big the long-term pan-European CSR programme of the Telefónica Group. The programme helps young people with making their ideas and projects reality – to benefit the communities in which they live.

March

Telefónica CR's project of a network portal for developers was voted the IT Project of the Year 2010 by the Czech Association of Information Technology Managers.

Employees raised CZK 394,265 to help the victims of the earthquake and tsunami in Japan. Telefónica CR matched this amount, thus raising the collection to CZK 788,530. The donation went to the humanitarian organisation ADRA.

Telefónica CR, looking to help parents with their reintegration back to work after a parental leave, launched an online presentation titled Mom and Dad at www.chcidoo2.cz.

April

According to independent survey by Ipsos Tambor, Telefónica CR had the best mobile data service and the best mobile internet coverage, ranking it the leader in mobile internet.

Telefónica CR launched VDSL, a new technology with up to three times faster internet for the home.

Telefónica CR's new campaign headlined 'Martin and Lucie' for entrepreneurs and small businesses brought a number of new products and improved standards of customer care to this segment.

Telefónica Slovakia's new tariff O2 Filip came with unlimited free calls to all numbers in the O2 network in Slovakia.

An Ordinary General Meeting of shareholders of Telefónica CR was held. The shareholders approved, among other things, a proposal of the Board of Directors for the payment of a dividend of

CZK 40 per share before tax. Vladimír Dlouhý was elected a new member of the Supervisory Board and a substitute member of the Audit Committee.

May

Telefónica changed the corporate name of its Czech operation to Telefónica Czech Republic, a.s. (from Telefónica O2 Czech Republic, a.s.).

Dana Dvořáková joined the Company as new Director of Corporate Communications.

Telefónica CR appointed a special O2 customer support team which operates in social networks; the team provides assistance, consultations, advice and answers questions from customers via the official facebook and twitter accounts and the O2 YouTube channel in section O2 Guru.
June
Telefónica CR reduced its carbon footprint by 5,000 tons of CO_2 and recycled 269 tons of waste electrical equipment.

The Company kicked off its campaign ‘Now I Know Why’ which seeks to explain the potential having small-screen internet to customers.

3. Board of Directors' Report on Business Activity

3.1. The Czech telecommunications market in the first half of 2011

In the first six months of 2011, the telecommunications market in the Czech Republic continued to decline as a result of a slow recovery in consumer spend, additional mobile termination rates (MTR) cuts and the competitive pressures in selected customer segments.

The mobile market was dominated largely by introduction of new data services.

At the beginning of the year, Telefónica CR introduced a cost-optimised new way of charging for mobile services. Customers paid CZK 15 for the first hour of connection and the maximum amount of CZK 30 for a full day (FUP data limit was 30 MB/day). Especially customers who surf the internet on their mobile only occasionally benefited from the new mobile data pricing.

T-Mobile Czech Republic, a.s. (T-Mobile) came out with three new data bundles for contract and prepaid customers (Twist Internet in Mobile for A Week, Twist Internet for Travelling for A Month and Internet for Travelling for A Day). T-Mobile also introduced new data roaming tariffs, in both a "One Day" and "One Week" option.

Vodafone Czech Republic a.s. (Vodafone) launched mobile data roaming tariffs for the occasional data user in February: Passport Data for A Day and Passport Data for Good. The tariffs allow for the local monthly tariff being used also for going online in selected countries.

In March, Vodafone expanded its internet access portfolio when it added Connect for Two Days tariff, which is designed mainly for the occasional user of mobile internet.

Since March 2011, Telefónica CR cut the prices of its baseline offer of data roaming services for all zones; the largest price cut was for the EU zone, from CZK 240/MB down to CZK 24/MB, which is approximately 90%. The prices for roaming data bundles were also reduced by a significant margin.

Just before the holidays, all operators cut their prices of data roaming and voice services.

An independent survey by Ipsos Tambor showed that Telefónica CR had the best mobile data services and the best mobile internet coverage. The respondents confirmed that Telefónica CR is the leader in mobile internet among all operators.

In March, T-Mobile launched Magic Tuesdays, a new concept of customer benefits which replaced the company's previous Bonus programme. Bonus remained in effect only for medium business and large corporate customers.

From April, Telefónica CR introduced a number of improvements in the way it serves its entrepreneur and small business clientele. Telefónica CR among other things abolished the interactive voice response system in the call centres. The customer is now put directly through to the live operator. Selected brand stores have been fitted with special priority desks staffed with qualified assistants for business customers.

During the first half of the year, all mobile operators continued to modernize 3G networks and expand their coverage in the Czech Republic.

In February, Telefónica CR and T-Mobile signed an agreement to share their 3G networks in areas which are not yet covered. The shared infrastructure will in the future include approximately 1,000

BTS, with each operator committing to building a half of them. Telefónica CR will cover the eastern part of the Czech Republic, while T-Mobile will do the western part of the country.

As part of the 3G network sharing arrangement with T-Mobile, Telefónica CR standardised its methodology for the calculation of population coverage. At the end of June, the Company covered 55% of the population with its 3G network, thus confirming its leadership among mobile operators.

Two new virtual operators went live in the Czech Republic at the beginning of the year. OpenCall, which uses the CDMA network of U:fon operated by MobilKom a.s. (MobilKom), offers wireless fixed access and mobile voice in the form of a prepaid card. The second one, Mujoperator, also uses U:fon’s network infrastructure to carry its services.

Several changes in the ownership relationships of companies occurred in the Czech fixed market during the first half of 2011.

The Office for the Protection of Economic Competition consented in January to the sale of České Radiokomunikace, a.s., to funds managed by Macquarie of Australia. The seller, Falcon Group, also owns almost 40% of T-Mobile.

In February, MobilKom, which operates the U:fon mobile network, announced a change in its ownership. Divenno Holdings, the parent company of Dial Telecom, a.s., acquired 100% of the shares in the company.

Also in February, UPC Česká republika, a.s. (UPC) took over Sloane Park Property Trust, a.s., which allowed UPC to interconnect the backbone optical networks of both companies. UPC established UPC Business, a unit dedicated solely to serving the business customer. In March, UPC also opened its first data centre in Prague.

In the fixed access segment, VOLNÝ, a.s., decided to terminate the provision of ADSL internet to the residential segment as part of its new strategic direction. Approximately 11 thousand of household accounts were taken over by Telefónica CR. The migration commenced in mid-March 2011 and the service parameters and the prices remained the same.

In February, MobilKom came out with a new proposition of fixed internet access using the ADSL technology, which complemented MobilKom’s existing portfolio of prepaid and postpaid mobile internet. MobilKom buys fixed line connectivity wholesale from Telefónica CR.

In early May, Telefónica CR launched its new VDSL technology, which offers up to three times faster broadband internet for the home. Existing customers were given a faster internet connection at no extra charge. The technology was available to approximately 45% of households which are within a 1.3 kilometre radius from the switch.

3.1.1. Regulation

Several changes occurred during the first half of 2011 in the regulatory environment which governs the field of electronic communications in the Czech Republic. The most material changes included the following:

- Enactment of the Government Resolution No. 156/2011 Coll., amending the Government Resolution No. 154/2005 Coll., on the determination of the amount and method of calculation of fees for using radio frequencies and numbers, as amended;
- Enactment of the Government Decree No. 53/2011 Coll., amending the Decree No. 117/2007 Coll., on network numbering plans and electronic communications services, as amended;

- Enactment of the Decree No. 22/2011 Coll., on the method of determination of coverage of terrestrial radio broadcasting over selected frequencies;
- Continuation of the implementation of the revised regulatory framework for electronic communications networks in the Czech law:
  - Directive 2009/136/EC of the European Parliament and of the Council of 25 November 2009 amending Directive 2002/22/EC on universal service and users' rights relating to electronic communications networks and services; Directive 2002/58/EC concerning the processing of personal data and the protection of privacy in the electronic communications sector and Regulation (EC) No. 2006/2004 on cooperation between national authorities responsible for the enforcement of consumer protection laws;
  - Directive 2009/140/EC of the European Parliament and of the Council of 25 November 2009 amending Directives 2002/21/EC on a common regulatory framework for electronic communications networks and services, Directive 2002/19/EC on access to, and interconnection of, electronic communications networks and associated facilities, and 2002/20/EC on the authorisation of electronic communications networks and services;
  - Regulation (EC) No. 1211/2009 of the European Parliament and of the Council of 25 November 2009 establishing the Body of European Regulators for Electronic Communications (BEREC) and the Office.

Telefónica CR was involved in the preparation of the above legislation by providing consultation either directly or on the platform of industry associations of telecommunications operators or through its parent company Telefónica, S.A.

Relevant markets analysis and product regulation

Telefónica CR continued to meet its duties with which it was tasked based on the relevant markets analysis undertaken by the Czech Telecommunication Office (CTO) in previous periods.

On 1 January 2011, the regulated wholesale price of mobile termination went down from CZK 1.66/minute to CZK 1.37/minute.

Further in January, the CTO issued a decision by which it gave a mandate to Ernst & Young, s.r.o., to develop a LRIC methodology and a model for the service of call termination in fixed public networks. The outputs from this project will be used by the CTO for the determination of maximum call termination prices for fixed public networks in late 2012 and early 2013.

Also in January 2011, the CTO decided to appoint the Asset Valuation Institute of the University of Economics in Prague to deliver a calculation of a WACC value for the purposes of regulation in the sector of electronic communications. Telefónica CR expects that the updated WACC will be used for the determination of regulated prices from 2012 onwards.

