

PORTUGAL TELECOM SGPS SA
Form 20-F
June 30, 2004

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 20-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES
EXCHANGE ACT OF 1934**

OR

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

For the fiscal year ended December 31, 2003

OR

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

Commission file number 1-13758

PORTUGAL TELECOM, SGPS, S.A.

(Exact name of Registrant as specified in its charter)

Republic of Portugal

(Jurisdiction of incorporation or organization)

Av. Fontes Pereira de Melo, 40, 1069-300 Lisboa Codex, Portugal

(Address of principal executive offices)

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

Title of each class	Name of each exchange on which registered
American Depositary Shares, each representing one ordinary share, nominal value €1 per share	New York Stock Exchange
Ordinary shares, nominal value €1 each	New York Stock Exchange*

*
Not for trading but only in connection with the registration of American Depositary Shares.

Securities registered or to be registered pursuant to Section 12(g) of the Act: **None**

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Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **None**

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

Ordinary shares, nominal value €1 per share	1,254,284,500
Class A shares, nominal value €1 per share	500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Item 17 Item 18

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CERTAIN DEFINED TERMS

Unless the context otherwise requires, the term "*Portugal*" refers to the Republic of Portugal, including the Madeira Islands and the Azores Islands; the term "*Portuguese Government*" refers to the government of the Republic of Portugal and, where the context requires, includes the Portuguese state; the term "*Parliament*" refers to the Assembly of the Republic of Portugal, the legislative body of the Portuguese state; the term "*EU*" refers to the European Union; the term "*EC Commission*" refers to the Commission of the European Communities; the terms "*United States*" and "*U.S.*" refer to the United States of America; the term "*Portugal Telecom*" refers to Portugal Telecom, SGPS, S.A.; and unless indicated otherwise, the terms "*we*," "*our*" or "*us*" refer to Portugal Telecom and its consolidated subsidiaries.

PRESENTATION OF FINANCIAL INFORMATION

We publish our financial statements in Euro, the single European currency adopted by certain participating member countries of the European Union, including Portugal, as of January 1, 1999. Unless otherwise specified, references to "Euros," "EUR" or "€" are to the Euro. References herein to "U.S. dollars," "\$" or "US\$" are to United States dollars. References to "Escudos" or "PTE" are to Portuguese Escudos. References to "Real," "Reais" or "R\$" are to Brazilian Reais. Certain Euro amounts have been translated into U.S. dollars at specified rates. Unless otherwise indicated, U.S. dollar equivalent information for amounts in Euro is based on the noon buying rate in the City of New York for cable transfers in Euros as certified for United States customs purposes by the Federal Reserve Bank of New York on December 31, 2003. For convenience and comparability, figures previously stated in Escudos have been converted to figures in Euros based on the fixed Escudo/Euro exchange rate of PTE 200.482 = €1.00. We are not representing that the Euro or US\$ amounts shown herein could have been or could be converted into US\$ or Euros, as the case may be, at any particular rate or at all. See "*Item 3 Key Information Exchange Rates*" for further information regarding the rates of exchange between Euros and U.S. dollars.

FORWARD LOOKING STATEMENTS

This Form 20-F includes, and documents incorporated by reference herein and future public filings and oral and written statements by our management may include, statements that constitute "forward-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995. These statements are based on the beliefs and assumptions of our management and on information available to management at the time such statements were made. Forward-looking statements include, but are not limited to: (a) information concerning possible or assumed future results of our operations, earnings, industry conditions, demand and pricing for our products and other aspects of our business under "*Item 4 Information on the Company*," "*Item 5 Operating and Financial Review and Prospects*" and "*Item 11 Quantitative and Qualitative Disclosures About Market Risk*"; and (b) statements that are preceded by, followed by or include the words "believes," "expects," "anticipates," "intends," "is confident," "plans," "estimates," "may," "might," "could," "would," the negatives of such terms or similar expressions.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Although we make such statements based on assumptions that we believe to be reasonable, there can be no assurance that actual results will not differ materially from our expectations. Many of the factors that will determine these results are beyond our ability to control or predict. We do not intend to review or revise any particular forward-looking statements referenced in this Form 20-F in light of future events or to provide reasons why actual results may differ. Investors are cautioned not to put undue reliance on any forward-looking statements.

Any of the following important factors, and any of those important factors described elsewhere in this or in other of our SEC filings, among other things, could cause our results to differ from any results that might be projected, forecast or estimated by us in any such forward-looking statements:

material adverse changes in economic conditions in Portugal or Brazil;

exchange rate fluctuations in the Brazilian Real and the U.S. dollar;

risks and uncertainties related to national and supranational regulation;

increased competition resulting from the liberalization of the telecommunications sector in Portugal and Brazil;

the success of our mobile operations in Brazil through our joint venture with Telefónica Móviles;

the development and marketing of new products and services and market acceptance of such products and services; and

the adverse determination of disputes under litigation.

PART I

ITEM 1 IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

We are not required to provide the information called for by Item 1.

ITEM 2 OFFER STATISTICS AND EXPECTED TIMETABLE

We are not required to provide the information called for by Item 2.

ITEM 3 KEY INFORMATION

Selected Consolidated Financial Data

The selected consolidated balance sheet data as of December 31, 2002 and 2003 and selected consolidated statement of income and cash flow data for each of the years ended December 31, 2001, 2002 and 2003 have been derived from our audited consolidated financial statements included herein. The selected consolidated balance sheet data as of December 31, 1999, 2000 and 2001 and selected consolidated statement of income and cash flow data for each of the years ended December 31, 1999 and 2000 have been derived from our audited consolidated financial statements not included herein.

We prepare our audited consolidated financial statements in accordance with Portuguese GAAP, which differs in certain significant respects from U.S. GAAP. See Notes 36, 37 and 38 to our audited consolidated financial statements for an explanation of the differences between Portuguese GAAP and U.S. GAAP. We have provided, in the information below, amounts in accordance with U.S. GAAP of operating revenues, operating income, net income, earnings per share, total assets, total liabilities and shareholders' equity for all periods and dates for which we have provided information.

The information set forth below is qualified by reference to, and should be read in conjunction with, our audited consolidated financial statements and the notes thereto and also "*Item 5 Operating and Financial Review and Prospects*" included in this Form 20-F.

During 1998, we acquired a 10.02% economic interest in, and voting control of, Telesp Celular S.A., or Telesp Celular, a mobile telecommunications operator in the Brazilian state of São Paulo. During 1999, we increased our economic interest in Telesp Celular to 13.92%. In January 2000, all shares of Telesp Celular owned by shareholders other than Telesp Celular Participações S.A., or TCP, were exchanged for newly-issued shares of TCP, and Telesp Celular became the wholly-owned operating subsidiary of TCP. In June 2000, we conducted a tender offer in Brazil for ordinary shares in TCP. As a result of the tender offer, we increased our economic interest in TCP to 29.92%. On November 7, 2000, TCP completed a capital increase in which we subscribed for additional shares in TCP, and, upon acquisition of such shares, our economic interest in TCP increased to 36.20%. In November 2000, after we exchanged with Telefónica our minority interest in Telesp Fixa (the wireline operator in the Brazilian state of São Paulo controlled by Telefónica) for an additional interest in TCP, we increased our economic interest in TCP further to 41.23%, our voting interest to 85.06% and our ownership of TCP's preferred shares to 17.7%. TCP completed a rights offering in September 2002, in which we subscribed to a total of 247,224 million common shares and 326,831 million preferred shares, thereby increasing our economic interest in TCP to 65.12%, our voting interest to 93.7% and our ownership of TCP's preferred shares to 49.8%. In October 2002, in connection with our agreements with Telefónica Móviles, S.A., or Telefónica Móviles (Telefónica's mobile telecommunications subsidiary), for the formation of Brasilcel (the 50/50 joint venture with Telefónica Móviles for mobile operations in Brazil), which operates under the brand name Vivo as of April 2003 and is referred to as Vivo elsewhere in this Form 20-F, we sold a 14.68% stake in TCP to Telefónica Móviles. On December 27, 2002, we transferred the rest of our interest in TCP to Vivo. We now hold, jointly with Telefónica Móviles, an indirect interest in TCP, as well as in the other Brazilian mobile telecommunications companies previously held directly by Telefónica Móviles. See "*Item 4 Information on the Company Our Businesses Brazilian Mobile Business*" and "*Item 4 Information on the Company Strategic Alliances Alliance with Telefónica*".

From July 1, 1998 until the end of 1999, we accounted for our interest in Telesp Celular by the proportional consolidation of its results in our consolidated financial statements in accordance with Portuguese GAAP. For the purposes of the reconciliation of our audited consolidated financial statements with U.S. GAAP, the financial statements of TCP were consolidated from July 1, 1998 using the full consolidation method. Since we increased our economic interest in TCP in 2000, our financial

statements for 2000 and 2001 fully consolidate the results of TCP in accordance with Portuguese GAAP.

As a result of the transfer of our interest in TCP to Vivo on December 27, 2002 and our acquisition of a 50% ownership interest in Vivo as of that date, our consolidated balance sheet as of December 31, 2002 and 2003 proportionally consolidates 50% of Vivo's assets and liabilities. Our consolidated statement of income and cash flow data for the year ended December 31, 2002 includes the full consolidation of TCP's income and cash flows. Our consolidated statement of income and cash flow data for the year ended December 31, 2003 proportionally consolidates 50% of Vivo's income and cash flows.

In February 2001, TCP acquired an 83% indirect economic interest in Global Telecom (corresponding to 49% of the voting rights), a mobile telecommunications company operating in the Brazilian states of Paraná and Santa Catarina. On December 27, 2002, TCP purchased the remaining 51% of the voting shares of the three holding companies that own Global Telecom and as a result holds a 100% indirect economic interest in Global Telecom. Our consolidated results of operations for the year ended December 31, 2002 presented below reflect the results of operations of Global Telecom based on the equity method of accounting. Global Telecom's assets and liabilities as of December 31, 2002 and 2003 are reflected in our consolidated balance sheet through our proportional consolidation of Vivo. Global Telecom's income and cash flows for the year ended December 31, 2003 are reflected in our consolidated statement of income and cash flows for the year ended December 31, 2003 through our proportional consolidation of Vivo's statement of income and cash flow data.

On April 25, 2003, TCP acquired a controlling interest in Tele Centro Oeste Participações, S.A., or TCO, a mobile telecommunications operator in the Midwestern and Northern regions of Brazil. As a result, TCO's assets and liabilities as of December 31, 2003 are reflected in our consolidated balance sheet as of that date through our proportional consolidation of Vivo, and TCO's income and cash flows from May through December 2003 are reflected in our consolidated statement of income and cash flows for the year ended December 31, 2003 through our proportional consolidation of Vivo's statement of income and cash flow data.

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Information provided in U.S. dollars for the year ended December 31, 2003 has been calculated on the basis of the Euro/U.S. dollar exchange rate on that date of €0.7938 = US\$1.00. See "Presentation of Financial Information" and "Exchange Rates".

