

*Telefonica*

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**Quarterly Results**  
Telefónica del Perú S.A.A.

April – June 2009

## Significant Events 2Q09

A summary containing the most significant events from April 1st to June 30th of 2009:

1. On April 22<sup>nd</sup> the Board of Directors adopted the following agreements:
  - Ratified the actual positions in the Board of Directors, specifically, the designation of Javier Manzanares Gutiérrez as a president of the Board of Directors; Jose Maria Alvarez Pallete Lopez as vice-president of the Board of Directors, Julia Maria Morales Valentin as secretary of the Board of Directors and Milagros Muñoz Bazan as a subsecretary of the Board of Directors.
  - Formulated the individual and consolidated financial statements corresponding to the first quarter 2009.
  - Approved the audited and consolidated financial statements 2008.
  - Designated José Juan Haro Seijas as Director of Strategy and Regulation.
2. On April 27<sup>th</sup>, the merger between TDP (Telefónica del Perú.S.A.A.) and TMPH (Telefónica Móviles Perú Holding S.A.A.) was registered. Also, June 15<sup>th</sup>, 2009 was set as the date of registry and exchange of the adjustment of the nominal value of Telefonica del Peru S.A.A. shares from S/. 1.52 to S/. 0.86; and of the exchange of TMPH shares for TDP shares, according to the relation of exchange established in the Merger Project approved by the shareholder meetings of both companies on December 22<sup>nd</sup>, 2008.
3. On April 30<sup>th</sup>, the Board of Directors accepted the resignation of Luis Fernandez Jiménez as a Director of Planning and Network Engineering. Also, The Direction of Networks and Systems was created, as a result of the merge between the Direction of Planning and Engineering and the Direction of Networks and Systems. Séneca de la Puente, former Director of Operation of Networks and Systems, was designated as Director of Networks and Systems.
4. On June 10<sup>th</sup>, the change of ownership of the common stock of TM (Telefónica Móviles S.A.) in favour of TDP was approved. Consequently, TDP maintains the ownership of 14 992 457 864 representative shares of the share capital of TM, that represents the 96,0937242% of its share capital. On the other hand, the exclusion of the representative shares of the share capital of Telefónica Móviles Peru Holding S.A.A. from the Public Registry of the Lima Stock Exchange has been asked.

5. The Board of Directors, on June 17th, approved a dividend payment of up to S/. 400 000 000.00 to the payment of dividends against accumulated results as of December 31<sup>st</sup>, 2008 and to voluntary reserves.
6. On July 1st, TdP approved a dividend distribution of S/. 400 million, which will be distributed to shareholders at the rate of S/. 0.119500763489 per share, without considering in such calculation those shares of own issuance purchased by the company. The company established the day of registry on July 17<sup>th</sup>, 2009 and the day of payment on July 23<sup>rd</sup> 2009.

## **Telefónica del Peru S.A.A.**

### **Discussion and analysis of the results of the second quarter ended on June 30<sup>th</sup>, 2009.**

*It is recommended the reading of this report along with the corresponding Financial statements and their Notes, presented at the same time, since they form integral part of this document and contain complementary information.*

#### **Economic Environment**

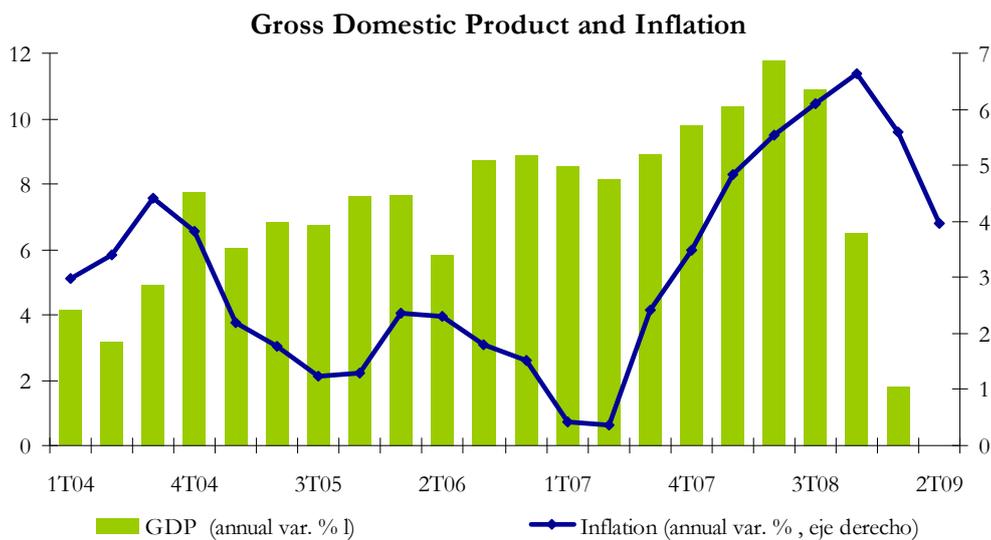
In the first quarter of 2009, GDP growth was only 1.8% compared to that of the first quarter of the previous year, the lowest quarterly growth rate since 2001. In both, supply side and demand side, all of the components showed a deceleration compared to previous levels. In the supply side, the most dynamic sectors were construction (5.1%), other services (4.5%), farming (3.9%), mining and hydrocarbons (3.7%), whereas the sectors more affected by the economic deceleration were fishing (- 19.8%), manufacture (- 5.1%) and commerce (0.4%). The manufacture and commerce were affected by the optimization process of inventories.