In February 2011, the CTO embarked on the third round of analysis of the relevant market No. 5 – wholesale broadband access in electronic communications networks. Telefónica CR expects that the analysis will be published in the form of a general measure by the end of 2011.

In April 2011, the CTO issued a decision, reflecting on the results of its analysis of the relevant market No. 6 – wholesale terminating segments of leased lines irrespective of the technology used for the provision of leased or reserved capacity, which changed the regulatory measures applicable to Telefónica CR in this market. Based on the decisions, pricing regulation no longer applies to the wholesale service. The imposed regulatory measures newly apply also to Ethernet leased lines.

Imposition of duties in connection with the Universal Service provision

Telefónica CR provided the following services as part of meeting its duties imposed by the CTO in relation to the Universal Service provision:

a) the public payphone service;
b) access to the public telephone service, of the same quality as for other end users, for people with disabilities, namely by means of special terminal equipment;
c) special price plans for persons with disabilities, which are different from the regular price plans provided under the standard commercial terms and conditions.

For services under a), a CTO decision from 2009 reduced the number of payphones included in the Universal Service in 2011. The duty to operate payphones as part of the Universal Service concerned municipalities under 4,999 residents.

For services under c), a CTO decision imposed on Telefónica CR the requirement to provide the Universal Service component for special prices for a period of three years starting from 2 July 2011.

Government policy in the area of broadband internet

In January 2011, the Czech government approved a State Policy in the Area of Electronic Communications – Digital Czech Republic. The strategy deals with the development of ICT, with a special emphasis on bridging the digital divide between urban and rural areas. The document set the following objectives:

1. to ensure that broadband internet with the minimum (downlink) speed of 2 Mb/s, and 10 Mb/s in towns, is available in all populated locations in the Czech Republic by 2013;
2. to ensure that, by 2015, broadband internet is available in all rural settlements, with a speed which will equal at least 50% of the average broadband speed in towns. 30% of homes and businesses in towns should have internet with a speed of at least 30 Mb/s available to them.

As part of the process to implement the policy Digital Czech Republic, the Ministry of Industry and Trade published the first draft of the development criteria for the planned auction of frequencies in the so-called 'digital dividend' band.

Continued support from the EU Structural Funds allowed ICT projects to continue in public institutions. The funding was directed mainly into the building of regional networks interconnecting public institutions, and also in the business sector. Telefónica CR was successful in tendering for public contracts financed with structural funding.

In April, the European Commission started the process of public consultation in the Community concerning the state aid rules with regard to fast roll-out of broadband networks.

3.2. Telefónica Czech Republic Group in the first half of 2011

The corporate names of some companies in the Telefónica Czech Republic (the Group Telefónica CR or the Group) changed in the first half of 2011: with effect from 10 May 2011, the corporate name of Telefónica O2 Slovakia, s.r.o., changed to Telefónica Slovakia, s.r.o. (Telefónica SK); with effect from 16 May 2011, the corporate name of Telefónica O2 Czech Republic, a.s., changed to Telefónica Czech Republic, a.s (Telefónica CR or the Company). The corporate names of the other members of the Group remained without change. The changes related to the effort to harmonize the corporate names of all European companies belonging to the group of Telefónica, S.A. In addition to the Czech Republic and Slovakia, Telefónica will be the one corporate brand also in the United Kingdom, Germany and Ireland. O_2 remains the commercial brand of Telefónica CR.

In the context of the fiercely competitive telecommunications market, in the first half of 2011 Telefónica CR continued to improve its services, build up the relationship with its customers, develop and market new products and services in growth areas. The Company's strategy was focused on maximum accommodation of customers' demands in fixed and mobile broadband internet and mobile voice services for contract customers. This effort resulted in a solid growth in the customer base and, depending on the segment, maintenance or growth of the market share.

The net additions of mobile contract customers of 93 thousands ensured a 57% share of total market net additions for Telefónica CR. The result was also aided by the continued demand for mobile data services and the related expansion of the mobile data portfolio. Telefónica CR also continued to expand the coverage of its 3G mobile network based on a network sharing arrangement with T-Mobile. In February, the Company entered into an agreement with T-Mobile to share 3G network infrastructure in not yet covered areas of the Czech Republic. At the end of June 2011, 3G services were available to approximately 55% of the population.

The expanding 3G network coverage propelled the market interest for small-screen internet and mobile internet. As the demand grew, so did the penetration of smartphones in Company's customer base, which was approximately 16% at the end of June and represented a 6 percentage point year-on-year increase. In the first half of the year, the share of smartphone sales in the total handset sales was approximately 50%. In order to stimulate demand for small-screen internet, Telefónica CR launched a new marketing campaign with Google and Samsung in June. The campaign 'Now I Know Why Have Internet in A Mobile' demonstrates the advantages of having small-screen internet and how smart applications can make people's lives easier. The campaign yielded its first results already in June, when the monthly incremental increase in the number of small-screen internet users more than doubled compared to the previous two months.

In the area of fixed broadband internet, the Company is pursuing its strategy to offer the best internet service in the marketplace and to strengthen its competitive position, to which end it focused on improving its services. In early May, Telefónica CR started to offer a VDSL service. Compared to ADSL, the new VDSL technology offered customers up to three times faster internet, while the prices for existing customers remained the same. The purpose was to retain the existing higher-value customers and to reduce churn. During a period of less than two months (until the end of June), the VDSL service was opted for by more than 40,000 customers, and in July already 9% of residential customers were using it and enjoying the benefits it brings. Telefónica CR thus managed to maintain its more than ten percent year-on-year growth in the number of xDSL customers, despite the highly competitive environment in the marketplace.

In Slovakia, the Group continued to offer its tariffs O_2 Fér and added a special tariff for entrepreneurs, small and medium business customers – O_2 Moja Firma. In April, a new tariff, O_2 Filip, was added to the portfolio, to capture higher-value customers with a view to increasing ARPU. Telefónica SK's attractive proposition to the market assured a strong growth and improvement of the quality of the customer base, which in turn led to a significant rise in revenues and financial performance. In the first half of 2011 the company posted a positive OIBDA.

All above-mentioned activities produced a solid operating result in terms of customer base growth. The number of xDSL customers reached 841 thousand at the end of the first half of 2011, which is an 11.1% year-on-year increase. The number of O_2 TV customers reached 130 thousand at the end of the first half year. As at the same date, the number of fixed accesses operated by Telefónica CR was 1.6 million. During the first six months of 2011, their number went down by 58 thousand, which is 6.2% less than in the same period of 2010. The number of mobile customers increased 0.5% to 4.9 million despite the highly saturated market. The increase was driven mainly by the growth in the number of contract customers, of which there were almost 3 million at the end of June, which is an increase of 6.5%. In the second quarter their number went up 57 thousand – the best result since 2009. The decline in the number of prepaid customers slowed down to 63 thousand in the first half of the year, compared to 70 thousand in the same period of 2010; in the second quarter alone, the number was down by only 15 thousand, which is the mildest drop since 2009. The number of mobile customers in Slovakia was up 122 thousand in the first half of 2011 and at the end of June stood at 1,003 thousand.

As in the previous years, also in the first half of 2011 the Company continued its campaign to improve its operating efficiency. The implementation of a restructuring programme which followed on the 2010 restructuring continued, and produced a Group-level headcount reduction of 192, down to 7,329 in the first half of 2011. In relation to the programme, the Company posted restructuring costs of CZK 158 million in the first half of the year.

As at 30 June 2010 and 2011, the total headcount of the Telefónica CR Group was the following in the geographical breakdown:

	As at 30 June	
	2010	2011
Telefónica Czech Republic, a.s.	7,647	6,767
Telefónica O2 Business Solutions, spol. s r.o.	243	162
Employees in the Czech Republic	**7,890**	**6,929**
Telefónica Slovakia, s.r.o.	408	400
Employees in Slovakia	**408**	**400**
Group headcount total	**8,298**	**7,329**

3.2.1. Telefónica Slovakia

In the first half of 2011, Telefónica SK continued to market its successful services O_2 Fér and O_2 Moja Firma, the latter of which is a tariff for entrepreneurs, small and medium business customers. In early April, Telefónica SK introduced O_2 Filip, a postpaid tariff for residential customers with a choice of three price points. The main selling point of the service was calls within the O_2 which were free right from the first second of call. Customers also welcomed a 'wallet' which gave them freedom to pick and choose their services for any given month. A customer would prepay a certain volume of service – 'load the wallet' – and use the credit for SMS, calls to other mobile networks or data services in a proportion that they could change every month as they wished.

In the first half of the year, Telefónica SK directed a lot of effort to covering the territory with its proprietary 3G network which started offering service on commercial basis on 18 July 2011. On that date, the network covered approximately 30% of the Slovak population and by the end of August the coverage expanded further to reach one third of all population. Together with the launch of the 3G network, the company came out with two new 3G data bundles in Slovakia – one for small-screen internet and the first ever internet for notebook PC (big screen).

At the end of June 2011, Telefónica SK's own network covered already 94.9% of the Slovak population, which gave the company the leverage to carry 90% of traffic in its proprietary network. The remaining 10% of calls were still connected through national roaming. The share of on-net calls grew one percentage point year on year.