Year Ended December 31,

	2003	2003	2002	2001	2000	1999
	US\$	EUR	EUR	EUR	EUR	EUR
STATEMENT OF PROFIT AND LOSS DATA:						
Amounts in accordance with Portuguese GAAP						
Operating revenues:						
Services rendered	6,369.6	5,056.5	4,950.9	4,976.3	4,329.8	2,832.4
Sales of merchandise and products	735.1	583.5	492.0	613.5	684.7	213.1
Telephone directory	171.5	136.1	139.1	136.8	131.7	126.1
Total operating revenues	7,276.2	5,776.1	5,582.0	5,726.6	5,146.2	3,171.6
Operating costs and expenses, excluding depreciation and amortization:						
Wages and salaries	889.2	705.9	694.8	668.6	578.1	520.8
Post retirement benefits	280.8	222.9	183.2	140.7	103.4	95.5
Costs of telecommunications	739.6	587.1	622.9	715.1	470.7	161.9
Subsidies	(26.0)	(20.6)	(31.5)	(36.8)	(38.1)	(38.5)
Maintenance and repairs	159.4	126.5	129.2	120.1	105.7	68.9
Own work capitalized	(93.8)	(74.5)	(114.0)	(179.3)	(133.9)	(120.8)
Raw materials and consumables	93.2	74.0	97.2	139.1	97.3	85.4
Costs of products sold	693.0	550.2	462.7	619.8	658.0	238.4
Telephone directories	113.9	90.4	92.0	89.2	87.1	82.2
Marketing and publicity	178.8	141.9	108.8	142.0	157.5	68.5
Concession rent			16.3	12.7	20.8	20.6
Other general and administrative	1,217.5	966.5	925.6	998.9	848.9	388.3
Provision for doubtful receivables, inventories & other	164.8	130.8	132.8	130.7	188.6	63.5
Other net operating income	(113.4)	(90.0)	(45.3)	(45.3)	(51.9)	(47.5)
Taxes other than income taxes	122.4	97.1	77.8	87.1	95.7	34.5
Total operating costs and expenses, excluding depreciation and amortization	4,419.5	3,508.4	3,352.5	3,602.6	3,187.9	1,621.7
Operating income before depreciation and amortization (EBITDA)	2,856.6	2,267.7	2,229.5	2,124.0	1,958.3	1,549.9
Depreciation and amortization	1,201.7	954.0	962.8	956.2	1,021.5	636.7
Operating income	1,654.9	1,313.7	1,266.7	1,167.8	936.8	913.2
Other expenses, net	302.8	240.3	543.9	1,063.5	423.8	261.5
Work force reduction program costs	395.7	314.1	53.7	183.9	252.7	457.7
Extraordinary items	78.0	62.0	15.6	281.1	(496.4)	(540.5)
Income before income taxes	878.4	697.3	653.5	(360.7)	756.7	734.5
Provision for income taxes	(476.0)	(377.9)	(337.1)	(174.6)	(258.6)	(241.9)
Consolidated net income before minority interests	402.4	319.5	316.4	(535.3)	498.1	492.6
Loss (income) applicable to minority interests	(99.8)	(79.2)	74.6	342.7	42.3	2.1

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Year Ended December 31,

Consolidated net income	302.6	240.2	391.1	(192.6)	540.3	494.7
Operating income per ordinary share, A share and ADS(1)	1.32	1.05	1.01	0.93	0.78	0.87
Earnings per ordinary share, A share and ADS(1)	0.24	0.19	0.31	(0.15)	0.45	0.47
Cash dividends per ordinary share, A share and ADS(1)(2)(3)	0.28	0.22	0.16	0.10		0.20
Share capital	1,580.0	1,254.3	1,254.3	1,254.3	1,201.8	1,045.0

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Amounts in accordance with U.S. GAAP						
Operating revenues	5,618.3	4,460.0	6,007.7	6,042.8	5,199.9	4,107.3
Operating income as restated(6)	910.8	723.1	383.2	696.1	395.8	592.7
<hr/>						
Net income before change in accounting principles as restated(6)	183.3	145.5	1,315.3	208.1	66.8	532.8
Cumulative effect of a change in accounting principles SAB 101					(126.7)	
Cumulative effect of a change in accounting principles SFAS 133				(57.5)		
Cumulative effect of a change in accounting principles SFAS 142			(1,038.9)			
Cumulative effect of a change in accounting principles SFAS 143	(9.3)	(7.4)				
<hr/>						
Net income after change in accounting principles as restated(6)	174.0	138.2	276.4	150.6	(59.8)	532.8
<hr/>						
Earnings per ordinary share, A share and ADS as restated(4)(6)	0.14	0.11	0.22	0.12	(0.05)	0.54
Diluted net income per share as restated(5)(6)	0.14	0.11	0.21	0.12	(0.05)	0.53
On a pro-forma basis(7)						
Net income before change in accounting principles SAB 101 as restated(6)	174.0	138.2	276.4	150.6	66.8	532.8
Net income after change in accounting principles SAB 101 as restated(6)	174.0	138.2	276.4	150.6	(59.8)	528.5
Earnings per ordinary share, A share and ADS after change in accounting principles SAB 101 as restated(4)(6)	0.14	0.11	0.22	0.12	(0.05)	0.53
Diluted net income per share after change in accounting principles SAB 101 as restated(5)(6)	0.14	0.11	0.21	0.12	(0.05)	0.52

- (1) Based on 1,045,000,000 ordinary and A shares issued in the year ended December 31, 1999, 1,201,750,000 ordinary and A shares issued in the year ended December 31, 2000 and 1,254,285,000 ordinary and A shares issued in the years ended December 31, 2001, 2002 and 2003.
- (2) Dividends for the year ended December 31, 2000 were not paid.
- (3) Cash dividends per ordinary share, A share and ADS for the years ended December 31, 1999, 2001, 2002 and 2003 in US\$ were US\$0.20, US\$0.09, US\$0.17 and US\$0.28, respectively.
- (4) Based on the weighted average number of shares as of the date given and taking into account the number of shares issued pursuant to capital increases and all treasury shares, there were 991,182,122 shares for the year ended December 31, 1999, 1,091,826,182 shares for the year ended December 31, 2000, 1,228,392,386 shares for the year ended December 31, 2001, 1,253,880,328 shares for the year ended December 31, 2002 and 1,249,778,188 shares for the year ended December 31, 2003.
- (5) The weighted average number of shares is computed as a weighted average as of the date given and taking into account the number of shares from the exchangeable bonds issued on June 4, 1999 and December 6, 2001, assuming conversion of the bonds into ordinary shares. For the years ended December 31, 2000, 2001 and 2003, the effects of the exchangeable bonds have been excluded from the calculation of diluted earnings per share since they would be antidilutive.
- (6) Operating income and net income for the years ended December 31, 1999, 2000 and 2001 have been restated to include the effect of the reduction in the reported amortization expense for the translated carrying value of goodwill in Portugal Telecom's investment in Telesp Celular Participações, as discussed in Note 36 c1) to our audited consolidated financial statements.
- (7) The pro-forma information shows the application of SAB 101, as if it had been applied in the year ended December 31, 1999.

Year Ended December 31,

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Year Ended December 31,

2003	2003	2002	2001	2000	1999
US\$	EUR	EUR	EUR	EUR	EUR

CASH FLOW DATA:

Amounts in accordance with Portuguese GAAP

Cash flows from operating activities	2,940.2	2,334.0	2,092.3	1,475.4	1,357.6	1,109.6
Cash flows from investing activities	(578.9)	(459.5)	(1,009.6)	(2,528.5)	(2,343.2)	(741.3)
Cash flows from financing activities	(2,083.7)	(1,654.1)	(486.1)	1,839.9	1,131.0	(1,425.6)

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Year Ended December 31,

	2003	2003	2002	2001	2000	1999
	US\$	EUR	EUR	EUR	EUR	EUR

(in millions, except number of ordinary shares)

BALANCE SHEET DATA:

Amounts in accordance with Portuguese GAAP

Current assets	6,348.5	5,039.7	4,850.9	3,628.1	2,032.6	1,205.1
Investments, net	564.4	448.1	376.4	2,000.3	1,295.3	1,498.2
Fixed assets, net	5,376.3	4,268.0	4,575.8	5,491.3	5,446.2	3,855.9
Intangible assets post retirement benefits				761.9	495.0	399.1
Intangible assets other, net	3,968.2	3,150.1	2,968.7	4,934.4	3,878.8	1,492.3
Other non-current assets, net	821.3	652.0	954.3	820.3	68.3	67.1
Total assets	17,078.8	13,557.8	13,726.1	17,636.3	13,216.2	8,517.7
Current liabilities	4,225.6	3,354.5	2,958.0	3,240.0	3,154.2	1,535.6
Long-term debt	5,738.7	4,555.6	5,219.1	5,428.3	2,815.2	2,649.6
Accrued post retirement liability	1,582.2	1,256.0	1,061.5	1,810.0	1,488.0	1,228.0
Deferred income investment subsidies	48.8	38.7	51.1	63.1	113.7	153.4
Deferred income post retirement benefits				23.0	26.2	28.5
Other non-current liabilities	967.6	768.1	878.0	1,685.1	143.7	85.4
Total liabilities	12,563.0	9,973.0	10,167.6	12,249.5	7,741.0	5,680.5
Net assets	4,515.8	3,584.8	3,558.5	5,386.7	5,475.2	2,837.2
Minority interests	811.2	644.0	447.2	1,220.0	1,113.1	78.2
Total shareholders' equity	3,704.6	2,940.8	3,111.3	4,166.8	4,362.1	2,759.0
Total liabilities and shareholders' equity	17,078.8	13,557.8	13,726.1	17,636.3	13,216.2	8,517.7
Number of ordinary shares	1,254,284,500	1,254,284,500	1,254,284,500	1,254,284,500	1,201,749,500	935,750,000

Amounts in accordance with U.S. GAAP

Total assets as restated(1)	14,819.4	11,764.3	12,554.2	16,747.8	14,534.6	11,958.7
Total liabilities as restated(1)	12,045.3	9,562.1	10,167.9	11,902.5	9,019.4	7,121.8
Total shareholders' equity as restated(1)	2,518.1	1,999.0	2,343.7	3,736.5	4,191.8	3,342.3

(1)

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Assets, liabilities and shareholders' equity as of December 31, 2001, 2000 and 1999 have been restated to include the effect of translation of goodwill in Telesp Celular Participações and the minimum pension liability adjustment, as discussed in Note 36 c1) to our audited consolidated financial statements.

Exchange Rates

Euro

Effective January 1, 1999, Portugal joined ten other member countries of the European Union in adopting the Euro as the common currency. During the transition period between January 1, 1999 and December 31, 2001, the Escudo remained legal tender in Portugal as a denomination of the Euro, and public and private parties paid for goods and services in Portugal using either the Euro or the Escudo. On January 1, 2002, the Euro entered into cash circulation, and from January 1, 2002 through February 28, 2002, both the Euro and the Escudo were in circulation in Portugal. From March 1, 2002, the Euro became the sole circulating currency in Portugal.

