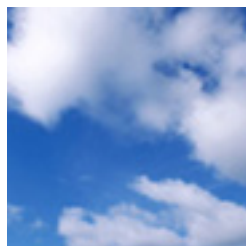
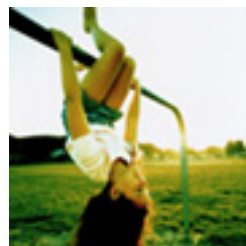




Strategic drivers & early lessons from Telefónica's *imagenio*» IPTV service

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Industry Panel on IPTV

Telefonica

September 28th, 2006

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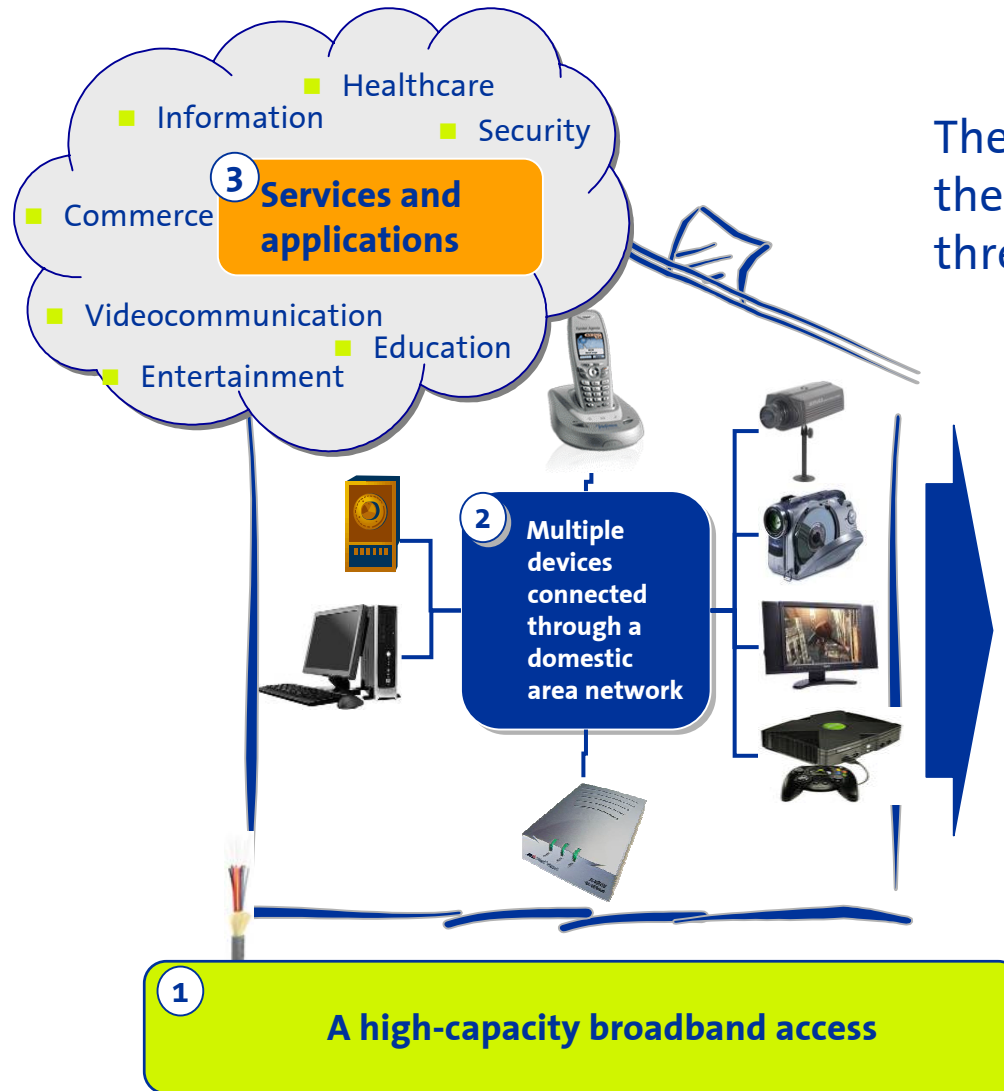


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Imagenio becomes a key element of the Digital Home concept pursued by Telefónica to maintain its market leadership ...