An independent survey by Ipsos Tambor for Telefónica SK revealed that Telefónica SK still has the highest score in the Customer Satisfaction Index among all mobile operators in Slovakia. The Customer Satisfaction Index (CSI) reached a historically record level and the company increased its lead over the nearest competitor.

As at 30 June 2011, Telefónica SK had 1,003 thousand customers, of which 411 thousand were contract customers. This represents a year on year growth in the customer base of 41.5%, which gave Telefónica SK the leverage to strengthen its position in the Slovak mobile market, where it held a 16.6% share at the end of June – up 1.9 percentage point compared to the end of 2010. Since the implementation of number portability (in November 2007) until 30 June 2011, customers ported already 313 thousand numbers to Telefónica SK.

The revenues of Telefónica SK reached EUR 73.1 million in the first half of 2011, which is up 49.8% year on year. The company also posted a positive Operating Income before Depreciation and Amortisation (OIBDA) for the first half year.

3.2.2. New products and services

On 27 January 2011, Telefónica CR changed the way it bills for occasional use of mobile data services. Users now pay CZK 15 for the first hour of connection, and CZK 30 for a full day. The daily FUP data limit was set at 30 MB. The new method of billing is economical especially for occasional use of mobile internet. To those who want to go online wherever and whenever via their mobile phone, the Company offered the postpaid O_2 Internet on Your Mobile Start for CZK 150 per month, O_2 Internet on Your Mobile for CZK 300 per month for even a more demanding user. The new method of billing applied equally to new and existing customers. The billing unit of time became activated when a data link was established. Within the frame of the billing unit the customer can download data continuously – but they can also pause the transmission. The customer is informed via SMS right after going online that the service is being billed.

For its customers who use the fixed line, Telefónica CR introduced new tariffs and bundles with calls to all mobile networks in the Czech Republic priced from CZK 2 per minute. Customers who call international benefited from a new service which offered calls to international fixed lines in 47 countries of the world priced from CZK 2 per minute. New tariffs and bundles O_2 Calling Mobile and O_2 Calling International can be combined depending on the most frequently called destinations. They can be used in pairing with fixed voice tariffs with free calls to fixed networks in the Czech Republic. For attractive prices, customers could call in all directions. The offer could be subscribed by residential customers, entrepreneurs and small businesses. O_2 Calling Mobile was activated by approximately 15 thousand customers in 6 months.

For new and existing mobile prepaid customers, Telefónica CR prepared a new cut-price call offer valid from the beginning of March. All users of the tariffs NA!HLAS or NA!PIŠTE could call three O_2 numbers of their choice for only CZK 0.50 per minute for up to six months.

From 1 March, the Company cut its data roaming prices – both in the baseline offer and for the majority of roaming bundles. The largest price cuts were for the EU zone, with prices slashed from CZK 240/MB to CZK 24/MB. The new pricing for the EU zone was the most competitive offer on the market. The zone encompassing the rest of Europe saw the prices cut from CZK 420/MB to CZK 240/MB, and the rest of the world from CZK 660/MB to CZK 300/MB. For roaming bundles available to both contract and prepaid customers, the prices were reduced to CZK 60/2 MB, CZK 120/4MB, CZK 240/10 MB and CZK 1,200/50MB. Additionally, the price for the roaming bundle EURODATA 250 MB was cut from CZK 2,388 to CZK 480 from 1 April. The benefits of this bundle product were welcomed especially by frequent travellers in the EU who need to use data roaming regularly. With regard to the reduced data roaming prices, EU limit, a service which makes sure that customers travelling in EU countries do not exceed a specific limit, also changed: the limit of CZK 1,176 now allows 49 MB of data.

Those of Telefónica CR's customers who are self-employed or run a small business could get 30% extra free minutes of calls to all networks with their O_2 Business or O_2 NEON tariff. If they simultaneously activated a second SIM card, they got 50% of free minutes extra. In order to improve the customer satisfaction in this segment, Telefónica CR stopped using the interactive voice response (IVR) system in its call centre from April; the customer was put through directly to a live operator. Especially for business customers, special priority desks were set up in selected brand stores, staffed with trained specialists. The priority desks were available from mid-April in 60 stores in the Company's retail network and their number has been steadily rising. At the beginning of April, Telefónica CR launched a new communication campaign to promote its proposition to entrepreneurs and business customers. The stars of the campaign are two cartoon characters, Martin and Lucie. The campaign sought to promote the benefits that are delivered by the products and improvements in customer care.

From 9 May 2011, Telefónica CR has a new fixed broadband internet using the VDSL technology on the market. VDSL is capable of delivering up to three times faster internet to the home. Existing customer had their home internet speed increased without any extra charge. Telefónica CR also introduced new fixed internet prices for download speeds up to 25 Mb/s and upload speed of up to 2 Mb/s. Existing customers got a speed upgrade without any extra charge above what they had been paying for home internet. If a customer committed for 12 months, they could claim a modem for only CZK 1. Customers who were not within the reach of VDSL could enjoy a host of O_2 Extra discounts with a number of retail partners. When committing for 12 months, these customers got a prepaid Mobile Internet set worth CZK 995 for only CZK 1. Customers of the tariff O_2 Internet Pro with the speed of up to 16 Mb/s were migrated to Internet Aktiv for a lower price of CZK 850 per month. Customers could choose one of the two new VDSL tariffs – Internet Optimal with a download speed of up to 16 Mb/s or Internet Aktiv with a download speed of up to 25 Mb/s and an upload speed of up to 2 Mb/s. Telefónica CR at the same time introduced promotional pricing for new customers willing to commit for 12 months. With the commitment, Internet Optimal cost CZK 500 compared to the listed price of CZK 700 per month; Internet Aktiv could be ordered for CZK 600 compared to the standard listed price of CZK 850.

Together with the marketing campaign 'Now I Know Why' in June, Telefónica CR introduced other new products and services for the users of small-screen internet. The upgraded O_2 Active portal and the O_2 official facebook page newly feature the section Mobile Applications. Customers can use a detailed guide through the world of applications and small-screen internet – either in print or through a special application Now I Know Why. In partnership with Samsung, Telefónica CR prepared an offer of smartphones for 'smart prices' and a special small-screen internet package for young people. In order to facilitate customers' first steps in the world of mobile applications, the Company introduced a number of innovations to customer care. A special team of operators now dispense advice and assistance in social networks – on the official facebook page and via the Company's twitter feed. The four-member team of specialists is available every day from 8am until 8pm including weekends to give assistance, advice and answer questions. Detailed video tutorials on the official YouTube feed in section O_2 Guru and specialists in O_2 brand stores were also available by way of assistance and advice.

Existing customers in the corporate segment benefited from Telefónica CR's offer of faster asymmetrical broadband internet connection using the VDSL technology and also a faster symmetrical internet connection, including a seamless migration from Internet Forte to Internet Business service.

From 1 May, Telefónica CR cut the prices of most mobile handsets for corporate customers. The new prices were much more competitive – in comparison with both the offers from other mobile operators and unaffiliated e-shops.

On 15 May, Telefónica CR introduced 'Exclusive Customer', a new proposition to corporate customers. Any company subscribing to all basic services (fixed voice, fixed internet, mobile voice) could apply for the status of Exclusive Customer, which came with premium benefits such as better customer care, proactive optimisation, special handset prices, personal assistance over a telephone and many others, to reward the customer for their loyalty, improve satisfaction and create opportunity for up-selling of new services from Telefónica CR. The Company believes that the new proposition will help it strengthen its market position in this highly competitive segment.

At the same time as it launched its new website www.o2.cz on 1 February 2011, Telefónica CR started to offer e-bill functionality. An electronic bill in section My O_2 gives an overview of fixed and mobile usage of customers. By implementing this feature, the Company responded to the market demand for this type of billing and improved its customer care.

3.2.3. Commented financial results

In this section we present and comment on the unaudited consolidated financial results of the Telefónica CR Group including the results of Telefónica Czech Republic, a.s. (Telefónica CR or the parent company), Telefónica Slovakia, s.r.o., Telefónica O2 Business Solutions, spol. s r.o. and other smaller operating companies. The results were prepared according to International Financial Reporting Standards (IFRS).

Consolidated Financial Statements

Consolidated business revenues went down 6.7% year on year to CZK 25,898 million in 1H 2011 (-7.2% year on year in 2Q to CZK 13,033 million). The financial performance of the Group was impacted by the prevailing competitive pressure largely in corporate and SMB mobile segments, MTR cuts, and lower ICT revenues. Fixed business revenues in the Czech Republic declined 7.9% year on year reaching CZK 11,300 million in 1H 2011(-7.6% year on year in 2Q 2011, down to CZK 5,657 million). At the same time, the mobile revenues in the Czech Republic declined 9.7% down to CZK 12,925 million in 1H 2011 and 10.7% year on year down to CZK 6,504 million in 2Q. With the impact of MTR cuts excluded, the growth rates would be at -7.0% and -5.0% in 1H and 2Q 2011, respectively. On the other hand, revenues in Slovakia continued to grow steadily and recorded a 49.8% year-on-year increase, reaching EUR 73.1 million in 1H 2011 (+46.7% year on year, up to EUR 38.5 million in 2Q 2011 alone).