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For the years ended December 2001, 2002 and 2003, the majority of our revenues, assets and expenses were denominated in Euro, although a significant portion of our assets and liabilities are denominated in Brazilian Reais and certain of our liabilities are denominated in U.S. dollars. We have published our audited consolidated financial statements in Euro and our shares trade in Euro on the Euronext Lisbon Stock Exchange. Our financial results could be affected by exchange rate fluctuations in the Brazilian Real and U.S. dollar. See "Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources Exchange Rate Exposure to the Brazilian Real and the U.S. Dollar".

Our future dividends, when paid in cash, will be denominated in Euros. As a result, exchange rate fluctuations have affected and will affect the U.S. dollar amounts received by holders of ADSs on conversion of such dividends by The Bank of New York as the ADS depository. The Bank of New York converts dividends it receives in foreign currency into U.S. dollars upon receipt, by sale or such other manner as it has determined, and distributes such U.S. dollars to holders of ADSs, net of The Bank of New York's expenses of conversion, any applicable taxes and other governmental charges. Exchange rate fluctuations may also affect the U.S. dollar price of the ADSs on the New York Stock Exchange.

The following tables show, for the period and dates indicated, certain information regarding the U.S. dollar/Euro exchange rate. The information is based on the noon buying rate in the City of New York for cable transfers in Euro as certified for United States customs purposes by the Federal Reserve Bank of New York. On June 15, 2004, the Euro/U.S. dollar exchange rate was €0.8231 per US\$1.00.

Year ended December 31,	Average Rate(1)
	(EUR per US\$1.00)
1999	0.9447
2000	1.0873
2001	1.1217
2002	1.0561
2003	0.8786

(1) The average rate is calculated as the average of the noon buying rates on the last day of each month during the period.

Period	High	Low
	(EUR per US\$1.00)	
December 31, 2003	0.7989	0.7907
January 31, 2004	0.8095	0.8009
February 29, 2004	0.8079	0.8009
March 31, 2004	0.8220	0.8116
April 30, 2004	0.8389	0.8332
May 31, 2004	0.8209	0.8168

None of the 25 member countries of the European Union has imposed any exchange controls on the Euro.

Brazilian Real

Although the majority of our revenues, assets and expenses are denominated in Euros, most of the revenues, assets and expenses from our Brazilian investments are denominated in Brazilian Reais. Consequently, exchange rate fluctuations between the Euro and the Brazilian Real affect our revenues.

There are two principal legal foreign exchange markets in Brazil: the commercial rate exchange market and the floating rate exchange market.

Most trade and financial foreign-exchange transactions are carried out on the commercial rate exchange market. These transactions include the purchase or sale of shares or payment of dividends or interest with respect to shares. Foreign currencies may only be purchased through a Brazilian bank authorized to operate in these markets. In both markets, rates are freely negotiated but may be influenced by Central Bank intervention. In 1999, the Central Bank placed the commercial rate exchange market and the floating rate exchange market under identical operational limits, which led to a convergence in the pricing and liquidity of both markets. Since February 1, 1999, the floating market rate has been the same as the commercial market rate, and the system relying on the foreign exchange rate band has been eliminated. However, there is no guarantee that these rates will continue to be the same in the future. Despite the convergence in pricing and liquidity of both markets, each market continues to be regulated separately.

The Brazilian government may impose temporary restrictions on the conversion of Reais into foreign currencies and on the remittance to foreign investors of proceeds from their investments in Brazil. Brazilian law permits the government to impose these restrictions whenever there is a serious imbalance in Brazil's balance of payments or reason to foresee a serious imbalance.

The following tables show, for the periods and date indicated, certain information regarding the Real/U.S. dollar exchange rate. On June 15, 2004, the Real/U.S. dollar exchange rate was R\$3.1227 per US\$1.00. The information is based on the noon buying rate in the City of New York for cable transfers in Brazilian Reais as certified for United States customs purposes by the Federal Reserve Bank of New York.

Year ended December 31,	Average Rate(1)
	(R\$ per US\$1.00)
1999	1.8641
2000	1.8333
2001	2.3507
2002	2.9886
2003	3.0565

(1) The average rate is calculated as the average of the noon buying rates on the last day of each month during the period.

Period	High	Low
	(R\$ per US\$1.00)	
December 31, 2003	2.9070	2.8785
January 31, 2004	2.9581	2.9170
February 29, 2004	2.9447	2.9085
March 31, 2004	2.9117	2.9010
April 30, 2004	2.9705	2.9370
May 31, 2004	3.1650	3.0770

Escudo

As of January 1, 2002, we ceased to use the Escudo. For the years ended December 31, 2001, 2002 and 2003, the majority of our revenues, assets and expenses were denominated in Euros. As a result, revenues, assets and expenses for years prior to 2001 have been translated from Escudos into Euros. All figures previously stated in Escudos have been converted to figures in Euro based on the fixed Escudo/Euro exchange rate, established on January 1, 1999, of PTE 200.482 per €1.00 or approximately €0.005 per PTE 1.00. See "Euro".

Risk Factors

Rapidly Growing Competition From Mobile Telephone and From Other Wireline Operators Could Significantly Reduce Our Wireline Businesses' Revenues

During 2003, approximately 37% of our consolidated revenues were derived from services provided by our wireline business in Portugal. Currently, the competition for these services comes from the rapid growth of mobile telephone services and from other wireline providers. As a result of the substitution of mobile for fixed telephone services, combined with the increase in competition, we have experienced, and may continue to experience, erosion of market share of both access lines and of outgoing domestic and international traffic. The number of active mobile telephone cards in Portugal has overtaken the number of wireline main lines. Some of our wireline customers are using mobile services as an alternative to wireline telephone services. Mobile operators can by-pass our international wireline network by interconnecting directly with wireline and mobile networks either in our domestic network or abroad. Competition is also forcing down the prices of our wireline telephone services for long distance and international calls. Lowering our international call prices has caused a significant decline in our revenues from international wireline telephone services.

The Portuguese telecommunications sector was opened to full competition on January 1, 2000. As a result, competitive pressure on our wireline telephone services has intensified. Other companies are now allowed to offer wireline telephone services to the general public. They can connect transmission lines they lease from us or from new network operators to our local and long distance network. They are also allowed to build their own networks.

The decrease in wireline traffic and lower tariffs resulting from competition could significantly harm our overall revenues. See "Item 4 Information on the Company Competition Competition Facing our Wireline Business".

A Growing Percentage of Our Revenue Is Derived From Businesses That Are Subject to Rapid and Sometimes Unpredictable Changes in Technology and to Increasing Competition

During 2003, approximately 63% of our consolidated revenues were derived from businesses other than our wireline business in Portugal. These businesses include mainly mobile telecommunications and multimedia services, particularly in Portugal and Brazil.

We believe that the development of mobile telecommunications and multimedia services presents our company with appreciable growth opportunities. However, the success of our mobile telecommunications and multimedia businesses is subject to rapid and sometimes unpredictable changes in technology and to increasing competition. These businesses also may have unforeseen capital requirements and shifts in customer preferences and demographics. Our business and financial results could suffer:

if we fail to compete effectively in these new businesses and markets;

if we fail to adapt on a timely and efficient basis to changes in technology;

if we cannot attract and retain employees with the requisite skill level necessary to build these new businesses; or

if customer usage does not increase, or if it declines or evolves away from the technologies and businesses in which we are investing.

Burdensome Regulation in an Open Market May Put Us at a Disadvantage to Our Competitors

The Portuguese telecommunications sector is highly competitive and is now fully open to competition. The Portuguese government, however, still imposes on us regulatory restrictions and

obligations dating from the previous monopoly environment. Many of the restrictions and obligations do not apply to other telecommunications operators and service providers in Portugal. The substantial resources we must commit to fulfill these obligations could adversely affect our ability to compete. See "*Item 4 Information on the Company Regulation Portugal*".

Regulation of Our Interconnection Rates Could Give Other Service Providers an Unfair Competitive Advantage

European Union and Portuguese regulations require us to allow other telecommunications network operators and service providers to connect their networks to ours and to terminate calls for them. We believe the interconnection rates should reflect the cost of operating our network in Portugal. The Portuguese regulatory authorities may, however, set our rates at levels comparable to rates in certain other EU countries, where interconnection rates are lower than the current rates in Portugal. See "*Item 4 Information on the Company Regulation Portugal*".

The Portuguese Government Could Terminate Our Wireline Concession and Licenses

Through our subsidiary PT Comunicações, S.A., we provide a significant number of services under a Concession and licenses granted to us by the Portuguese government. The Concession runs until 2025, with provisions for renewal. The Portuguese government can revoke the Concession after 2010, if it considers the revocation to be in the public interest. It can also terminate our Concession at any time if we fail to comply with our obligations under it. The Portuguese government can also terminate our licenses under certain circumstances. If the Portuguese government took such action, we would not be able to conduct the activities authorized by the Concession or the relevant licenses. This loss would eliminate an important source of our revenues. During 2002, we acquired the ownership of the basic network used for our fixed line services and such assets will no longer revert to the Portuguese State on termination of the Concession Agreement.

Regulatory Investigations and Litigation May Lead to Fines or Other Penalties

We are regularly involved in litigation and regulatory inquiries and investigations involving our operations. ANACOM, the Portuguese telecommunications regulator, the European Commission and the Autoridade da Concorrência, the Portuguese competition authority, can make inquiries and conduct investigations concerning our compliance with applicable laws and regulations. Current inquiries and investigations include a preliminary investigation by the Autoridade da Concorrência relating to alleged anti-competitive practices by PT Comunicações and PT Prime. See "*Item 4 Information on the Company Regulation Regulatory Institutions*" and "*Item 8 Financial Information Legal Proceedings Regulatory Proceedings*".

If we are found to be in violation of applicable laws and regulations in this or other regulatory inquiries and investigations, or in litigation proceedings, which are currently pending against us or which may be brought against us in the future, we may become subject to substantial penalties, fines, damages or other sanctions. Any adverse outcome could have a material adverse effect on our operating results or cash flows.

The Portuguese Government Holds All of Our A Shares Which Afford It Special Approval Rights

All of our A shares are held by the Portuguese government. Under our articles of association, as the holder of all of our A shares, the Portuguese government may veto a number of actions of our shareholders, including the following:

election of one-third of the directors, including the chairman of the board of directors;

authorization of a dividend in excess of 40% of our distributable net income in any year;

capital increases and other amendments to our articles of association;

issuance of bonds and other securities;

authorization for a shareholder that is engaged in an activity in competition with us to hold more than 10% of our ordinary shares;

altering our general objectives, strategy or policies; and

defining our investment policies, including the authorization of acquisitions and disposals.

An ADS Holder May Face Disadvantages Compared to an Ordinary Shareholder When Attempting to Exercise Voting Rights

Holders of our ADSs may instruct the depositary to vote the ordinary shares underlying the ADSs. For the depositary to follow the voting instructions, it must receive them on or before the date specified in our voting materials. The depositary must try, as far as practical, subject to Portuguese law and our articles of association, to vote the ordinary shares as instructed. In most cases, if the ADS holder does not give instructions to the depositary, it may vote the ordinary shares in favor of proposals supported by Portugal Telecom's board of directors, or, when practicable and permitted, give a discretionary proxy to a person designated by us. We cannot be certain that ADS holders will receive voting materials in time to ensure that they can instruct the depositary to vote the underlying ordinary shares. Also, the depositary is not responsible for failing to carry out voting instructions or for the manner of carrying out voting instructions. This means that ADS holders may not be able to exercise their right to vote and there may be nothing they can do if their ordinary shares or other deposited securities are not voted as requested.