In the demand side, the internal demand fell 0.8% and exports dropped by 3%, contributing to the decrease of the global demand (- 1.6%). Private consumption (slightly higher than 60% of the GDP) decelerated from 4.3%, in the previous quarter, to 3.7%. The internal gross investment registered a strong contraction (- 14.5%), although private investment (83% of the total investment) grew 1.8%, and that the public investment grew 22.2%, due to the execution of its Economic Stimulus Plan . The fall in the internal gross investment in the first quarter of the year was basically determined by a strong adjustment of inventories (- 141.3%) and its contribution to GDP's growth (- 4.9 %).

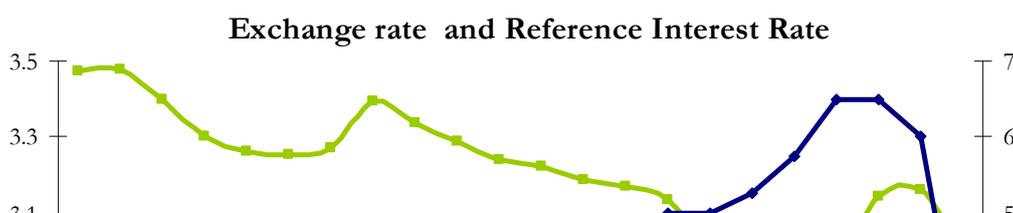
In April, the GDP fell 2.01% compared to the same month of the previous year, being the first negative result after 93 consecutive months of growth. The result confirms the strong deceleration of the economy, observed from 3Q-08, affected by a contraction of the sectors related to internal demand and ,mainly, external demand, as a result of the worldwide recession. In the period January-April 2009, the accumulated growth of GDP was 0.93% in relation to the same period of the previous year, whereas in the last 12 months it has expanded 6.4%.

Regarding inflation, the variation of the Consumer Price Index (CPI) in June was -0,34% compared to the previous month. This is the smallest variation registered in the last 37 months and it is the lowest result observed in the months of June of the five preceding years. Thus, an inflation of 0.03% is accumulated from January to June 2009, and 3.06% in the last 12 months, slightly over the upper limit of the inflation goal of the BCRP (2% +/- 1%).

The sectors that explained the reduction of the inflation were: 1) foods and drinks (- 0.72% compared to May) that continued showing lower average prices in the main agricultural products, despite the increase of prices derived from the lower supply in the last week of the month due to the transport problems generated by the blockade of highways; and 2) rent of house, fuels and electricity (- 0.28% compared to May), a fall explained by the reduction of electricity tariff in 1,4%, although gas propane price was increased by 0,5%. Thus, the result of June 2009 confirms the downward trend of inflation and its convergence to the goal has guided the expectations of inflation of the market.



Regarding the exchange rate, in June, the Peruvian Sol closed the month in 3,01 New Sol/Dollar, 1.5% lower than the same month of the previous year, but maintaining its appreciation of 4.1% compared to December 2008. This is explained by the lower aversion to the risk of emergent markets, the best results in the balance of payments, which reflected significant flows of dollars to the country, and by the partial return of the market to consider the macroeconomic foundations of the New Sol. In addition, between January and June 2009, the Central Bank of Reserves of Peru (BCRP) reduced its reference interest rate 450 bps, to a level of 2%, reflecting its preoccupation by a deceleration greater than expected.



The country risk, approximated by the Emergent Markets Bond Index (EMBI+) of JP Morgan, fell to 291 points, in the first half of July, slightly better than that of other countries in the region. Moreover, the sovereign bonds yields continued decreasing in the first half of July (1.1% on average), with a higher incidence in the short part of the curve (3.1% on average) as a result of the fall in the BCRP reference interest rate. The Global Bonds yield curve followed the same trend, with reductions of 2.2% and 2.0% in the total average and in the short section of the curve, respectively.