The Digital Home strategy is the result of the integration of three building blocks:

- Broadband access
- Multiple devices connected through a domestic area network
- Services and applications



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Imagenio has been conceived as a unique value proposition with distinctive features for family homes ...



imagenio »



Flexible configuration of packages: **Basic & Advanced**

Spanish Football: live & recorded

Up to 78 TV and 15 audio channels



Video on demand: +3,000 hours of cinema, concerts, TV series, news, documentaries, ...



20 Interactive services: electronic magazine on TV, email & Internet access on screen ...

- Provides 6Mbps ADSL access for our customers to receive Digital TV
- Uses ADSL2+ technology for increased coverage
- Compatible with Digital Terrestrial Television



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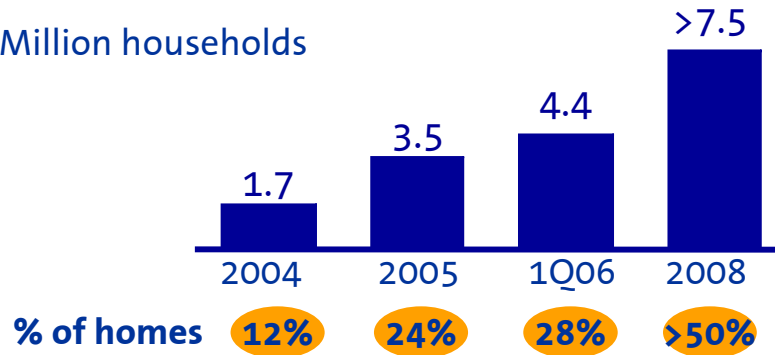
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... with an increasing coverage based on business criteria



Evolution of national coverage

Million households

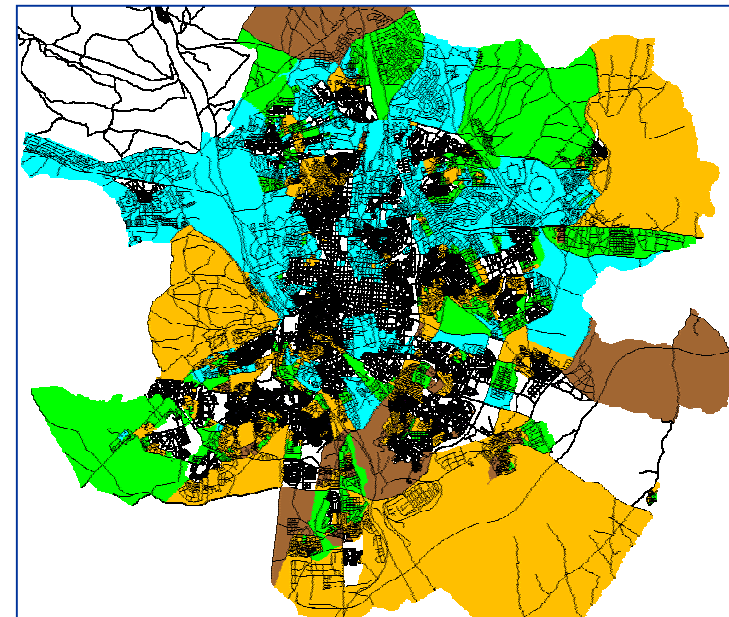


- As of today, Imagenio is available in all Spanish regions
- Increased coverage will be achieved following a profitability likelihood planning method

Case study: Priority Investment areas in the Madrid region

Data mining demand model, tuned by Imagenio customer base

Priority





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Imagenio has become one of the main drivers of success for Telefónica in the Spanish broadband market