We Are Exposed to Exchange Rate and Interest Rate Fluctuations

We are exposed to exchange rate fluctuation risks mainly due to the significant level of our investments in Brazil. These investments are not hedged against exchange rate fluctuations. We are required to make adjustments to our equity on our balance sheet in response to fluctuations in the value of foreign currencies in which we have made investments. For example, as of December 31, 2003, cumulative foreign currency transaction adjustments related to investments in Brazil were negative €2,234.0 million. Further devaluations in the Brazilian Real could result in further negative adjustments. See "*Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources Equity*" and "*Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources Exchange Rate Exposure to the Brazilian Real and the U.S. Dollar*".

All of the debt of our Brazilian subsidiaries is either Real-denominated or has been swapped into Reais and, thus, is not exposed to exchange rate fluctuations.

We are also exposed to interest rate fluctuation risks. We have entered into financial instruments to reduce the impact on our earnings of an increase in market interest rates, but there can be no assurance that such instruments will continue to reduce the impact of interest rate fluctuations in the future or that these financial instruments will prevent unexpected and material fluctuations of interest rates from having any material adverse effect on our earnings.

An Economic Crisis in Brazil Could Reduce Expected Returns on Our Brazilian Investments

A material portion of our business, prospects, financial condition and results of operations is dependent on general economic conditions in Brazil. In particular, it depends on economic growth and its impact on demand for telecommunications and other related services. Since 1998, we have made

significant investments in Brazil. The major factors that could have a material adverse effect on our investments and results of operations in Brazil, including Vivo, are:

Adverse political and economic conditions. The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. The Brazilian government has utilized salary and price controls, currency devaluation and foreign exchange controls as tools in its previous attempts to stabilize the Brazilian economy and control inflation. Changes in the government's exchange control policy, or in general economic conditions in Brazil, could have a material adverse effect on the results of our operations in Brazil. Deterioration in economic and market conditions in other countries (mainly in other Latin American and emerging market countries) may adversely affect the Brazilian economy and our business.

Devaluation of the Real and increases in interest rates. The Brazilian currency has historically experienced frequent devaluations. The Real devalued against the Euro by 1.1% in 2000, by 12.8% in 2001 and by 81.4% in 2002. During 2002, the Real underwent significant devaluation due in part to political uncertainty in connection with the elections and the global economic slowdown. In the period leading up to, and after, the general election in 2002, there was substantial uncertainty relating to the policies that the new government would pursue, including the potential implementation of macroeconomic policies that would differ significantly from those of the prior administration. This uncertainty resulted in a loss of confidence in the Brazilian capital markets, and the continued devaluation of the Real. The Real appreciated during 2003 against the Euro by 0.11% amidst indications that the new government is doing better than expected. Any substantial negative reaction to the policies of the Brazilian government could have a negative impact, including devaluation. The devaluation of the Real could negatively affect the stability of the Brazilian economy. A devaluation of the Real relative to the Euro could negatively affect the profitability and results of our operations. It would also increase costs associated with financing our operations in Brazil. In addition, a devaluation of the Real relative to the U.S. dollar may increase the costs of imported products and equipment. Our operations in Brazil rely on imported equipment and, as a result of such devaluation, such equipment would be more expensive to purchase.

As all debt issued in Brazil is denominated in or swapped into Real, a devaluation of this currency against the Euro could decrease our total debt, although this impact could be offset by the differential between Euro and Real interest rates.

The current international economic environment is unfavorable, and the flow of foreign investments into Brazil may be diminishing. To make up for the decrease in foreign and invested capital and revenue, the Brazilian government may have to raise funds at higher interest rates. A slowdown of the U.S. economy may also adversely affect the Brazilian economy, as well as interest rates in Brazil. An increase in interest rates could negatively affect our profitability and results of operations and would increase the costs associated with financing our operations in Brazil. In addition, such an increase would raise our interest costs because part of the interest on our debt is floating, primarily in relation to Real-denominated debt, which floats based on the commercial rate exchange market.

Inflation in Brazil. Brazil has historically experienced extremely high rates of inflation. Inflation, as well as governmental measures put in place to combat inflation, have had a material adverse effect on the Brazilian economy. Since the implementation of the Real Plan in 1994, the rate of inflation has been substantially lower than in previous periods. However, inflationary pressures persist, and actions taken in an effort to curb inflation, coupled with public speculation about possible future governmental actions, have contributed to economic uncertainty in Brazil and heightened volatility in the Brazilian securities market. The general price index, or the IGP-DI (the Índice Geral de Preços Disponibilidade Interna), an inflation index developed by the Fundação Getúlio Vargas, a private Brazilian economic organization, reflected inflation of 7.67% in 2003 compared to 26.41% in 2002 and 10.40% in 2001. If Brazil continues to experience significant inflation, Vivo may be unable to increase service rates to its

customers in amounts that are sufficient to cover its increasing operating costs, and its business may be adversely affected, which could in turn have an adverse effect on our results of operations.

Our Strategy of Enhancing Our Mobile Operations in Brazil Through Our Joint Venture With Telefónica Móviles May Not Be Successful

The successful implementation of our strategy for our mobile operations in Brazil depends on the development of our mobile services joint venture company with Telefónica Móviles. On December 27, 2002, we and Telefónica Móviles transferred our direct and indirect interests in Brazilian mobile operators to the mobile services joint venture company, Brasilcel, operating under the brand name Vivo, with headquarters in the Netherlands.

As in any joint venture, it is possible that Telefónica Móviles and we will not agree on Vivo's strategy, operations or other matters. Any inability of Telefónica Móviles and us to operate Vivo jointly could have a negative impact on Vivo's operations, which could have a negative impact on our strategy in Brazil and could have a material adverse effect on our results of operations. In addition, we cannot be sure that Vivo will be able to take advantage of its position in the Brazilian market to increase the scope and scale of its operations or that any anticipated benefits of the joint venture will be realized. See "*Item 4 Information on the Company Strategic Alliances Alliance with Telefónica*".

Regulation May Have a Material Adverse Effect on Vivo's Results

Our mobile business in Brazil is subject to extensive government regulation, including certain regulatory restrictions and obligations relating to licenses, competition, taxes and rates (including interconnection rates) applicable to mobile telephone services. Changes in the regulatory framework and the opening of the market to other competitors in the mobile telecommunications sector may have a negative impact on Vivo's revenues and results of operations. Moreover, Vivo's operating subsidiaries are restricted from increasing some of the rates that they charge for services provided even if the devaluation of the Real and an increase of interest rates by the Brazilian government increase their costs. Such circumstances may limit Vivo's flexibility in responding to market conditions, competition and changes in its cost structure, which could have a material adverse effect on its results of operations and in turn adversely affect our results of operations.

The Conditions Applying to Vivo's Subsidiaries Under the New SMP Licensing Regime May Result in Reducing Our Revenues and Results of Operations

In September 2000, ANATEL, the Brazilian telecommunications regulator, introduced a new mobile services licensing regime, referred to as the SMP regime. The SMP regime permits existing mobile service providers operating under concessions to migrate to the SMP regime and become SMP license holders. Each of Vivo's subsidiaries has migrated to the SMP regime and now holds a SMP license instead of their previous concessions.

The new SMP regime imposes restrictions on the provision of wireline services. As a result of the restrictions, because ANATEL considers Vivo's subsidiaries to be affiliated with Telefónica, which provides wireline long distance services in the state of São Paulo and was awarded a license to provide such services nationwide, ANATEL will not award a wireline long distance license to any of Vivo's subsidiaries. As a result, Vivo's subsidiaries no longer receive revenues from wireline long distance services but receive revenues from interconnection fees paid by wireline long distance operators for wireline long distance traffic originating and terminating on their networks. The interconnection fees do not fully compensate, however, for the loss of wireline long distance revenues, and this has had a negative impact on the overall revenues of Vivo's subsidiaries.

Under the SMP regime, an SMP mobile operator will pay for the use of another SMP mobile operator's network in the same authorization area only if the traffic carried from the first operator to

the second exceeds 55% of the total traffic exchanged between them. In that case, only those calls that have surpassed the 55% level will be subject to payment for network usage. This rule is valid until June 30, 2005, after which no payments will be due for network usage between SMP networks, regardless of the amount of traffic. As a result, if the traffic Vivo's subsidiaries terminate for other SMP mobile operators exceeds the traffic other SMP mobile operators terminate for Vivo's subsidiaries, Vivo's, and consequently our, revenues and results of operations may be adversely affected. See "*Item 4 Information on the Company Regulation Brazil SMP Regulation*".

Interconnection Negotiations May Not Result in Sufficiently Remunerative Revenues for Terminating Calls on the Mobile Networks of Vivo's Subsidiaries and May Negatively Affect our Revenues

Under the new SMP regime, interconnection fees for termination of calls on mobile networks will be determined by commercial negotiation between Vivo's subsidiaries and the wireline operators after June 30, 2004. The conditions of the network usage fee negotiations will be regulated by ANATEL. Because a significant number of mobile subscribers use prepaid mobile services and typically receive more calls than they make, Vivo's subsidiaries derive an important part of their revenues from the interconnection fees paid to them by the wireline operators due to traffic originating on wireline networks and terminating on their mobile networks. If the interconnection fees are reduced, operating revenues may be negatively affected as a result.

Vivo Faces Substantial Competition in Each of its Markets that may Reduce its Market Share and Harm our Financial Performance

Since the opening of the Brazilian market for mobile telecommunications services to competition in 1998, several licenses have been granted for mobile telecommunications services in the areas where Vivo's subsidiaries operate. The introduction of the SMP regime has further increased the number of licensees, which has intensified competition. There has been consolidation in the Brazilian telecommunications market, and we believe this trend may continue. Consolidation may result in increased competitive pressures within the market, for example if financially stronger companies are better positioned to compete with Vivo's subsidiaries or if some brand names become better known than others. Vivo's subsidiaries may be unable to respond adequately to pricing and other competitive pressures resulting from consolidation, which would adversely affect their businesses, financial condition and results of operations. The level of competition from wireline service providers is also increasing. Failure by Vivo's subsidiaries to compete successfully could result in them losing market share and revenues. For more information about the various bands of licenses granted for mobile services in Vivo's coverage areas and competing operators, see "*Item 4 Information on the Company Competition Competition Facing Vivo in Brazil*".

ITEM 4 INFORMATION ON THE COMPANY

Overview

Portugal Telecom's legal and commercial name is Portugal Telecom, SGPS, S.A. Portugal Telecom is a limited liability holding company, organized as a *Sociedade Gestora de Participações Sociais* under the laws of the Republic of Portugal. The company was originally incorporated as Portugal Telecom, S.A., a *sociedade anónima* in June 1994. Our principal offices are located at Avenida Fontes Pereira de Melo, 40, 1069-300 Lisboa, Portugal. Our telephone number is +351 21 500 1701 and our facsimile number is +351 21 355 6623. Portugal Telecom's agent for service of process in the United States is CT Corporation System at 111 Eighth Avenue, New York, New York 10011. Our home page is located at www.telecom.pt. The information on our website is not part of this report. The website address is included as an indicative textual reference only.