## **Competitive Environment**

During 2Q09, the telecom operators have focused in the increase of value of the traditional business. For example, Telefónica launched the National Flat Tariff, service that allows the communication of limitless national long distance by a monthly fixed payment; whereas Telmex extended its coverage of packaged services in Chiclayo. On the other hand, Claro and Telmex entered in the wireless fixed telephony market in Lima and in the rest of the country.

Also, Telefonica launched the mobile Internet service aiming to fidelize the “packaged” clients and to consolidate the brand “Speedy Total” among its clients.

At quarter end, Telefónica launched a new portfolio of products focused on the PYME segment (Middle and Small enterprises) to satisfy and improve the communication needs of these clients boosting his growth and development.

## **Operating Results**

### **Operating Revenues**

Operating Revenues in 2Q09 reached S/. 963 million, 6,3% higher than 2Q08. The increase in revenues are explained by: the Television by subscription business (+S/.39 million), Data and Information Technology (+S/.16 million), Interconnection and Circuits Services(+S/.12 million), Internet (+S/.10 million) and Others (+S/.21 million). The same are partially offset by the fall in Local Telephony (- S/.25 million), Long Distance Telephony (-S/.8 million) and Public and Rural Telephony (-S/.8 million).

Operating revenues of 6M09 reached S/. 1 938 million, which were increased in 6,0% compared to 6M08, because of higher revenues in Television by Subscription (+S/.72 million), Data and Information Technology (+S/.34 million), Interconnection and Circuits Services (+S/.22 million), Internet (+S/.21 million) and Others (+S/.45 million). Nevertheless, the following business showed lower revenues: Local Telephony (- S/.61 million), Long Distance Telephony (-S/.12 million) and Public and Rural Telephony (- S/.11 million).

Telefónica del Perú S.A.A maintains its commercial penetration strategy by offering services for each market segment, through diverse campaigns - commercialization of Telefonica's trios and duos - and its fidelization campaign, aiming to multiply the number of accesses in the market. Thus, by 2Q09, total operating accesses showed an inter-annual growth of (i) 18.9% in broadband accesses, essentially by the strong increase in Speedy clients due to the greater supply of multi-products (TV, Speedy and line), as well as the commercialization of complete connection to Internet "Speedy Total", (ii) 8.1% in accesses of Public and Rural Telephony, as a result of the impact of the campaign "Flat Tariff" in SLMFF (Mobile-Fixed Local Service) and LDNFF (Fixed-Fixed Long national distance) which was offset by the growth of the mobile substitution, that has implied an increase in dropped lines, and (iii) 7,6% of Television by Subscription clients, due to the present commercial model of multi-product packages (Trios and Duos TV).

Local Telephony revenues reached S/.326 million in 2Q09, 7.0% less than 2Q08. This is mainly explained by a reduction of 16,5% in the Fixed-Other operator traffic (mobile and fixed) as a result of the mobile substitution and lower revenues in the Invoiced Fixed - Fixed Traffic (-15.1%, minutes out of the offered packet of minutes) given the migration towards flat price lines and per second pricing lines. Moreover, the monthly rent income registered a fall of 2,5% as a result of a smaller base of clients that fell 4.7% compared to the previous quarter.

Similar behaviour is observed in 6M09 where revenues reached S/. 659 million, a reduction of 8.4% compared to 6M08 due to lower revenues in Other operators interconnection traffic (-19,2%) and monthly rent (-2,6%), as explained before.

Long Distance revenues fell 10.6% in 2Q09 vs. 2Q08, totalizing S/. 69 million. This fall (- 17.0%) is as a result of lower revenues in national long distance (LDN) due to mobile substitution, as well as by the strong pre-paid card competition and the smaller base of invoiced plans. Long international distance revenues (LDI) fell - 3,8% due to lower Dialed LDI revenues. Accumulated results reached S/. 145 million in 6M09, a drop of 7.5% compared to 6M08, due to Lower LDN revenues (- 15.7%) that were offset by an increase in LDI Revenues (+1.3%).

Rural and Public Telephony revenues were S/. 108 million in 2Q09, 6.7% lower than in 2Q08. The reduction is as a result of mobile substitution, informal "locutorios" as well as "Tarifa Plana" campaign in SLMFF and LDNFF. On the other hand, 6M09 revenues reached S/. 220 million, a fall of 4.6% compared to 6M08. This fall occurred notwithstanding the inter-annual growth of 8.1% of the plant in service (160,289 lines in the urban zone and 11,642 lines in the rural zone by 6M09).

Television by Subscription revenues registered S/.43 million in 2Q09 (S/. 3,4 million in 2Q08) and S/. 76 million in 6M09, an important increase compared to 6M08. This increase is essentially explained by the inter-annual growth of the number of clients who reached 183 thousand clients in 6M09, as a consequence of the present commercial model (multi-product packages: Trios and Duos TV). The rest of the base of clients (520 thousand) belongs to the subsidiary Telefónica Multimedia. It is important to highlight that expenses related to the revenues of this business belongs to the wholesale service that Telefónica Multimedia gives to TDP, and are registered as general and administrative expenses.