In 1H 2011, the Company continued in its effort to deliver cost efficiencies in both commercial and non-commercial areas, to compensate for pressure on the revenues. Despite the higher commercial activity, largely in fixed and mobile broadband areas, the total consolidated operating costs were down 4.1% year on year, reaching CZK 15,867 million (-5.0% excluding brand fees and management fees); the situation was also positively influenced by MTR cuts. The positive impact coming from 2010 and 1H 2011 restructuring programs led to a 9.7% year-on-year reduction of personnel expenses in 1H 2011. The total Group headcount reached 7,329 at the end of June 2011, down 11.7% year on year. In 1H 2011, the headcount has been reduced by additional 192 employees.

Group's Operating Income Before Depreciation and Amortisation (OIBDA) reached CZK 10,275 million in 1H 2011, -8.3% year on year (-11.2%, down to CZK 5,205 million in 2Q 2011 alone). In 1H 2011, Telefónica SK recorded a positive OIBDA again, reaching individual millions of EUR in the period. At the same time, the guided OIBDA[1] fell 6.8% year on year, reaching CZK 10,845 million in 1H 2011, while the OIBDA margin remained almost flat at 41.7%, on the back of the already mentioned focus on cost efficiency and profitability improvement in Slovakia.

Depreciation and amortization charges went up 1.0% year on year in 1H 2011, impacted by an impairment reversal booked in 3Q 2010 (higher gross value of fixed assets), as commented on in

[1] In terms of 2011 guidance calculation, OIBDA excludes brand fees and management fees (CZK 423 million in 1H 2010 and CZK 551 million in 1H 2011), assuming constant FX rates of 2010.

the previous quarters. Consolidated net income amounted to CZK 3,611 million and CZK 1,871 million in 1H and 2Q 2011, down 17.1% and 20.1% year on year, respectively, due to the decline in OIBDA and the higher depreciation and amortization, which were not fully compensated by the lower financial expenses and the lower income tax expense.

Consolidated CapEx reached CZK 2,554 million in 1H 2011, up 7.4% year on year. In line with the strategy to focus its investments into growth areas, the Company continued to target investments into capacity expansion and quality improvement of 3G network. In addition, CapEx was spent on a further expansion of the 3G network coverage, including the coverage of currently unserved areas on the basis of a network sharing contract with T-Mobile. The Company increased the 3G population coverage to ~ 55% as at the end of June 2011. Additionally, the Company focused its investments into the upgrade of the fixed broadband network in connection with the launch of a new VDSL-based customer proposition on 9 May 2011, which was aimed at strengthening of the Company’s position on the highly competitive fixed broadband market in the Czech Republic. In Slovakia, CapEx was largely spent on additional network investment related to the planned launch of 3G services in mid July.

Group free cash flows decreased 15.2% year on year, reaching CZK 6 billion in 1H 2011, as a combination of a 6.1% decline in cash from operating activities, better than recurring OIBDA decline and a 15.5% higher CapEx related cash payments due to the different CapEx phasing in 2011 compared 2010.

Consolidated financial debt amounted to CZK 3,111 million as at 30 June 2011, which produced a 2.9% growth compared to the end of 2010. Cash and cash equivalents reached CZK 10,820 million, up from CZK 4,798 million at the end of 2010, due to the accumulation of cash for the dividend payment in October 2011.

CZ Mobile Business Overview[2]

In 1H and largely in 2Q 2011, the mobile business continued to deliver a solid commercial performance in the mobile contract segment, which was supported by the market demand for mobile broadband services – in spite of the intense competitive pressure. The financial performance continued to be negatively impacted by the tough competition, MTR cuts (-30.1% year on year[3]) and the slow recovery of customer spend patterns.

The total mobile customer base reached 4,869 thousand at the end of June 2011, which is a 0.5% year-on-year increase. In 2Q 2011, the Company recorded 42.1 thousand net additions in its mobile customer base, the best figure in last seven quarters, on the back of the continuous strong contract base growth and a significant improvement in prepaid base. The number of contract customers went up 6.3% year on year, reaching 2,956 thousand at the end of 2Q 2011 with 56.9 thousand net adds in the quarter (+62.7% year on year, excluding the disconnection of 111 thousand inactive contract customers in 2Q 2010). This performance continued to be driven by customers migrating from the prepaid to the contract segment and the positive contribution of the growth in the number of mobile broadband customers. At the end of June 2011, contract customers accounted already for 60.7% of the base (+3.3 percentage points year on year). The number of prepaid active customers reached 1,912 thousand at the end of 1H 2011, down 7.2% year on year, with only 14.8 thousand net losses in the quarter, down from 47.9 thousand in 1Q 2011 and 62.6 thousand in 4Q 2010.

The blended monthly average churn rate reached 1.72% in 2Q 2011, posting a 1.1 percentage point year-on-year decrease (-0.3 percentage point excluding the impact of the disconnection of inactive

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

[3] From CZK 2.37 to CZK 1.96 in January 2010, to CZK 1.66 in July 2010 and to CZK 1.37 in January 2011

customers in 2Q 2010) and a 0.3 percentage point decline compared to 1Q 2011. This is a result of the improvement in prepaid churn (-0.6 percentage point year on year and -0.5 percentage points quarter on quarter), which was driven by the increased focus on acquiring higher-value customers and the success of the customer loyalty scheme, which rewarded for regular top-ups. The contract churn declined 0.1 percentage points year on year compared to 2Q 2010 and 1Q 2011.

In terms of usage, the total mobile traffic[4] from customers in the Czech Republic reached 4,433 million minutes in 1H 2011, up 1.0% year on year.

In 1H 2011, the mobile blended ARPU[5] reached CZK 426.4, down 8.9% year on year (-10.2% year on year, down to CZK 428.7 in 2Q alone), in which the MTR cuts played a part. With the impact of MTR cuts excluded, the total ARPU in 2Q 2011 would have declined 6.3% year on year. Voice ARPU dilution, which itself was driven by the intense competition and the slow recovery of customer spend patterns, were, for the most part, the key drivers of the decline. Contract ARPU reached CZK 586.9 and CZK 585.1 in 1H and 2Q 2011, down 11.6% and 13.1% year on year, respectively (-9.6% year on year in 2Q 2011, excluding the impact of the MTR cuts). Prepaid ARPU fell 8.6% and 9.2% year on year in 1H and 2Q 2011, reaching CZK 185.8 and CZK 190.1 in these periods (-4.3% year on year in 2Q 2011, excluding the impact of the MTR cuts). Data ARPU declined 1.9% and 2.5% year on year in 1H and 2Q 2011, reaching CZK 114.8 and CZK 114.5. As was the case in 1Q 2011, the cuts in data roaming prices and the continuous SMS/MMS bundling were the key drivers behind the data ARPU dilution. With the effect of these two factors discounted, the data ARPU would improve 5.4% year on year, with the mobile broadband customer base uptake remaining the key driver of the improvement.

The total mobile business revenues in the Czech Republic declined 9.7% to CZK 12,925 million in 1H 2011 and 10.7% year on year, reaching CZK 6,504 million in 2Q alone, while the revenues from mobile services went down 10.4% and 11.5% year on year in these periods, as a result of the above-mentioned competitive pressure, MTR cuts, slow recovery in spend and the lower data roaming prices. Mobile termination rate cuts diluted the mobile service revenues by 3.8 percentage points in 1H as well as in 2Q 2011. Despite the 1.0% year-on-year growth in the outbound mobile voice traffic, the traffic revenues decreased 16.8% year on year, down to CZK 3,505 million in 1H 2011 (-18.5% year on year in 2Q), as a result of the frequent traffic bundling and the competitive pressure. Interconnection revenues went down 28.2% year on year to CZK 1,400 million in 1H 2011, largely due to the MTR cuts and the lower incoming traffic. Other revenues (including SMS & MMS, data and other business revues) declined 2.7% year on year in total, reaching CZK 3,517 million in 1H 2011 (-2.7% year on year in 2Q), largely due to the lower data roaming prices and more SMS/MMS bundling. With the effect of SMS/MMS bundling and data roaming price cuts excluded, data revenues would report a 5.6% year-on-year growth in 1H 2011, confirming the positive impact of the growing contribution of revenues from mobile broadband services.

CZ Fixed Business Overview[6]

In 1H 2011, the fixed business recorded again a solid commercial performance in terms of the broadband customer base and a further slowdown of the rate of decline in the number of fixed accesses. Similarly to the previous periods, revenues from traditional voice services recorded a further decline; however the decline rate slightly decelerated in 2Q, aided by the better performance in transit revenues. Broadband revenues sustained the growth seen in the previous quarter, which is very relevant in the highly competitive fixed broadband environment. Additionally, the financial performance in 2Q 2011 continued to be impacted by the lower ICT revenues.

[4] Outbound and inbound, including roaming abroad, excluding inbound roaming

[5] Including inter-segment revenues

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

The total number of fixed accesses declined 5.7% year on year, reaching 1,611 thousand at the end of June 2011, with 58.4 thousand net losses in 1H 2011 (-6.2% year on year). The trend was supported by the steadily solid uptake of naked accesses and VoIP lines for corporate customers.

The number of xDSL accesses reached 841 thousand at the end of 2Q 2011, up 11.1% year on year. In 1H 2011, their number went up by 34.7 thousand, posting an 11.3% year-on-year growth. As was communicated already with respect to 1Q, on 9 May 2011 Telefónica Czech Republic launched its VDSL-based proposition, which offers the customers considerably higher speeds and enhances their experience. Already 41 thousand customers subscribed to the new service by the end of June 2011. The total number of O_2 TV customers reached 130 thousand at the end of 1H 2011.