We provide telecommunications and multimedia services in Portugal and Brazil. Our service offering covers a full range of:

wireline services, which include fixed line telephone services for retail and wholesale customers, leased lines, interconnection, distribution of programming for TV and radio broadcasters, Internet access, data and business solutions, portal and e-commerce services;

mobile telecommunications services, such as voice, data and Internet-related services;

multimedia services, such as cable and satellite television services and TV programming, film distribution and screening, newspaper publishing and distribution, radio programming and Cable Internet; and

sales of telecommunications equipment.

In Portugal, we are the leading provider of all of these services. The provision of wireline services in Portugal continues to account for a larger proportion of our revenues (37% during 2003) as compared to revenues derived from any other line of business in our group. In Brazil, we have a leading position in the mobile market. To strengthen our position in the Brazilian mobile telecommunications market, we entered into a strategic alliance with Telefónica Móviles, the Spanish telecommunications company, pursuant to which we created, on December 27, 2002, a new mobile telecommunications services company in Brazil, Brasilcel, which was rebranded Vivo on April 8, 2003. See " *Brazilian Mobile Business*", below.

We are focusing our efforts on market segments and businesses that have the potential for high growth, and we are positioning our company as the leading integrated supplier of a full range of telecommunications services in Portugal. We derive an increasing share of our revenues from new services in fast-growing businesses in Portugal, such as mobile services, multimedia and Internet services, and from mobile services in Brazil.

The telecommunications market is increasingly characterized by new opportunities resulting from technological development, the growth in demand for mobile and Internet-related services and the increasing use of information technology in telecommunications services. Our objectives are to:

continue to leverage our experience as the leading provider of wireline, mobile and multimedia services in Portugal;

capitalize on our leading position in the Portuguese market to preserve the profitability and cash flow of our wireline and mobile businesses;

exploit new growth opportunities in service areas, such as multimedia and Internet services in Portugal; and

continue to pursue opportunities for growth in the mobile business in Brazil, through Vivo.

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For information regarding our current and historic principal capital expenditures and divestitures, see "*Item 5 Operating and Financial Review and Prospects Capital Investment and Research and Development*".

Our Businesses

Business Units

Our market is characterized by increasing competition and rapid technological change. In 1999, the board of directors of Portugal Telecom adopted a plan to reorganize the company to better position it in this competitive market. As part of our reorganization, Portugal Telecom changed its name and corporate purpose from Portugal Telecom, S.A., a telecommunications operating company, to Portugal Telecom, SGPS, S.A., a group holding company, and we aligned our subsidiaries according to business lines. Portugal Telecom's business unit subsidiaries are held by Portugal Telecom in its role as holding company. We have integrated different functions across the board, with particular emphasis on information systems (PT Sistemas de Informação), research and development capabilities (PT Inovação), back office activities (PT Pro), central purchasing capabilities (PT Compras) and call center operations (PT Contact). In addition, in April 2004 we created Portugal Telecom Investimentos Internacionais Consultoria Internacional, S.A. to manage all of our international businesses. See "*Item 5 Operating and Financial Review and Prospects Overview Our Business Reorganization and Revenue Reporting Categories*".

The diagram below presents our different businesses, taking into account the internal reorganization we initiated during 2003 and completed in the first quarter of 2004.

-
- (1) Providing wireline services in Portugal, including our fixed telephone service, Internet access services, wholesale services and data and business solutions services.
 - (2) In our discussion of this business segment below, we have provided a diagram of the organizational structure of Vivo.
 - (3) Providing multimedia services in Portugal, including cable operations through TV Cabo, audiovisuals services through Lusomundo Audiovisuals and Lusomundo Cinemas, and media services through Lusomundo Media. In our discussion of this business segment below, we have provided a diagram of the different businesses operating under PT Multimédia Serviços de Telecomunicações e Multimédia, SGPS, S.A., or PT Multimedia.
 - (4) Various international investments, including global telecommunications operators in Cabo Verde Islands and Macau, mobile operators in Morocco, Angola and Botswana, and other investments in various countries.
 - (5) Various instrumental companies providing services to PT group companies, including PT Sistemas de Informação (information systems), PT Inovação (research and development), PT Pro (shared services), PT Compras (central purchasing) and PT Contact (call centers).

Wireline Business

Our wireline business consists of the three operating companies, PT Comunicações, PT Prime and PTM.com, which are currently managed on an integrated basis, providing the following services on our wireline network:

retail, including fixed line telephone services and Internet access services to residential and small office home office customers;

wholesale, including leased lines, transmission of television and radio signals and interconnection services;

data and corporate, including data communications, leased lines to major clients, network managing and outsourcing; and

other wireline services, including our directories business and sales of telecommunications equipment.

PT Comunicações holds and operates our fixed line network, providing fixed line telephone services, wholesale services, directories and sales of telecommunications equipment. PT Comunicações provides fixed line telephone services pursuant to a Concession granted to us by the Portuguese government and transferred to PT Comunicações pursuant to Decree Law 219/2000. On December 11, 2002, PT Comunicações entered into a definitive agreement to acquire full ownership of the basic telecommunications network from the Portuguese government for €365 million, which included the 2002 Concession rental payment of €16.6 million. Since then, PT Comunicações has owned the basic telecommunications network.

PT Prime offers corporate customers in Portugal data and corporate services through a "one-stop-shop" for a variety of flexible, efficient and innovative solutions using information technology, telecommunications, Internet and outsourcing. Until October 6, 2003, we held 87.5% of the share capital of PT Prime. SIBS, a Portuguese entity operating the ATM network and the inter-bank payment system in Portugal, held the remaining 12.5%. On July 20, 2003, we signed an agreement with SIBS for the acquisition of its 12.5% stake in PT Prime for €39 million, which was completed on October 6, 2003.

PTM.com is the leading Internet company in Portugal, operating as an Internet access service provider using our fixed line network and in portal and related activities through sapo.pt, Portugal's leading Internet portal. PTM.com was formed in March 2000 by PT Multimedia to aggregate all of its Internet activities focused on the residential and small and medium size enterprise markets. On October 17, 2002, we entered into an agreement with PT Multimedia to acquire its 100% interest in PTM.com. The sale of PT Multimedia's Internet business to us was intended to encourage the continued growth of our broadband businesses and increase the loyalty of fixed line subscribers, while providing a single platform for investment and development of on-line services and content for the Portugal Telecom group. The results from our services provided through PTM.com have been included in our wireline business segment since 2003. We have adjusted our results for prior years to include PTM.com's results in our wireline business segment, as opposed to our PT Multimedia business segment. See "*Item 5 Operating and Financial Review and Prospects Overview Our Business Reorganization and Reporting Categories*".

Fixed Line Network. We, through PT Comunicações and PTM.com, maintained approximately 4.2 million main lines in service at December 31, 2003, excluding external supplementary lines, direct extensions and active multiple numbers. We break our fixed line network down into traditional main lines (PSTN), ISDN lines and ADSL lines. Because of their large capacity, we count ISDN lines, which transmit voice and data at higher rates than analog lines, as equivalent to either two or up to 30 (depending on whether they are basic or primary ISDN lines) traditional main lines. Using this

counting convention, total main lines included approximately 812,530 equivalent ISDN lines. We offer high-speed Internet access through ADSL lines. As of December 31, 2003, we had 188 thousand ADSL lines, of which 161 were attributable to our ADSL retail business (which is operated by PTM.com), and 4,037 PSTN/ISDN lines, of which 79.2% were residential/small office home office clients, 15.2% business and the remainder mainly payphones, wholesale lines and other.

The following table shows the number of our main lines by category.

	As of December 31,				
	1999	2000	2001	2002	2003
Fixed line main lines in service (thousands)					
Traditional main lines	3,753	3,650	3,501	3,317	3,224
ISDN main line equivalents	477	653	800	826	813
ADSL	0	0	3	53	188
Total	4,230	4,303	4,304	4,196	4,225
PSTN/ISDN fixed line main lines per 100 inhabitants					
	41.5	41.9	42.3	41.9	41.2
Public pay phones (thousands)	42.5	44.6	45.5	43.8	41.4

Over past years, PT Comunicações has made significant investments to meet subscriber demand for lines and to modernize our fixed line network. As a result, the number of PSTN/ISDN lines per 100 inhabitants almost doubled from 20.9 fixed line main lines at the end of 1989 to approximately 41.2 fixed line main lines at the end of 2003.

In September 1999, the number of active mobile cards (the mobile equivalent of main lines) overtook the number of fixed line main lines in Portugal, and traffic that once was transmitted in whole or in part on our fixed line network is being carried on our mobile network or on the network of other mobile operators. We are addressing this trend by encouraging increased use of our fixed line network for other data services.

During 2003, PT Comunicações focused its attention on attracting new wireline customers through a campaign entitled "Rediscover the Fixed Business". PT Comunicações offered its wireline customers a large portfolio of modern and innovative products and services.

All of our local switches in Portugal have been digital since 1999. Digital technology is used on all long distance and trunk connections. This level of digitalization of our fixed line network permits us to market and provide network-based value-added services, such as call waiting, call forwarding and voice mail, resulting in increased line usage. By the end of December 2003, PT Comunicações was providing approximately 1,042,713 voicemail boxes.

Our fixed line network includes ISDN lines, which transmit voice and data at higher rates than analog lines. We, through PT Comunicações, have offered ISDN services commercially since 1994. PT Comunicações offers a basic-rate service, which provides two communications channels. It also offers a primary-rate service which provides up to 30 communications channels. At the end of December 2003, PT Comunicações had 272,700 subscribers to the basic-rate ISDN service and 8,973 subscribers to the primary-rate ISDN service.

The following chart sets forth the number of ISDN equivalent main lines at the end of each of the last five years:

ISDN Lines

By the end of 2003, ISDN lines represented 20.1% our total equivalent fixed line main lines, as compared with 19.9% one year before. The conversion of traditional main lines to ISDN lines results in increased quality of service, and PT Comunicações' ISDN subscribers tend to produce higher levels of usage per line than traditional main line subscribers.

We, through PT Comunicações, have started to deploy higher-speed ADSL lines. PT Comunicações launched ADSL service on a wholesale basis in Lisbon and Oporto in 2002, covering 98.9% and 99.2% of those cities, respectively. Throughout the remainder of 2002, ADSL services were made available in the rest of Portugal, increasing total coverage throughout Portugal to 84.7% at the end of 2003. In addition, through PTM.com we launched a plug & play solution ADSL service in the third quarter of 2002, targeting residential customers, and a tailor-made service developed for small office home office and small and medium-sized enterprise customers.

PT Comunicações had 0.2 billing complaints per 1,000 bills and 10.1 reported faults per 100 main lines in the year ended December 31, 2003. The percentage of faults repaired in less than 12 working hours was 74.5% in the year ended December 31, 2003, compared with 88.1% in 2002. PT Comunicações offers residential customers detailed billing on request without extra charge.