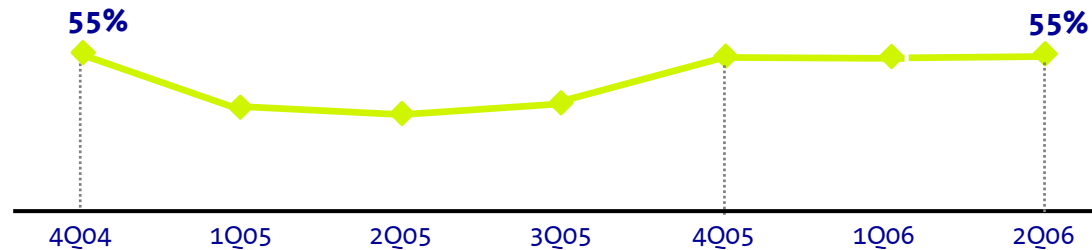
(1) Includes 31 TV and 15 audio channels, Football (PPV), VoD, TDT channels and interactive services + National Calls. Decoder monthly fee rental not included (6,5 EUR/month)

(2) Includes 31 TV and 15 audio channels, Football (PPV), VoD, TDT channels and interactive services + National Calls + ADSL 24 H. Decoder monthly fee rental not included (6,5 EUR/month)

Imagenio client base accelerated with 2-Play and 3-Play offers launched in Sept. 05 to reach 267,473 clients by end June 2006

1,2 – 1,4 million Imagenio customers by 2009

Retail Internet BB Market Share ¹



1. Estimated for the Telefónica Group in Spain

Telefónica is driving Internet Broadband penetration growth while maintaining market share

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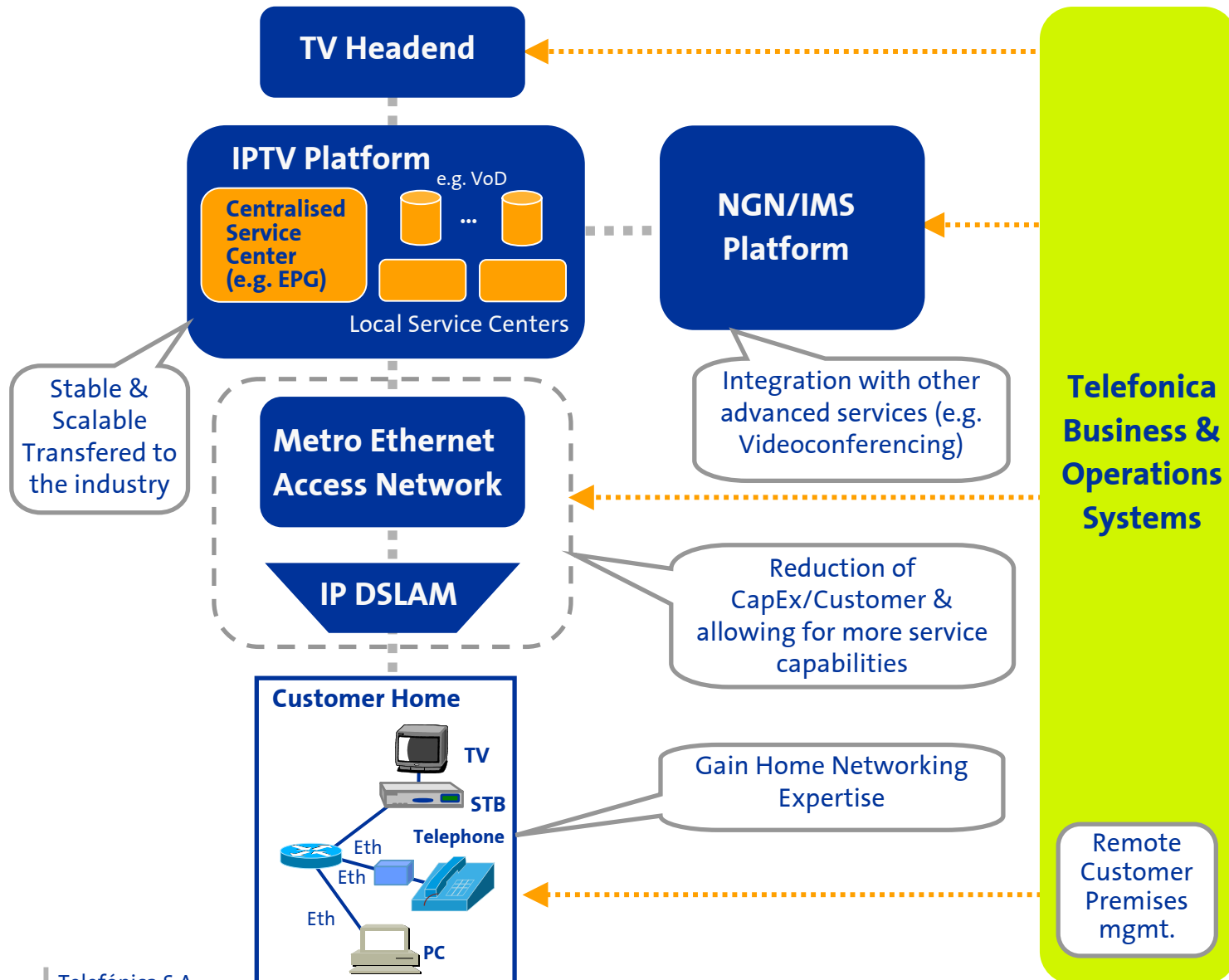