Voice traffic generated in the fixed network went down 13.8% in 1H 2011 to 795 million minutes as a result of the continuing losses in the number of fixed accesses and the effects of fixed-to-mobile substitution.

In 1H 2011, the total fixed business revenues went down 7.9% year on year, to CZK 11,300 million. However, in 2Q alone, the decline rate decelerated to 7.6% year on year (-8.3% year on year in 1Q 2011 and -11.6% year on year in 4Q 2010). Revenues from traditional accesses fell 16.6% year on year in 1H as well as in 2Q 2011, reaching CZK 2,239 million in 1H 2011, due to continued losses of fixed accesses, while the revenues from traditional voice services went down 9.0% year on year, to CZK 3,398 million in 1H 2011. However, in 2Q alone, they declined by only 7.6% year on year; the positive effect came from the higher transit revenues posted in the quarter. Internet & broadband revenues increased 0.8% year on year in total in 2Q and 1H 2011, and reached CZK 3,012 million in 1H 2011, positively impacted by the growth in the number of xDSL customers, which is good news in the highly competitive fixed broadband market. Revenues from IT services and business solutions declined 6.8% year on year to CZK 959 million in 1H 2011 (-7.3% year on year in 2Q 2011), as a result of the lower number of projects in the government segment.

Slovakia

In 1H 2011, Telefónica SK continued to report a strong set of commercial and financial results, thus further strengthening its position in the Slovak mobile market. By the end of June 2011, the total number of active customers increased 41.5% year on year to a total of 1,003 thousand on 30 June 2011. The total subscribers net additions reached 122.2 thousand, driven by a growth in the contract customer base. The number of contract customers grew 59.1% year on year, reaching 411 thousand, which represents 76 thousand net additions over 1H 2011, while the number of prepaid active customers increased 31.4% year on year, ending up at 592 thousand at the end 1H 2011 (+46.2 thousand in 1H 2011). Consequently, the customer mix in Slovakia improved further and contract customers represented an already significant 40.9% share of total customer base, up 4.5 percentage point year on year. In terms of financial performance, the total revenues of Telefónica SK in the local currency increased 49.8% year on year to EUR 73.1 million in 1H 2011 (+46.7% year on year in the quarter to EUR 38.5 million, up from EUR 34.6 million in 1Q 2011), which had been fuelled by the strong base growth and also the year-on-year ARPU growth. In 1H 2011, Telefónica SK recorded a positive OIBDA again in the range of individual millions of EUR. In 2Q 2011, the contract ARPU reached EUR 18.2 (EUR 17.5 in 1Q), while the prepaid ARPU improved 2.4% year on year to EUR 8.7 (EUR 8.3 in 1Q).

Outlook for the second half of 2011

Based on the results delivered in the first half of 2011 and outlook for the second half, Telefónica CR Group confirms its full year guidance[7] for OIBDA and CapEx.

Telefónica CR believes that the overall performance of mobile market in the Czech Republic will marginally improve and produce a slower rate of decline in revenues compared to the first half year. The solid commercial achievements in contract customer base during the first half of 2011, when the Company captured close to 60% of the total market net additions, it expects it will maintain its relevant share of the mobile subscriber market.

In line with the further expansion of its 3G network coverage, the Company expects the growth trend of internet-capable handsets and mobile broadband customer base to continue. This will reflect in the growth of non-SMS data ARPU in the second half of 2011.

The strong commercial and financial results of Telefónica SK in the first half year will positively impact the Group's financial performance in the next six months. The operation in Slovakia is very efficient due to its leverage on finance, network, operations, IT and other back office functions in the Czech Republic. As a result, the expected continued revenue growth in Slovakia will directly flow to OIBDA. Consequently, OIBDA in the second half year should almost double compared to the level in the first six months.

In addition to the facts mentioned above, Telefónica CR Group will persevere in its effort focused on delivering maximum efficiency of commercial and non-commercial expenditure in order to compensate for the revenue decline and to sustain its operating profitability. Initiated already in the first half of the year, the restructuring program will result in a full-year group-level headcount reduction of approximately 7% and an approximately similar saving of related personnel expenses.

[7] OIBDA decline of -1% to -5%, CapEx around CZK 5.7 billion. In terms of 2011 guidance calculation, OIBDA excludes brand fees and management fees (CZK 1,057 million in 2010). In addition, 2010 OIBDA base excludes reversal of the impairment loss of CZK 4,343 million. 2011 guidance excludes changes in consolidation, includes potential capital gains from non core asset sales assuming constant FX rates of 2010.

4. Corporate governance

During the first half of 2011, the Board of Directors met twelve times, the Supervisory Board held two meetings and the Audit Committee (an independent governing body of the Company) met three times.

The Ordinary General Meeting of Telefónica CR was held on 28 April 2011. The supreme governing body of Telefónica CR approved the annual financial statements and the consolidated financial statements of the Company prepared under International Financial Reporting Standards (IFRS) for the year 2010. Both sets of financial statements were recommended by the Board of Directors to the General Meeting for approval and they had been verified by the auditors Ernst & Young who gave an unqualified opinion. The General Meeting approved the Board of Director's proposal for the distribution of profit and the payment of dividend. The proposal was based in a prudent analysis of the Company's results in the previous period, the current situation of the balance sheet and with regard to the Company's future outlook made by the Board of Directors, its investment plans and cash flow projections. The shareholders approved the payment of dividends from the profit made in the year 2010 of CZK 12,680,745,921.87 and a part of the retained earnings from the previous period of CZK 202,850,078.13, which is CZK 12,883,596,000 in total and a dividend of CZK 40 per share before tax.

The General Meeting also approved the proposal of the Board of Directors to amend the Company's Articles of Association. The corporate name of the Company was changed to Telefónica Czech Republic, a. s., which better reflects the Company's membership in the Telefónica Group (the change became effective as of 16 May 2011); the Company's website address also changed; the website is used, among other things, to publish announcements and disclosures to shareholders. The registered business of the Company was expanded to include the provision of low-value payments service pursuant to the Act No. 284/2009 Coll., on the payment system. Last but not least, the position and the remit of the Board of Directors were amended, and the number of members of the Audit Committee was reduced from six to five.

Changes in the personnel composition of the Company's governing bodies in the period from January until March 2011 are described in the Company's 2010 Annual Report (section Corporate Governance). No changes occurred in the personnel composition of the Board of Directors during the second quarter of the year. With respect to the Supervisory Board, the previously co-opted members were confirmed in their respective posts by a vote of the General Meeting. The members are Anselmo Enriquez Linares and Vladimír Dlouhý; their résumés are available on the Company's website, section About. The General Meeting also approved the execution of a contract for the performance of the office of a Supervisory Board member between the Company and Anselmo Enriquez Linares and Vladimír Dlouhý.

The General Meeting also voted into office Vladimír Dlouhý as substitute member of the Audit Committee.

Several changes occurred in the executive macrostructure of Telefónica CR compared to the situation published in the Company's 2010 Annual Report: as of 1 April 2011, the Strategy and Business Development Division was disbanded, while its units Customer Experience, Strategy and Market Intelligence and Wholesale have been transferred directly into the reporting line of the Chief Executive Officer. Another change occurred on 15 May 2011, when, following the departure of Jiří Šuchman, Director, External Affairs, the agenda of public affairs was spun off from the External Relations unit and subordinated to the Legal and Regulatory Affairs Division. The External Affairs unit at the same time changed its name to Corporate Communication, to better reflect its current agenda. Dana Dvořáková (her résumé is available at the Company's website, section About Us) was appointed Director of Corporate Communications.

All material information and documents relating to the corporate governance of Telefónica CR are available to shareholders and stakeholders on the Company's website (www.telefonica.cz).

The changes from the situation described in the 2010 Annual Report of Telefónica CR in respect of the subsidiary and affiliate companies, which occurred during the first half of 2011, concerned Telefónica Slovakia, s. r. o., and Telefónica O2 Business Solutions, spol. s r. o. The corporate name of Telefónica Slovakia, s. r. o., changed following the renaming of its parent company, with effect from 10 May 2011. As regards the subsidiary Telefónica O2 Business Solutions, spol. s r. o., in June 2011 the Board of Directors approved the plan to transform the company by spin-off into a newly incorporated subsidiary Internethome, s. r. o., which will provide electronic communications services. The spun-off company Telefónica O2 Business Solutions, spol. s r. o., will not be wound up and the transformation will become legally effective on the day of the record of the change in the Commercial Register.