Traffic. During the five-year period from 1999 through 2003, total traffic originating on the network increased by an average of 0.3% per year, although 2002 was the first year in which it

decreased. The chart below sets forth the rate of growth or decrease of traffic originated on our fixed line network.

Total Growth of Originated Traffic

The following table shows the breakdown of fixed line traffic originated on our fixed line network among mobile, Internet and data and other domestic and international traffic for the periods indicated.

Year ended December 31,

	1999		2000		2001		2002		2003	
	Millions of minutes	(%)	Millions of minutes	(%)	Millions of minutes	(%)	Millions of minutes	(%)	Millions of minutes	(%)
Domestic	9,972	69.4	8,933	53.7	7,431	43.0	6,480	39.6	5,841	40.1
International	410	2.8	413	2.5	411	2.4	402	2.5	382	2.6
Fixed-to-Mobile	1,083	7.5	1,290	7.8	1,215	7.0	1,119	6.8	1,023	7.0
Internet	2,800	19.5	5,630	33.8	6,920	40.0	6,581	40.3	5,023	34.5
Other	114	0.8	379	2.2	1,319	7.6	1,758	10.8	2,294	15.8
Total	14,379	100.0	16,645	100.0	17,296	100.0	16,340	100.0	14,563	100.0

During 2003, Internet-related traffic accounted for approximately 34% of the total traffic originated on the fixed line network compared with 40% during 2002. According to an administrative decision by ANACOM, the Portuguese telecommunications regulator, of February 21, 2001, PT Comunicações changed its billing structure for Internet service. This billing regime accommodates two different types of billing arrangements. Under the first method, ISPs pay a call origination charge to PT Comunicações, and, if the ISPs request that PT Comunicações invoice customers on their behalf, they pay PT Comunicações the correspondent invoicing charge. Under the second method of billing, PT Comunicações charges the ISPs a wholesale flat rate and the ISPs bill their own customers. On March 16, 2004, ANACOM issued a new administrative decision regarding the billing structure for Internet service. As a result, the billing arrangements between PT Comunicações and ISPs are now ruled by two different billing regimes. The primary differences between the two billing regimes relate to origination prices, the manner in which ISP infrastructures are connected to PT Comunicações' wireline network and billing arrangements. The regime introduced in March 2004 has lower origination charges, involves the use of leased lines and does not require PT Comunicações to maintain billing arrangements with ISPs. The ISPs determine which billing regime will apply to their billing arrangements with PT Comunicações. For additional information, see "Regulation Interconnection Internet Access" and "Item 5 Operating and Financial Review and Prospects Overview Internet Interconnection Charges".

PT Comunicações is required to provide carrier selection to its customers on all kinds of traffic. See " *Regulation Portugal Number Portability and Carrier Selection*". Carrier selection, excluding non-geographical services, such as number translation services, has not yet resulted in large-scale reduction in its traffic.

Except for customer pre-selection and Internet traffic, PT Comunicações accounts for traffic originating on our network in its fixed line telephone services unit. Traffic originating on other networks but terminating on our network is allocated to its wholesale unit. Until the fourth quarter of 2000, PT Comunicações did not own traffic that originated on its network and terminated on mobile networks. It collected the revenues for such traffic and transferred them to the mobile network operators which then repaid PT Comunicações the amount allocable to the fixed line portion of the call under its interconnection agreements. This repayment was accounted for by PT Comunicações as wholesale revenues. Since October 1, 2000, PT Comunicações owns this traffic. As a result, PT Comunicações bills its customers for fixed-to-mobile traffic, while mobile operators charge PT Comunicações for call termination. PT Comunicações allocates the revenue billed to customers to its fixed line telephone retail service revenue. As a result of this change, PT Comunicações' absolute margins have not changed, but its percentage margins decreased. See " *Wholesale Traffic*", below.

Marketing. Our wireline business, through PT Comunicações, is increasing marketing efforts towards customer loyalty and promoting increased usage of our wireline telephone services.

Promotional Efforts and Market Analysis. PT Comunicações has increased its promotional and marketing campaigns. It wants the public, and particularly its customers, to recognize that it provides better service and more attractive billing packages than its competitors. PT Comunicações is aggressively promoting the sale of products and services targeted to specific customers, in line with its "resegmentation of customers" policy implemented in 2003, through:

the promotion of a special pricing package named "PT Preços para Si" addressed both to the residential and business markets, which sold more than 550,000 packages since its launch in April 2003 through the end of 2003, exceeding expectations;

the launch of a campaign to exchange old equipment for updated equipment, allowing access to new facilities and increasing traffic;

the launch of "ADSL network PT" to wholesale ISPs. During 2003, total ADSL lines grew 257% and represented 4.7% of PT Comunicações' fixed line main lines, compared to 1.3% in 2002; and

the launch and promotion of innovative products and services and special pricing packages, such as "SMS for fixed network", "Concept Juris" designed for lawyers, "Concept Hotel" providing high-speed Internet access to hotel customers, and "Concept Business", "PT 1a Vez", "Portugal 15", "Night and Week End", "Hello Card PT" and "Telecom Card PT" addressed both to the residential and business markets and designed to promote domestic and international traffic.

Internet customers can also profit from special programs created by PT Comunicações that provide special conditions for access and use of PT Comunicações' network. PT Comunicações also sells higher-speed Internet access, including ADSL services, to take advantage of the growing use of Internet services in Portugal and of the group's various Internet-related services.

PT Comunicações uses market research programs to evaluate customer satisfaction and service quality and to help develop products. PT Comunicações focuses its marketing on different segments of its residential and business market. It has a state-of-the-art billing and customer information system and a marketing information database that combines usage and other data.

Targeted Subscriber Packages. PT Comunicações has targeted its products and pricing packages to specific segments of the retail market, such as family groups and small and medium-sized enterprises.

Customer Care. To provide support and marketing services to its residential and business customers, PT Comunicações has developed a network of regional organizations and retail service centers. In addition, it has separate call centers dedicated to increasing services to its residential and business customers. The call centers are interconnected and cover the whole country. This system allows PT Comunicações' customer service representatives to access the history of customers' telephone use and commercial dealings with PT Comunicações.

Increased Selling Efforts. PT Comunicações has developed its distribution network through its retail service centers and agents such as supermarkets and other retail outlets. Its customer support system enables it to develop strategies to sell new and expanded services to its customers. In addition, PT Comunicações is expanding its telemarketing activities, addressing both residential and small and medium-sized enterprise marketing segments and developing more proactive and closer relationships with its customers.

Retail

Fixed Line Telephone Services. Our group's largest business is providing public fixed line telephone services in Portugal to retail customers, primarily through our subsidiary PT Comunicações. This business area provided €1,324.4 million, €1,411.6 million and €1,624.7 million to our consolidated operating revenues during 2003, 2002, and 2001, respectively. We distinguish between two principal sources of revenue in the provision of fixed telephone services:

Fixed charges, including network access charges based on a monthly line rental and an initial installation fee; and

Traffic, including charges for the use of our fixed line network based on rates dependent on amount and type of usage.

We divide traffic into domestic and international traffic. Domestic traffic includes domestic telephone services provided by PT Comunicações directly to subscribers that originate or terminate calls on our fixed line network. International traffic includes international telephone services provided by PT Comunicações directly to users that originate calls on our fixed line network.

Since January 1, 2000, public switched fixed line telephone services in Portugal have been fully open to competition. As a result of the introduction of competition, combined with the substitution of mobile for fixed-line services, we have experienced, and may continue to experience, increased erosion of market share of both access lines and of outgoing domestic and international traffic. See "*Competition Competition Facing Our Wireline Business*".

Fixed Charges. PT Comunicações' fixed charges to domestic fixed line telephone subscribers include a one-time installation charge and a monthly line rental fee. These fixed charges provided €647.5 million, €629.1 million and €638.7 million to our consolidated operating revenues during 2003, 2002, and 2001, respectively.

As of December 31, 2003, the installation charge to our subscribers was €71.83. The standard line rental fee is €12.3 per month for standard lines and €24.5 per month for ISDN basic lines, in each case excluding value-added tax.

The chart below illustrates changes in PT Comunicações' prices and fees from 1999 through 2003. All prices are in Euros and exclude VAT.

Fixed Fees for Fixed Line Telephone Services(1)

	As at December 31,				
	1999	2000(2)	2001	2002	2003
Installation fee	79.94	77.69	74.41	71.83	71.83
Line rental per month	11.66	12.08	12.27	11.85	12.3

(1) Amounts rounded to nearest hundredth.

Traffic. Traffic contributed €676.9 million, €782.5 million and €986.0 million to our consolidated operating revenues during 2003, 2002, and 2001, respectively. Measured in minutes, total fixed line retail traffic originating on our fixed line network decreased by 3.5% during 2003, compared with 2002. The decrease was primarily due to the effects of mobile substitution, the migration of heavy dial-up Internet users to ADSL and a more challenging economic environment.

Domestic. PT Comunicações estimates that domestic traffic generated operating revenues of €570.5 million in 2003, €662.7 million in 2002 and €862.8 million in 2001.

Prices In 1999, PT Comunicações' charging system for traffic was based on a fixed line price pulse. On January 1, 2000, PT Comunicações introduced a system for charging its customers on a per-second basis, after a time credit included in the initial call price. PT Comunicações has three domestic tariffs: local, regional and national. Between the end of 1999 and the end of 2003, weighted average prices for domestic fixed line telephone services decreased by 1.9% per year in nominal terms. Compared with 2002, over the course of 2003, domestic prices decreased a further 0.27% in nominal and annual terms. See " *Regulation Portugal Pricing of Wireline Services*".

The chart below illustrates changes in PT Comunicações' prices from 1999 through 2003. The call prices from 1999 through 2003 are for a three-minute call at peak rates in 2003 constant prices. All prices are in Euros and exclude VAT.

Principal Prices for Domestic Fixed Line Telephone Services(1)

	As at December 31,				
	1999	2000(2)	2001	2002	2003
Local call prices	0.10	0.13	0.12	0.12	0.12
Regional call prices	0.31	0.31	0.24	0.23	0.21
National call prices	0.66	0.42	0.35	0.33	0.29

(1) Amounts rounded to nearest hundredth.

(2) For a three-minute call the prices are greater in 2000 than in 1999 due to per-second pricing introduced in 2000.

Prices for local, regional and national calls did not change in 2003. The average annual reduction in 2003 for the basket of prices was about 1.2% in nominal terms. PT Comunicações' pricing structure has come more into line with pricing structures in the rest of the EU over the last nine years. The following table compares our estimates of average domestic services prices per minute, excluding VAT,

for a three-minute call at peak rates in the EU with average prices in Portugal in effect at December 31, 2003.

Principal Prices for Domestic Fixed Line Telephone Services: EU and Portugal

	As of December 31, 2003	
	EU Average	Portugal
Local call prices	0.12	0.12
Regional call prices	0.18	0.21
National call prices	0.21	0.29

To increase its price competitiveness, PT Comunicações is promoting innovative differentiated pricing plans for market segments. For example, it offers various plans specially designed for business customers as well as other plans for residential customers. PT Comunicações also offers a prepaid card and pricing plans suited for Internet users, as well as plans aimed at the development of education and the information society.