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In 2004, Telefonica decided to evolve its network architecture based on its prior experience



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There are multiple lessons to be learned with regards to the key design parameters of an IPTV solution



**What
almost
everybody
talks about**

- Broadband network: access (IPDSLAM), transport (GEThernet/ SDH), IP Core
- IPTV Platform: middleware/ DRM/ STB/ Look&Feel
- Video compression technology: MPEG2/ MPEG4/ WM9
- Systems: provisioning & billing
- Content

**What
almost
nobody
talk about**

- Home networking
- Knowledge of access
- Design & availability for video signal
- Knowledge of customer behaviour
- Network & services architecture
- O&M/ customer care systems & processes

Early issues and challenges range across the whole customer experience




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Area

Details

1

Customer acquisition

- TV over ADSL constitutes a very powerful offer at a reasonable price
- Adequate coverage and product awareness are key factors for a successful and effective commercialization
- Customers barriers to purchase include:
 - ... the product is perceived too new for some customers and they prefer to wait to see how it works
 - ... telecom operator not perceived as a TV provider
 - ... content offer fitted to diverse customer needs
 - ... installation process perceived as a complex operation
- Sales channels must be trained to handle a complex new product/ business

2

Provisioning and installation

- Operational processes are critical due to the quantity of new details to be taken into account in order to ensure customer satisfaction:
 - Incorrect coverage verification or product incompatibility
 - Saturation in operations and infrastructure deployment due to the high growth in sales
 - Customers canceling prior to installation
 - Problems during the installation, multiple causes

3

Customer retention

- Situations that must be avoided since day 1 include:
 - Technical and malfunctioning service problems
 - Insufficient value added perceived in the product (product/price relation)
 - Difficult retention at the end of aggressive but needed try& buy promotions



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In the short term we have an ambitious P/S roadmap for digital households



Household roadmap 2006-2007

Broadband Access

High-speed connectivity as a basis for Advanced and Connected Digital Homes

Domestic Area Network with multiple devices

TV videoconference with 3G interworking

Domotics: Integrated home devices and remote management

Seamless Fixed and mobile services

Services and Applications

Personal TV: HDTV, Shift TV, DVR, flexible content selection.

New customer experience (IPTV 2.0)