Personnel composition of the Supervisory Board of Telefónica CR

(as at 1 August 2011)

Alfonso Alonso Durán	Chairman of the Supervisory Board
María Eva Castillo Sanz	1st Vice-chairman of the Supervisory Board
Lubomír Vinduška	2nd Vice-chairman of the Supervisory Board
Eduardo Andres Julio Zaplana Hernández-Soro	Member of the Supervisory Board
Antonio Botas Bañuelos	Member of the Supervisory Board
Vladimír Dlouhý	Member of the Supervisory Board
Anselmo Enriquez Linares	Member of the Supervisory Board
Tomáš Firbach	Member of the Supervisory Board
Petr Gazda	Member of the Supervisory Board
Pavel Herštík	Member of the Supervisory Board
Guillermo José Fernández Vidal	Member of the Supervisory Board
Luis Lada Díaz	Member of the Supervisory Board
Maria Pilar López Álvarez	Member of the Supervisory Board
Dušan Stareček	Member of the Supervisory Board
Ángel Vilá Boix	Member of the Supervisory Board

Personnel composition of the Audit Committee of Telefónica CR

(as at 1 August 2011)

María Eva Castillo Sanz	Chairman of the Audit Committee
Alfonso Alonso Durán	Vice-chairman of the Audit Committee
Pavel Herštík	Member of the Audit Committee
Maria Pilar López Álvarez	Member of the Audit Committee
Jaime Smith Basterra	Member of the Audit Committee
Vladimír Dlouhý	Substitute member of the Audit Committee

Personnel composition of the Board of Directors of Telefónica CR

(as at 1 August 2011)

Luis Antonio Malvido	Chairman of the Board of Directors
Jesús Pérez de Uriguen	1st Vice-chairman of the Board of Directors

Petr Slováček	2nd Vice-chairman of the Board of Directors
Martin Bek	Member of the Board of Directors
John Gerald McGuigan	Member of the Board of Directors
Jakub Chytil	Member of the Board of Directors
František Schneider	Member of the Board of Directors

Executive management of Telefónica CR

(as at 1 August 2011)

Luis Antonio Malvido	Chief Executive Officer
Martin Bek	Director, Support Services Division
Jiří Dvorjančanský	Director, Marketing Division
Dana Dvořáková	Director, Corporate Communication Division
Tony Hanway	Director, Consumer Division
Jakub Chytil	Director, Legal, Regulatory and Public Affairs Division, Company Secretary
Ctirad Lolek	Director, Human Resources Division
Jesús Pérez de Uriguen	Director, Finance Division
František Schneider	Director, Business Division
Petr Slováček	Director, Operations Division

5. Financial part

5.1. Interim condensed consolidated financial statements for the six months ended 30 June 2011 prepared in accordance with International accounting standard 34

General information

Telefónica Czech Republic, a.s. Group (the "Group") consists of Telefónica Czech Republic, a.s. (the "Company") and its subsidiaries: Telefónica Slovakia, s.r.o., Telefónica O2 Business Solutions, spol. s r.o., CZECH TELECOM Germany GmbH and CZECH TELECOM Austria GmbH.

The Company has a form of a joint stock company and is incorporated and domiciled in the Czech Republic. The address of its registered office is Za Brumlovkou 266/2, Prague 4, 140 22, Czech Republic.

The Group is a member of the Telefónica Group of companies (the "Telefónica Group") with a parent company, Telefónica, S.A. (the "Telefónica").

The Company is the principal supplier of fixed line telecommunication services and is one of the four suppliers of mobile telephone services in the Czech Republic.

The Company’s shares are traded on the Prague Stock Exchange.

The Company and T-Mobile Czech Republic a.s. signed an agreement on sharing the 3G network. The agreement concerns currently unserved areas with lower population density and will bring high-speed mobile data to more locations. The joint project will accelerate construction of the network and significantly expand the 3G coverage of both operators.

The Company´s name has been changed from Telefónica O2 Czech Republic, a.s. to Telefónica Czech Republic, a.s. and the change was incorporated in Commercial Register on 16 May 2011.

On 10 May 2011 the name of the company Telefónica O2 Slovakia, s.r.o. has been changed to Telefónica Slovakia, s.r.o. and the change was incorporated in Commercial Register of the Slovak Republic.

These condensed consolidated financial statements were not audited.

Interim consolidated statement of comprehensive income

For the six months ended 30 June 2011

In CZK million	Notes	For the six months ended 30 June 2011	For the six months ended 30 June 2010
Revenue	0	25,974	27,908
Gains from sale of non-current assets	4, 5	28	(3)
Internal expenses capitalized in fixed assets		317	310
Operating expenses		(16,039)	(16,993)
Impairment loss		(5)	(13)
Depreciation and amortisation		(5,792)	(5,733)
Operating profit	0	4,483	5,476
Interest income		52	34
Interest expense		(111)	(132)
Other finance expense (net)		23	(23)
Profit before income tax	0	4,447	5,355
Taxes on income	1,2	(836)	(1,001)
Profit for the year	**1**	**3,611**	**4,354**
Other comprehensive income			
Translation differences		(46)	(59)
Other comprehensive income, net of tax		(46)	(59)
Total comprehensive income, net of tax		**3,565**	**4,295**
Profit attributable to:			
Equity holders of the Company		3,611	4,354
Total comprehensive income attributable to:			
Equity holders of the Company		3,565	4,295
Earnings per share (CZK) – basic*		11	14

* There is no dilution of earnings as no convertible instruments have been issued by the Company.

Interim consolidated statement of financial position

As at 30 June 2011

In CZK million	Notes	30 June 2011	31 December 2010
ASSETS			
Property, plant and equipment		53,901	56,651
Intangible assets		20,893	21,437
Investment in associate	12	22	22
Other financial assets		172	175
Non-current assets		**74,988**	**78,285**
Inventories		592	606
Receivables and prepayments		7,938	8,638
Income tax receivable		896	453
Cash and cash equivalents	6	10,820	4,798
Current assets		**20,246**	**14,495**
Non-current assets classified as held for sale		**4**	**12**
Total assets		**95,238**	**92,792**
EQUITY AND LIABILITIES			
Ordinary shares		32,209	32,209
Share premium		24,374	24,374
Retained earnings, funds and reserves		7,297	16,593
Total equity		**63,880**	**73,176**
Long-term financial debts		2,801	2,883
Deferred taxes		3,615	3,936
Non-current provisions for liabilities and charges		64	52
Non-current other liabilities		86	25
Non-current liabilities		**6,566**	**6,896**
Short-term financial debts		310	141
Trade and other payables		24,268	12,408
Provisions for liabilities and charges		214	171
Current liabilities		**24,792**	**12,720**
Total liabilities		**31,358**	**19,616**
Total equity and liabilities		**95,238**	**92,792**

Interim consolidated statement of changes in shareholders' equity

For the six months ended 30 June 2011

In CZK million	Notes	**Share capital**	**Share premium**	**Foreign exchange translation reserve**	**Equity settled share based payments reserve**	**Funds**	**Retained earnings**	**Total**
At 1 January 2010		**32,209**	**24,374**	**(55)**	**38**	**6,452**	**10,861**	**73,879**
Currency translation differences – amount arising in period		-	-	(59)	-	-	-	(59)
Net profit	1	-	-	-	-	-	4,354	4,354
Total comprehensive income		**-**	**-**	**(59)**	**-**	**-**	**4,354**	**4,295**
Capital contribution		-	-	-	14	-	-	14
Dividends declared in 2010	3	-	-	-	-	-	(12,884)	(12,884)
At 30 June 2010		**32,209**	**24,374**	**(114)**	**52**	**6,452**	**2,331**	**65,304**
At 1 January 2011		**32,209**	**24,374**	**(162)**	**38**	**6,452**	**10,265**	**73,176**
Currency translation differences – amount arising in period		-	-	(46)	-	-	-	(46)
Net profit	1	-	-	-	-	-	3,611	3,611
Total comprehensive income		**-**	**-**	**(46)**	**-**	**-**	**3,611**	**3,565**
Capital contribution		-	-	-	23	-		23
Dividends declared in 2011	3	-	-	-	-	-	(12,884)	(12,884)
At 30 June 2011		**32,209**	**24,374**	**(208)**	**61**	**6,452**	**992**	**63,880**

Interim consolidated statement of Cash flow

For the six months ended 30 June 2011

In CZK million	Notes	For the six months ended 30 June 2011	For the six months ended 30 June 2010
Cash from operating activities			
Cash received from operations		28,192	29,476
Cash paid to suppliers and employees		(17,184)	(17,994)
Dividends received		5	3
Net interest and other financial expenses paid		(14)	(20)
Taxes paid		(1,599)	(1,466)
Net cash from operating activities		**9,400**	**9,999**
Cash flow from investing activities			
Proceeds on disposals of property, plant and equipment and intangible assets		42	49
Payments on investments in property, plant and equipment and intangible assets		(3,443)	(2,980)
Net cash used in investing activities		**(3,400)**	**(2,931)**
Cash flow from financing activities			
Dividends paid		21	34
Net cash used in financing activities		**21**	**34**
Effect of foreign exchange rate changes on collections and payments		**2**	**2**
Net increase / (decrease) in cash and cash equivalents during the period		**6,022**	**7,104**
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD		**4,798**	**1,269**
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	**6**	**10,820**	**8,373**
BALANCE AT THE BEGINNING OF THE PERIOD		**4,798**	**1,269**
Cash on hand and at banks		4,774	1,251
Other cash equivalents		24	18
BALANCE AT THE END OF THE PERIOD		**10,820**	**8,373**
Cash on hand and at banks		10,799	8,348
Other cash equivalents		21	25

Accounting policies

A. Basis of preparation

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

The consolidated financial statements were prepared in accordance with International Accounting Standard IAS 34 Interim Financial Reporting (“IAS 34”).

The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group´s annual consolidated financial statements as at 31 December 2010.

The amounts shown in these consolidated financial statements are presented in millions Czech Crowns (“CZK”), if not stated otherwise.

B. Significant accounting policies

The accounting policies adopted in the preparation of the interim condensed consolidated financial statements are consistent with those followed in the preparation of the consolidated annual financial statements for the year ended 31 December 2010.

C. Change in accounting policy

No significant changes in accounting policies were applied in the interim period of 2011 and 2010.

D. Seasonality of operations

There is no seasonal nature either in fixed line segment or mobile telecommunication segment. Telecommunication business of the Group is not regarded as highly seasonal.