International. PT Comunicações estimates that operating revenues from international fixed line telephone services were €106.5 million in 2003 compared with €119.8 million in 2002 and €123.2 million in 2001. Revenues from international fixed line telephone services come primarily from charges to its individual and business subscribers in Portugal for outgoing calls. PT Comunicações must pay a portion of these charges to other international operators whose facilities carry the calls. In 2003, 2002 and in 2001, PT Comunicações' revenues from international fixed line telephone services decreased while international traffic continued to grow. This decrease in revenues resulted from decreases in international accounting rates and decreases in prices for outgoing international calls. PT Comunicações expects these decreases to continue.

Accounting RatesHistorically, the amount of incoming traffic has been significantly greater than the amount of outgoing traffic. As a result of this imbalance, PT Comunicações receives higher payments from other international telecommunications operators than it pays out to these operators. PT Comunicações negotiates the amount of the payments with these operators periodically.

In recent years, the accounting rates among operators have been declining steadily, both for incoming and outgoing traffic. PT Comunicações estimates, however, that, on an aggregate basis in Euros, termination rates for international traffic at the end of 2003 decreased by a weighted average of approximately 9% for incoming traffic and decreased by 10% for outgoing traffic as compared to the end of 2002.

With the opening of the Portuguese market to competition on January 1, 2000, international telecommunications operators are now able to provide services directly in Portugal. They can lease lines from PT Comunicações or obtain international lines from other operators and then interconnect with our fixed line network. The revenues PT Comunicações receives from such services are interconnection fees and thus fall into the wholesale business category of our wireline business. As a result, while PT Comunicações' share of the international market has declined, increases in our wholesale business have, to a substantial extent, offset this decline.

PricesPT Comunicações sets traffic charges for international fixed line telephone services in a number of different groups of countries. Within each group, it charges different prices according to the time of day and the day of the week that the customer makes the call.

Between the end of 1999 and the end of 2003, PT Comunicações experienced aggregate reductions in real terms of 39% in international traffic. These included an average reduction in nominal terms of 3.4% for international calls over the course of 2003.

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The table below shows changes in prices for our international fixed line telephone services to selected destinations since 1999. The prices for 1999 through 2003 are peak rate prices per minute on the basis of a three minute call, set at 2002 constant prices. They are in Euros and exclude VAT.

Selected Prices for the International Services(1)

	As of December 31,				
	1999	2000	2001	2002	2003
EU(2)	0.38	0.29	0.28	0.27	0.27
Other European countries(3)	0.70	0.67	0.63	0.61	0.61
United States	0.38	0.30	0.29	0.28	0.28
Canada	0.39	0.30	0.29	0.28	0.28
Brazil	0.70	0.67	0.59	0.57	0.57

- (1) Euro amounts rounded to nearest hundredth.
- (2) Including Switzerland.
- (3) Excluding Norway and Iceland.

ADSL Services and ISPs. Through Telepac, PTM.com's ISP, PTM.com is the leader in providing Internet access in Portugal. By December 31, 2003, Telepac had approximately 1.5 million access subscribers in Portugal. This was an overall increase of 59% over one year before. We estimate that 30% of Portuguese Internet traffic in minutes was connected through Telepac during 2003. Telepac offers dial-up paid and free Internet access services. We estimate that altogether Telepac provided Internet access to about 20% of the Portuguese subscriber market at December 31, 2003. The number of hours of subscriber use in 2003 decreased by 30% to 23 million hours compared to 33 million hours in 2002, reflecting the increasing penetration of broadband, soft cable and ADSL in Portugal.

Application Service Provider (ASP). Telepac also provides ASP services in Portugal. These activities include remote applications services, web hosting and web design services to small and medium-sized enterprises. Telepac had approximately 3,072 thousand customers for its ASP business at December 31, 2003.

ISP Traffic Revenues. PTM.com provides its Internet services in cooperation with our other companies in the Portugal Telecom group. It offers Internet access through the lines of our fixed line network. Until June 1, 2001, in accordance with regulation of ANACOM, PTM.com recovered 35% of the revenues from the fixed line traffic from PT Comunicações, which retained 65% of such revenues. From September 2001, PTM.com retains all of the revenues from Internet traffic and pays PT Comunicações for use of the fixed line network. See "Item 5 Operating and Financial Review and Prospects Overview Internet Interconnection Charges".

Wholesale

Our wireline business' wholesale services, which are provided primarily through PT Comunicações, consist of:

domestic and international interconnection telephone services that we provide to other telecommunications service providers in Portugal, including other companies in our group;

leasing of Portuguese and international lines to other telecommunications service providers and Portuguese cable television operators, including other companies in our group;

transmission of television and radio signals for major broadcast television companies in Portugal; and

Internet interconnection services, which we began to provide to ISPs in Portugal in June 2001.

Consolidated operating revenues from wholesale services provided to companies outside our group were €315.1 million in 2003, €371.5 million in 2002 and €356.2 million in 2001.

Traffic. Interconnection traffic comprises about 58.8% of our wholesale business in terms of revenues. The service providers who purchase interconnection services include mobile telephone network operators, data communications providers, Internet service providers, value-added service providers and service providers whose international calls are terminated on or carried by PT Comunicações. Providing interconnection services means allowing third parties to connect their networks to our network, and vice versa. This interconnection is necessary, for example, to allow calls or data signals that originate on another network to terminate on our network, and vice versa. Since the introduction of full competition into the Portuguese telecommunications market on January 1, 2000, we, through PT Comunicações, have begun to provide interconnection telephone services to 11 other operators of public switched voice telephone networks, although traffic volume has been low. PT Comunicações has interconnection rates for call termination, call origination, transits and international interconnection. At this time, interconnection rates per minute for call termination include local transit rates equal to €0.775, single transit rates equal to €1.115 and double transit rates equal to €1.409, each based on a three-minute call made during peak hours. PT Comunicações also classifies value-added services, including audio text services, on an interconnection basis. PT Comunicações published the latest version of its reference offer for unbundled access to our local loops on September 15, 2003, and since then has made available to its competitors, where technical and space conditions are available, all of the local switches, 59 of which are co-located. See "*Regulation Portugal Unbundling of the Local Loop*" and "*Regulation Portugal Number Portability and Carrier Selection*".

On February 21, 2001, ANACOM issued an administrative decision instructing PT Comunicações to submit a reference Internet access offer proposal changing its billing structure for the connection of ISPs to our fixed line network from a model based on revenue sharing to one based on call origination charges and establishing maximum prices that PT Comunicações is permitted to charge ISPs for Internet access service. PT Comunicações published such a proposal on March 1, 2001. As discussed below in "*Item 8 Financial Information Legal Proceedings*," PT Comunicações has submitted a claim to the Lisbon administrative court requesting relief from this decision and contesting its legality. See also "*Regulation Portugal Interconnection Internet Access*".

Wholesale services traffic is generated by the interconnection portion of our wholesale business. Its revenues from leased lines and television signal transmission do not depend on traffic levels. Domestic traffic generated by our wireline business' wholesale interconnection services decreased by 12.9% in 2003 compared with 2002. This decrease was primarily due to a decrease in Internet traffic, which was partially compensated for by increases in indirect access traffic. The following table sets forth the total

amount of wholesale services domestic traffic on our fixed line network during the period 1999 through 2003.

**Wholesale Services Domestic Traffic
(millions of minutes)**

	Year ended December 31,				
	1999	2000	2001	2002	2003
Mobile	1,192	1,172	1,061	998	959
Internet	2,800	5,630	6,916	6,581	5,023
International	N/A	1,138	1,343	1,420	1,318
Other	114	594	2,336	2,831	3,008
Total	4,106	8,534	11,656	11,830	10,308

The traffic figures for mobile include fixed-to-mobile, mobile-to-fixed and mobile-to-mobile traffic between different networks. Since October 1, 2000, fixed-to-mobile traffic has been allocated to PT Comunicações' fixed line telephone services revenues instead of PT Comunicações' wholesale business revenues. The data presented for previous years was adjusted in accordance with this allocation. See "Retail Fixed Line Telephone Services Traffic", above.

We estimate that international wholesale mobile traffic accounted for approximately 46.2% of the Portugal Telecom group's total outgoing international traffic and approximately 36.4% of total incoming international traffic in 2003. We estimate that, in 2002, these percentages were approximately 43% and 37%, respectively.

Leased Lines. We, through PT Comunicações, lease lines to other telecommunications providers for mobile and data communications services, including our other subsidiaries and competitors. Since 1996, PT Comunicações has leased lines to resellers who offer voice services to corporate networks and closed user groups. Leased line services involve making a permanent point-to-point connection for voice and data traffic between two geographically separate points.

PT Comunicações' Concession requires it to provide leased lines to third parties. ANACOM defined a minimum set of leased lines as including 2-wire and 4-wire traditional lines and 64 kbit/s to 34 Mbit/s digital lines. PT Comunicações is also providing higher capacity 140 Mbit/s and above digital lines to third parties in Portugal.

The three current mobile telephone operators in Portugal, which include our subsidiary TMN, Vodafone Portugal and Optimus, are among our wireline business' largest leased line customers. PT Comunicações leases lines to TMN and TV Cabo on a basis that does not discriminate against other customers.

Prices. The net prices and fees PT Comunicações receives from providing access to our fixed line network on a wholesale basis are less per minute than those it charges for domestic and international fixed line telephone services. PT Comunicações has entered into a variety of different pricing arrangements for providing access to our fixed line network. PT Comunicações usually negotiates the amount of these prices with the service provider. The prices usually include a negotiated volume-based discount.

Domestic interconnection revenue per minute for calls terminated on our network declined by 19% in nominal terms in 2003 compared with 2002. International interconnection revenue per minute declined by 9% in nominal terms in 2003 compared with 2002. In accordance with EU and Portuguese regulation, PT Comunicações' interconnection prices are cost-oriented and non-discriminatory.

Since December 31, 2000, there have been no restrictions on leased line pricing, and PT Comunicações is able to negotiate freely prices for leased lines. See " *Regulation Portugal Pricing of Wireline Services*". PT Comunicações does not discriminate on prices between retail customers and customers that provide services to other providers, such as data network service providers and Internet service providers, although we do offer discounts according to the usage of the customer.

Data and Corporate

Our data and corporate services, within our wireline business, are provided by PT Prime to corporate customers that have a need for complex telecommunications solutions, with a focus on the top 6,500 companies in Portugal. It offers those customers data and business solutions, such as:

low speed data communications

digital leased lines

broadband data

networking and systems integration solutions

Internet-related services and applications including Intranet and Extranet services

interactive systems and related applications

outsourcing of telecommunications application systems

consultancy services

Web design and site management

fixed line and mobile convergence services

business-to-business e-commerce

housing and hosting solutions, including application service provider, or ASP, and enterprise resource planning, or ERP

telephone services using Internet protocol

PT Prime is the leading supplier of the full range of these services in Portugal. Data and corporate operating revenues amounted to €226.7 million in 2003, €225.9 million in 2002 and €201.7 million in 2001.