Connectivity Bundled with VAS: Home content management

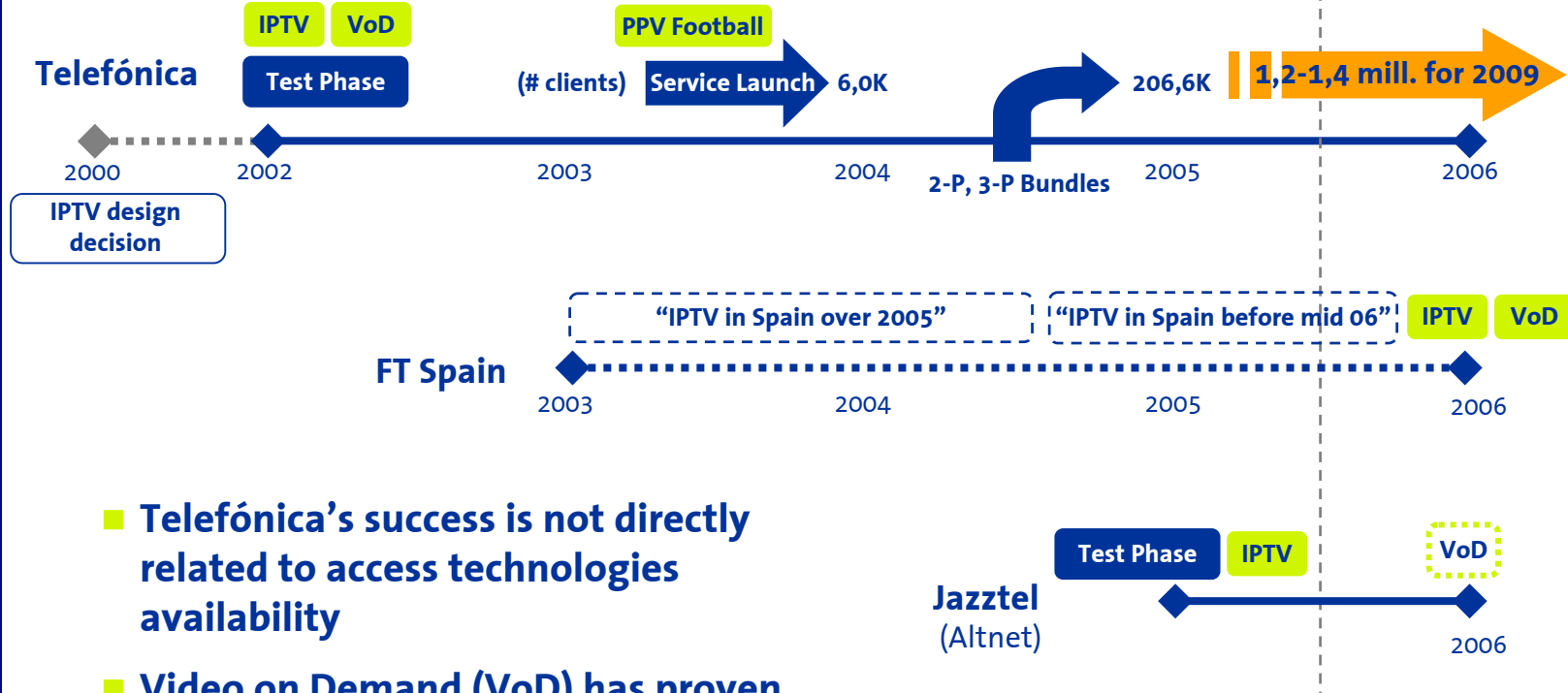
Family management (education, security and health)



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Telefonica has had a 4-year learning period, already having a business model not easily replicable by its main competitors



- Telefónica's success is not directly related to access technologies availability
- Video on Demand (VoD) has proven to be the hardest technological milestone to be achieved

Dotted lines means "Announced, but not available"
Source: Telefonica and companies' press releases

Telefonica is now exporting its IPTV winning model abroad: CTC (Chile), TeleSP (Brazil) and Telefonica O2 Czech Rep.

Telefónica has decided the creation of the IPTV Competence Center internally to foster the Innovation in this area and optimize the efficiency (development/deployment)

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Currently we do not see any limits to the growth and development of Imagenio



Main figures

- 267K customers connected at 1H06
- 34% of our customers buy “video club” VoD films (3 films by month in average)
- 21% of our customers buy football contents (2 matches by month in average)
- 20% of our customers have at least one subscription service
- Massive service with national coverage

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Near future:

- More customers: 1,2-1,4 million by 2009
- More channels (beyond basic package), more flexible
- More complete/ attractive VoD content offering
- More interactivity, new and better services
- More coverage: 50% of households by 2008

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