Notes to the interim condensed consolidated financial statements

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1. Segment information

Business segments recognised by the Group are as follows:

- Fixed - network communications services using a fixed network and IS/ICT services provided by the Company and other consolidated subsidiaries,
- Mobile - mobile communications services provided by the Company and by Telefónica Slovakia, s.r.o.

For the six months ended 30 June 2011	**Fixed**	**Mobile***	**Group**
In CZK million			
Revenues	11,533	14,786	26,319
Inter-segment sales	(158)	(187)	(345)
Total consolidated revenues	11,375	14,599	25,974
Operating profit	**630**	**3,853**	**4,483**
Interest and other financial costs (net)			(36)
Profit before tax			4,447
Tax			(836)
Profit after tax			3,611
Minority interest			-
Net profit			3,611
As at 30 June 2011			
Assets (excluding goodwill and non-current assets held for sale)	52,774	29,004	81,778
Goodwill	136	13,320	13,456
Non-current assets held for sale	4	-	4
Total assets	**52,914**	**42,324**	**95,238**

* Standalone Revenues of Telefónica Slovakia, s.r.o. of CZK 1,780 million included.

For the six months ended 30 June 2010	**Fixed**	**Mobile***	**Group**
In CZK million			
Revenues	12,587	15,727	28,314
Inter-segment sales	(171)	(235)	(406)
Total consolidated revenues	12,416	15,492	27,908
Operating profit	**1,529**	**3,947**	**5,476**
Interest and other financial costs (net)			(121)
Profit before tax			5,355
Tax			(1,001)
Profit after tax			4,354
Minority interest			-
Net profit			4,354
As at 31 December 2010			
Assets (excluding goodwill and non-current assets held for sale)	52,220	29,859	82,079
Goodwill	128	13,320	13,448
Non-current assets held for sale	161	-	161
Total assets	**52,509**	**43,179**	**95,688**

* Standalone Revenues of Telefónica Slovakia, s.r.o. of CZK 1,256 million included.

Revenue of the Group is predominantly derived from domestic trading activities and as a result, segment reporting is only shown on the basis of business segments.

The inter-segment pricing rates applied in 2011 and 2010 were determined on the same basis as rates applicable for other mobile operators and are consistent with rates applied for pricing with other mobile operators.

2. Income tax

In CZK million	For the six months ended 30 June 2011	For the six months ended 30 June 2010
Total income tax expense is made up of:		
Current income tax charge	1,157	1,275
Deferred income tax credit	(321)	(274)
Taxes on income	836	1,001

Deferred income taxes are calculated using currently enacted tax rates expected to apply when the asset is realized or the liability settled. For 2011 and 2010 19% applied.

3. Dividends proposed

In CZK million	30 June 2011	30 June 2010
Dividends declared (including withholding tax)	12,884	12,884

Dividends include withholding tax on dividends paid by the Company to its shareholders. There has been no interim dividend paid in respect of 2011 and 2010. Approval of the 2010 profit and the decision regarding the amount of any dividend payment for this financial year took place at the Annual General Shareholders Meeting on 28 April 2011 (2010: 7 May 2010). Pursuant to the decision of the Annual General Shareholders Meeting the dividend for 2010 profit is expected to be paid out on 6 October 2011 in amount CZK 40 per share.

4. Property plant and equipment

Acquisitions and disposals

During the six months ended 30 June 2011, the Group acquired assets with a cost of CZK 1,919 million (as at 30 June 2010: CZK 1,799 million). Assets with a net book value of CZK 26 million were disposed of by Group during the six months ended 30 June 2011 (as at 30 June 2010: CZK 6 million).

The Group achieved a total gain from the sale of the above fixed assets (including assets held for sale) amounting to CZK 25 million (as at 30 June 2010: CZK 13 million) and total losses in amount CZK 11 million (as at 30 June 2010: 18 CZK million) during the six months ended 30 June 2011.

5. Intangible fixed assets

Acquisitions and disposals

During the six months ended 30 June 2011, the Group acquired assets with a cost of CZK 635 million (as at 30 June 2010: CZK 580 million).

The Group achieved a total gain from the sale of the above intangible fixed assets amounting to CZK 3 million (as at 30 June 2010: CZK 0 million) during the six months ended 30 June 2011.

6. Cash and cash equivalents

In CZK million	**30 June 2011**	**31 December 2010**
Cash at current bank accounts	177	220
Cash at cash-pooling structures (inter-company) (Note 11)	10,643	4,578
Total cash and cash equivalents	10,820	4,798

As at 30 June 2011, the Group had available equivalent of CZK 4,204 million (as at 31 December 2010: CZK 4,240 million) of undrawn committed facilities.

As of 30 June 2011 and 31 December 2010 no cash and cash equivalents were pledged.

7. Inventories

As at 30 June 2011 the inventories are stated net of an allowance of CZK 67 million (as at 31 December 2010: CZK 61 million), reducing the value of the inventories to their net realisable value.

8. Restructuring costs

During the six months period ended 30 June 2011 restructuring costs of CZK 158 million (as at 30 June 2010: CZK 427 million) have been recognised for the redundancy payments.

9. Contingencies

The Company is a participant to several litigations ensuing from common business relations. The following has changed compared to the 2010 Annual Report:

1) AUGUSTUS spol. s r.o. – CZK 294 million sued

The proceeding regarding the petition filed by AUGUSTUS spol. s r.o. for CZK 294 million was finally terminated due to the failure to pay the court fee. The petition was based on the contract for issuing phone cards between the Company and AUGUSTUS spol. s r.o., which was terminated 13 years ago. The claims were unjustified.

2) The Office for Protection of Competition (OPC) – a penalty of CZK 81.7 million

On 24 March 2011, the Regional Court in Brno revoked again the resolution of the Office for Protection of Competition, namely the statement from 2004 imposing a penalty in the amount of CZK 81.7 million for an alleged abuse of a dominant position. The OPC returned the amount in 2010, after the resolution was revoked for the first time. The administrative proceedings will have to take place again.

3) Vodafone Czech Republic a.s. – a litigation regarding an interconnection contract

On 30 June 20115, Vodafone Czech Republic a.s. (formerly Český Mobil/Oskar Mobil) filed a petition with the Metropolitan Court in Prague against the Company for damages in the amount of CZK 538 million, including appurtenances, and for returning the unjustified enrichment in the amount of CZK 117 million, incl. appurtenances. According to the petition, the Company failed to transfer traffic in the network operated by the mobile operator in compliance with the respective mutual interconnection agreements. On 30 September 2009, the Metropolitan Court in Prague rejected the petition by judgement as unjustified. On 15 February 2011, The High Court confirmed the rejection to a full extent. The proceeding was thus finally terminated in favour of the Company. Vodafone Czech Republic a.s. filed a protest in June, however, only to the extent of

CZK 26 million. With respect to the development to date, the Company believes that the protest is unjustified and that even the filing conditions have not been met.

4) The administrative proceedings in the matter of an alleged abuse of a dominant position on the Internet broadband connection market

After the Regional Court in Brno ordered the Office for Protection of Competition (OPC) to refrain from executing the preliminary investigation proceeding from November 2008 until February 2011, the OPC commenced an administrative proceeding in March 2011, the subject matter of which is an alleged abuse of a dominant position on the Internet broadband connection market. The Company provided the OPC with a statement proving that it had no dominant position, therefore it could not have abused it. At the same time, it provided the OPC with other items of evidence demonstrating correctness of all procedures. The OPC continues to request other supporting data.

5) VOLNÝ, a.s. – a litigation for CZK 4 billion

On 28 March 2011, VOLNÝ, a.s. filed a petition with the Metropolitan Court in Prague against the Company for an amount exceeding CZK 4 billion for an alleged abuse of a dominant position on the market of Internet broadband connection provided to households via ADSL. The amount is meant to represent the lost profit for years from 2004 until 2010. VOLNÝ, a.s. claims to have had 30% share on the dial-up Internet market in 2003 and thus implies in its petition that it should automatically have the same result on the broadband market, which it does not. Allegedly, it is due to the margin squeeze applied by the Company in the wholesale access to ADSL services. The Company replied to the petition in July 2011 by noting that both the claim and the calculations submitted by the plaintiff were unsubstantiated and by pointing at discrepancies in the petition claims.

The Company considers disclosing other information regarding the said litigations not advisable, as it might anticipate the Company’s position in these cases.

The Company’s management is convinced that all risks relating to the litigations have been duly reflected in the financial statements.

10.Commitments

Operating leases

The aggregate future minimum lease payments under operating leases are as follows:

In CZK million	**30 June 2011**	**31 December 2010**
No later than 1 year	1,378	1,421
Later than 1 year and not later than 5 years	4,585	4,630
Later than 5 years	3,763	4,087
Total	9,726	10,138

Capital and other commitments

In CZK million	**30 June 2011**	**31 December 2010**
Capital and other expenditure contracted but not provided for in the financial statements	5,022	4,699

The majority of contracted amounts relate to the telecommunications network and service contracts.

11. Related party transactions

The Group provides services to all related parties on normal commercial terms. Sales and purchase transactions with related parties are based on contractual agreements negotiated on normal commercial terms and conditions and at market prices. Outstanding balances of assets and liabilities are unsecured, interest free (excl. financial assets and liabilities used for financing) and the settlement occurs either in cash or by offsetting. The financial assets balances are tested for the impairment at the balance sheet date, and no allowance or write off was incurred.