Internet revenues reached S/. 206 million in 2Q09, 4.9% higher than 2Q08. This increase is mainly explained by the growth of the broadband plant in 18,9%. This increase has allowed to reach a plant in service of 744 thousand accesses given the wider supply of multi-products. Furthermore, by the end of June 2009, Telefónica began the commercialization (in trio and duo packets) of a complete connection service to Internet through "Speedy Total", that includes WiFi and Mobile Broadband services. As a result, 6M09 revenues reached S/. 407,0 million, 5.3% higher than in 6M08.

Interconnection and Circuits Service Revenues reached S/.99 million in 2Q09, 13.4% higher than in 2Q08. This increase is mainly explained by higher interconnection services from Mobile to Fixed Telephony. In accumulated terms, revenues reached S/.199 million in 6M09, an increase of 12,5% compared to 6M08.

Data and Information Technology reached S/. 91 million in 2Q09, (+21.7% compared to 2Q08) and S/. 181 million in 6M09, that represents an increase of 22.9% compared to 6M08. These results are mainly explained by important projects to corporate clients in Managed Telephony, Sale of Power Stations and Information Technology Projects.

Others revenues reached S/. 24 million (S/. 3 million in 2Q08) as a result of higher revenues in PdTI (Computer science Job, services that offer solutions to small and medium businesses) of S/. 21 million. Accumulated results reached S/. 51 million in 6M09, a strong increase compared to 6M08, due to higher PdTI revenues in S/. 46 million.

## **Operating expenses**

Operating expenses in 2Q09 reached S/. 833 million (+2.6% compared to 2Q08). This increase is the result of higher general and administrative expenses (+S/. 57 million), that include the TV wholesale service expenses given by the subsidiary Telefónica Multimedia and the higher expenses in Other net Revenues and expenses (+S/.10 million). These increases were partially offset by the reversion of the provision of the Optional Retirement Program (S/. 31 million), and the lower expenses in Management and Technical Capacity Transfer Fee (S/.14 million) as well as Personnel (S/.7 million).

The accumulated operating expenses in 6M09 increased in 4,2% vs. 6M08, reaching S/. 1 685 million, due to higher general and administrative expenses (+S/. 115 million), materials and provisions (+S/. 21 million), personnel (+S/. 20 million), that was partly offset by lower depreciation and amortization (S/. 41 million), the reversion of the provision of the Optional Retirement Program (S/. 31 million), and lower Other Revenues and Expenses (S/. 10 million).

### **Operating Result**

Operating Result in 2Q09 reached S/. 130 million, an increase of S/..36 million vs. 2Q08, as a result of higher total revenues and the contention of the operational expenses. In addition, Operating result reached S/..253 million in 6M09 (+20,1% compared to 6M08). In the same way, this increase is a consequence of higher revenues versus lower operational expenses, a product of lower Depreciation and Amortization and the reversion of the provision of the Optional Retirement Program.

### **Non Operating result**

Non operating result increased from S/..37 million, in 2Q08 to S/. 90 million in 2Q09. This evolution is basically explained by the participation in Results of Related Parts in S/. 48 million, mainly from the subsidiary Telefónica Móviles.

Non-operating results increased S/. 178 million, from 6M08 to 6M09, due to participation in Results of Related Parts (S/. 152 million) and to lower financial expenses (S/. 26 million).

### **Net result**

The net result reached S/. 164 million in 2Q09, vs. S/. 101 million in 2Q08. In accumulated terms the net result also increased in S/. 189 million to reach S/..358 million. These increases are essentially explained by operating and non-operating results.

### **Balance Sheet**

Current Assets reached S/. 1,598 million in 2Q09. An increase of S/. 256 million compared to 1Q09. Current liabilities fell in S/. 147 million. Thus, current liquidity

ratio was 0.84 in 2Q09, vs. 0.65 in 1Q09. The net fixed assets were S/. 3,389 million, S/. 67 million less than in 1Q09.

The financial debt reached S/. 3,450 million in 2Q09, S/. 26 million higher than in 1Q09. Also, net shareholders' equity increased S/. 113 million compared to 1Q09, reaching S/. 4,076 million in 2Q09 - the Net Result of 2Q09 (S/.164 million) was partially offset by the negative effect of the valorisation of the financial derivative instruments, which is registered in Other reserves. It is important to highlight that Telefonica del Perú S.A.A. decided the distribution of a total dividend of S/.400 million to be paid on July 23<sup>rd</sup>, 2009.