The following transactions were carried out with related parties:

I. Parent company:

Balance sheet **In CZK million**	**30 June 2011**	**31 December 2010**
a) Receivables	1	1
b) Payables (excl.dividend payable)	393	1,072

Comprehensive income **In CZK million**	**For the six months ended 30 June 2011**	**For the six months ended 30 June 2010**
a) Sales of services and goods	-	4
b) Purchases of services and goods	22	9

There was no dividend paid as at 30 June 2011 to Telefónica, S.A. The dividend payable to Telefónica, S.A. is in the amount of CZK 8,943 million (31 December 2010: 0 Kč).

For the six months ended 30 June 2011 the royalty fees to Telefónica, S.A. amounted to CZK 382 million (for the six months ended 30 June 2010: 423 CZK million).

II. Other related parties – Telefónica Group:

Balance sheet **In CZK million**	**30 June 2011**	**31 December 2010**
a) Receivables	422	445
b) Payables (excl.dividend payable)	1,806	1,536
d) Short-term receivables (interest)	8	3
e) Cash equivalents (Note 6)	10,643	4,578

Comprehensive income **In CZK million**	**For the six months ended 30 June 2011**	**For the six months ended 30 June 2010**
a) Sales of services and goods	361	398
b) Purchases of services and goods	563	335
c) Interest income	36	22

There was no capital purchases for the six months ended 30 June 2011 and 30 June 2010.

The list of the Telefónica companies with which the Company had any transaction in 2011 and 2010 includes the following entities: Telefónica S.A., Telefónica de Espaňa, S.A.U., Telefónica Germany GmbH& CO.OHG, Telefónica UK Ltd., Telefónica Ireland Ltd., Telefónica Móviles España, S.A.U., Telefónica Móviles Argentina, S.A., Pléyade Peninsular, O2 Holdings Ltd., Telefónica Deutschland GmbH, ALTAIR ASSURANCES S.A., Telefónica Móviles Guatemala, S.A., Telefónica Móviles El Salvador, S.A. de C.V., Telefónica Móviles Panamá, S.A., Telefónica Móviles Chile, S.A., Otecel, S.A., Telefónica Móviles Nicaragua, S.A., Telefónica Móviles Columbia, S.A., Telefónica Investigación y Desrrollo, S.A., Portugal Telecom, Telecom Italia

S.p.A., Telfisa Global, BV., Telefónica International Wholesale Services, Telefónica International Wholesale Services II, S.L., S.A., Atento Chequia, Telefónica Compras Electrónica, S.L., Telefónica Móviles Mexico, S.A., Telefónica Móviles del Uruguay, S.A., Telefónica Móviles Peru, S.A., Telefónica Venezuela, S.A., China Unicom (Hong Kong) Limited, Telefónica Global Roaming GmbH, Vivo, S.A., Telefónica Europe People Services Limited, Jajah Ltd., O2 Communication, Hansenet Telekommunication GmbH, MOPET CZ a.s., TELEFÓNICA FACTORING E.F.C., S.A.

Liabilities to TELEFÓNICA FACTORING E.F.C., S.A. represent due balances arising from the assigned receivables by the suppliers using Group factoring.

a) Key management compensation

Members of the Board of Directors and of the Supervisory Board of the Telefónica Czech Republic, a.s. were provided with benefits as follows:

In CZK million	**For the six months ended 30 June 2011**	**For the six months ended 30 June 2010**
Salaries and other short-term benefits	55	57
Personal indemnification insurance	3	3
Total	58	60

b) Loans to related parties

There were no loans provided to members of Board of Directors and Supervisory Board in 2010 and 2011.

There were no loans was provided to related parties by the Group.

12.Principal subsidiary undertakings and associates

	Subsidiaries	**Group's interest**	**Cost of investment in CZK million**	**Country of incorporation**	**Activity**	**Method of consolidation**
1.	Telefónica O2 Business Solutions, spol. s r.o.	100 %	237	Czech Republic	Network and consultancy services in telecommunications, IT/ICT services	Full consolidation
2.	CZECH TELECOM Germany GmbH	100 %	10	Germany	Data transmission services	Full consolidation
3.	CZECH TELECOM Austria GmbH	100 %	11	Austria	Data transmission services	Full consolidation
4.	Telefónica Slovakia, s.r.o.	100 %	6,116	Slovakia	Mobile telephony, internet and data transmission services	Full consolidation
	Associates					
5.	První certifikační autorita, a.s.	23 %	9	Czech Republic	Rendering of certification services	Not consolidated
6.	AUGUSTUS spol. s r.o.	40 %	-	Czech Republic	Sales by auctions and	Not consolidated

					advisory services	
7.	MOPET CZ a.s.	14 %	13	Czech Republic	Real time payment services via mobile phones	Not consolidated

13.Events after the statement of financial position date

WiFi acquisitions and demerger project

As of the date of preparation of this Interim condensed consolidated financial statements Telefónica O2 Business Solutions, spol. s r.o. purchased a WiFi network infrastructure, customer base and related assets from seven local providers of Internet access on WiFi technology platform. These purchases were made through purchase of assets or part of enterprise and were reported in accordance with IFRS 3.

On 27 July 2011 the company of Telefónica Czech Republic, a.s. as the sole shareholder of Telefónica O2 Business Solutions, spol. s.r.o. (hereinafter the „demerged company“) approved a demerger spin-off project. Based on the project a part of enterprise is to be spun-off into a newly founded subsidiary Internethome, s.r.o. The effective date of the transaction is 1 January 2011. The main activity of the part of enterprise being spun-off was providing O2 Info content for Telefónica Czech Republic, a.s. transmitted on television channel O2 TV. The spin-off into the newly flunder subsidiary Internethome, s.r.o. will be legally effective following completion of all statutory requirements once it is registered in the Commercial Register.

From the accounting point of view the activities of the demerged company associated with the acquisition of the WiFi network infrastructure and related assets from local providers of the Internet access on WiFi technology platform made through purchase of assets or part of enterprise will be treated as transactions carried out on account of the new subsidiary. The main activity of the new subsidiary is to provide Internet access on WiFi platform.

The demerged company will continue with its core business of providing services of the information and communication technologies.

6. Other information for shareholders and investors

The shareholder structure of Telefónica CR as at 30 June 2011:

Telefónica, S.A.	69.41%
Investment funds and individual shareholders	30.59%

Trading in Telefónica CR shares

The total volume of Telefónica CR shares traded on the stock market of the Prague Stock Exchange (PSE) reached CZK 15.3 billion in the first half of 2011, compared to CZK 21.1 billion in the first half of 2010. This ranked the Company among TOP 5 blue chips and accounted for approximately 8% of all trades. Compared to the first half of 2010, the average daily trading volume declined in the first half of 2011 by CZK 161.6 million to CZK 117.8 million. As at 30 June 2011, the market capitalisation of the Company was CZK 140.6 billion, which propelled Telefónica CR to the fourth position among companies traded on the stock market of the PSE. It represented 10% of the total market capitalisation of the PSE stock market at the end of the first half of 2011.

In the period from the start of the year until 30 June 2011, the share price of Telefónica CR went up 14.42% to CZK 436.50, which was also the peak of the half year. The performance of the PSE stock market, as measured by the PX Index, increased only 0.05% in the same period reaching 1,225.4 points at the end of June 2011.

General meeting

An Ordinary General Meeting of the Company's shareholders was held on 28 April 2011. An overview of the main conclusions of the General Meeting is given in section Corporate Governance of this Half-year Report.

Dividends

The shareholders at the General Meeting approved a proposal by the Board of Directors of the Company for the distribution of profit for 2010 and the retained earnings from previous periods, as well as of any disposable resources of the Company as the case may be, and for the determination of royalties for the year 2010. The General Meeting passed a resolution to pay dividends from the 2010 profit (CZK 12,680.7 million) and a part of the retained earnings from previous periods (CZK 202.9 million). The total amount of dividends to be paid out is CZK 12,883.6 million, which CZK 40 per share in the nominal value of CZK 100 and CZK 400 per share in the nominal value of CZK 1,000, all before tax. The record day for the payment of the dividend is 7 September 2011 and the payment date is on 6 October 2011. The dividends will be disbursed by Česká spořitelna, which will inform all shareholders entitled to collect dividends after the record date of the method of disbursement.

Institutional investors and shareholders may contact:

Investor Relations
Telefónica Czech Republic, a.s.
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Tel.: +420 271 462 076, +420 271 462 169, fax: +420 271 463 566
E-mail: investor.relations@o2.com, http://www.telefonica.cz/en/investor-relations/

7. Declaration of competent persons responsible for Half-Year Report

Luis Antonio Malvido, Chairman of the Board of Directors and Chief Executive Officer of Telefónica Czech Republic, a.s.

Jesús Pérez de Uriguen, 1st Vice-chairman of the Board of Directors and Director, Finance Division of Telefónica Czech Republic, a.s.

hereby declare that, to their best knowledge, the consolidated Half-Year Report gives a true and faithful reflection of the financial situation, business activity and the results of the Company and its consolidated whole for the past half-year, and of the outlook on the future development of the financial situation, business activity and the results of the Company and the its consolidated whole.

Luis Antonio Malvido
Chairman of the Board of Directors
Chief Executive Officer

Jesús Pérez de Uriguen
1st Vice-chairman of the Board of and
Directors and Director, Finance Division