Services. PT Prime is one of the focal points for our group's interface with business customers in Portugal for our data, Internet, fixed line and mobile services. PT Prime has developed a full range of telecommunications services, and it integrates these services, as well as other services within the group, such as fixed line services and domestic mobile services, to provide its customers with packaged groups of services. In addition, PT Prime has its own license to provide a full range of telecommunications and related services in Portugal. By combining its communications capabilities with its software-based integrated systems and applications, PT Prime can offer integrated voice, data and image solutions, virtual private networks, convergence solutions, consultancy and outsourcing on a single commercial interface. We believe that PT Prime is the main service provider in Portugal capable of offering customers a full range of integrated and customized services rather than stand-alone services. Despite increasing competition, overall demand for data and corporate services has been increasing. As a result of competition, PT Prime has reduced its prices for leased lines and data services.

PT Prime is able to respond to the changing needs of its customers as quickly as new entrants in the Portuguese market do and to pursue and form strategic partnerships to take advantage of opportunities in domestic and international markets. It offers its services in partnership with leading operators and service providers such as British Telecom, Telefónica, Equant and Infonet. It uses systems and networks in partnership with Siemens, Alcatel, Cisco Systems, Newbridge, Motorola, Nortel Networks, Matra/EADS Telecom and IBM.

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PT Prime leases lines and broadband capacity to large businesses for data communications and other private uses and provides related services. It also provides integrated voice and data services to corporate customers. It offers X.25/X.32 synchronous services and X.28 asynchronous services and other switched and non-switched data communications services, such as frame relay, virtual private networks over IP for data communications, broadband services, security/firewall services and VSAT satellite communications services. In addition, it offers a new range of data, voice and Internet services,

such as Intranet, Extranet and managed services, including "voice over IP". It is using IP-based solutions to improve interconnections between companies and their employees and between customers and commercial partners through remote access, and exploring virtual private network capabilities. These solutions enable customers to integrate voice, video and data services in a flexible cost-effective manner with add-on capacity. The offering of web contact centers solutions represents an evolution of the classic call center for customers.

PT Prime provides a range of broadband solutions. The type of solution depends on the type (voice, data or image), volume, priority level and stability of information flow required by its customers.

PT Prime also provides reporting services targeted to special customers to control service level agreements and the overall performance of the network.

In addition, PT Prime is outsourcing corporate networks and services for our group's customers. For example, PT Prime operates and manages the SIBS network as well as the corporate networks of its strategic partners, Caixa Geral de Depósitos and Banco Espírito Santo. Consequently, PT Prime has developed substantial experience structuring and managing the network infrastructures of major Portuguese financial institutions. PT Prime delivers international seamless services aimed at multinational customers in association with Telefónica, British Telecom, Infonet and Equant.

PT Prime has entered into a partnership with Casa da Moeda, CTT and SIBS to create a company called Multicert, with PT Prime, Casa da Moeda and CTT each holding a 20% stake and SIBS holding the remaining 40%, which intends to provide digital certificates and communications security services to both consumer and business segments.

Networks. PT Prime network services use their own switched and access points in customer premises and their own network and lines leased from our fixed line network. PT Prime provides its services over the largest IP backbone in Portugal, leasing the necessary fixed line capacity from PT Comunicações. It has points of presence in all major cities throughout Portugal. This broadband data transmission network provides high capacity, flexibility and security. It can progressively incorporate current voice and data infrastructures at lower costs than alternative networks. PT Prime also provides high speed Internet access through asymmetric digital subscriber lines, known as ADSL. The ADSL lines are linked to digital subscriber line access multiplexes, or DSLAMs, located at fixed line network switching centers. PT Prime leases the necessary fixed line capacity from PT Comunicações. PT Prime supplies full IP and broadband connectivity for our whole group.

Revenues from services that offer leased lines of PT Comunicações are typically divided between PT Prime's own direct billings to its customers and our leased line revenues from our wholesale business. Revenues from our group's fixed line voice services for corporate customers are not reflected directly in PT Prime's revenues. PT Prime obtains fixed line voice services from PT Comunicações. Because PT Prime is integrating the services of other companies in the group, such as PT Comunicações and TMN, it receives agency fees for arranging and selling these services which are cancelled out in the group's financial consolidation process. In 2003, these agency fees amounted to approximately €8.8 million.

Systems Integration. PT Prime offers an integrated range of telecommunications and information technology services to the business market. PT Prime's goal is to service all of its customers' telecommunications needs and to leverage the traditional offering of products and services from our group.

PT Prime has a strong and competitive position in the development of information technology solutions where communications are an integral part of the services provided. To reinforce its position as a leader in this area, PT Prime is pursuing a partnership strategy with the main information technology suppliers in the market, particularly software and hardware providers. PT Prime is also

exploring synergies arising from its relationship with our subsidiary PT Sistemas de Informação, the information technology arm of our group.

To support these new services and to respond to the increasing demand of e-business integrators, PT Prime developed a corporate Internet Data Center. This facility allows it to provide services, such as co-location, sophisticated web hosting, ISP services, data storage and ASP services. To develop, build up and manage the Internet Data Center, PT Prime has selected IBM Global Services, the world leader in this market segment, as its partner. Pursuant to the terms of an agreement between PT Prime and IBM, the Corporate Internet Data Center began to provide Internet hosting services for corporate customers in April 2001.

PT Prime also offers services focused on the integrated management of networks ranging from local area networks, or LANs, to software applications, including PC management.

Marketing and Customer Care. PT Prime is focusing significant resources on marketing and customer care. Over 300 of PT Prime's 509 employees are involved in marketing services directly to business customers. Account managers are being given clear incentives to meet and exceed sales targets. PT Prime is upgrading its sophisticated customer relationship management platform, or CRM, to increase focus on market and Internet efficiency.

PT Prime is seeking to compete in Portugal on the basis of the quality of its services as well as its position as the leading supplier of integrated telecommunications and IT services. PT Prime is pricing its various service offerings on the basis of the volume of traffic, the duration of service agreements and the scope of the services offered to each customer.

PT Prime offers its customers services available from other companies in our group. Our subsidiary PTM.com, for example, provides significant support for product development and the marketing of Internet access and web hosting services for small and medium-sized enterprises. PT Prime offers mobile telephone services options for corporate accounts while our subsidiary TMN also maintains its own direct relationships with this important customer segment.

PT Prime uses customer care capabilities that were developed for PT Comunicações. To maximize customer loyalty, PT Prime is developing systems that provide integrated assessments of customer profiles, based on a CRM system. We believe that to reinforce its competitiveness, PT Prime must change and optimize its processes and focus the entire organization on its customers more effectively.

Other Wireline Services

Other wireline services include primarily our directories business and sales of telecommunications equipment.

Directories. Operating revenues from our directories business amounted to €136.1 million in 2003, €139.1 million in 2002 and €136.8 million in 2001. We subcontract to Páginas Amarelas (an associated company 25% owned by us) for the publication and distribution of telephone directories throughout Portugal in return for an annual payment of approximately 64% of its gross revenues from the sale of advertising space. Currently, the provision of yellow page directory services is not subject to significant competition.

Sales of Telecommunications Equipment. Revenues from sales of telecommunications equipment amounted to €36.8 million in 2003, €34.8 million in 2002 and €43.0 million in 2001, including the sale of handsets, modems and other telecommunications equipment.

Domestic Mobile Business

TMN, our Portuguese mobile operating company, is the leading provider of mobile voice, data and Internet services in Portugal in terms of the number of active mobile telephone cards connected to its network and by revenues, margins and profits.

Operating revenues from TMN amounted to €1,346.7 million in 2003, €1,266.6 million in 2002, and €1,171.9 million in 2001. Mobile services have undergone extraordinary growth in recent years in Portugal. At December 31, 2003, there were approximately 89.8 active mobile telephone cards per 100 Portuguese inhabitants. This was more than the number of wireline main lines per 100 Portuguese inhabitants at December 31, 2003, which was 40.3, according to ANACOM.

The table below provides statistical information relating to TMN.

	As of December 31,				
	1999	2000	2001	2002	2003
TMN Portugal					
Number of subscribers (thousands)	2,115	2,939	3,905	4,426	4,887
Subscribers growth per annum (%)	48	39	33	13	10
Number of subscribers per 100 inhabitants (including competitors' subscribers)	46.7	65.0	77.2	81.9	89.8
Estimated market share by number of subscribers (%) ⁽¹⁾	45.3	44.1	49.0	51.9	52.3
Churn rate (%) ⁽²⁾	28.3	26.1	23.5	25.3	23.5
Number of employees	930	1,019	1,194	1,192	1,109

(1) Source: ANACOM and TMN.

(2) TMN defines the "churn rate" as the percentage of TMN mobile subscribers that end their use of TMN's mobile services either by terminating their service or by changing their mobile handset and card number without terminating their existing TMN service. Generally, a pre-paid card can receive or send calls for a period of three months after the last recharge, depending upon the pre-paid service. After this period, if the card is not recharged, it can only receive calls for an additional three months. After this second three-month period, provided the pre-paid card receives one paid call over the course of the next month, then the pre-paid card is allowed to receive calls for an additional month. This will continue, as long as the pre-paid card continues to receive at least one paid call a month, for a maximum of six months. Once the card ceases to receive paid calls, or after the end of six months, it becomes non-active.

Services. TMN provides GSM mobile telephone services. GSM is a European and worldwide mobile telephone standard using digital technology. Through roaming agreements, TMN's subscribers can use GSM to make and receive mobile calls throughout Europe and in many other countries.

TMN provides GSM services in the 900 MHZ and 1800 MHZ band spectrums. TMN began to offer GSM 1800 services in May 1998 in addition to the GSM 900 service it already offered. TMN's strategy has been to use GSM 1800 services to offer an increased number of channels in high traffic density areas. Dual-band handsets, which select available channels from each frequency band, enable users to benefit from the wider range of available channels.

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TMN paid spectrum fees in 2001, 2002 and 2003 of €25 million, €29 million and €30 million, respectively, for the use of its 900 MHz and 1800 MHz GSM network.

During 2001, 2002 and 2003, TMN continued to introduce new products and services, such as:

"TMN Multi" and "TMN Familiar", which offer discount packages to groups;

WAP services, including "Bolsa on-line" (providing share price information), together with sapo.pt;

"MyTMN", personalized internet and data services which offer text messaging, WAP and voice-based services that can be customized by each subscriber;

"TMN Empresas", which was launched in the third quarter of 2001 and provides services for corporate customers, such as marketing and technical assistance services, in cooperation with our pme.link.pt portal;

the first SMS InterWorking agreement, an interconnection agreement (February 2002);

"DataXpress", a wireless data compressed transmission service using GPRS technology (April 2002);

opening of the second TMN Megastore, in Oporto, which sells products and services of TMN;

first public demonstration of mobile video telephony service, using a UMTS network (May 2002);

corporate solutions to small office home office customers in partnership with pme.link;

MMS services, or multimedia messages, which combine picture and sound (May 2002);

GPRS roaming service, launched in partnership with Telefónica (April 2002);

"Spik" products, a mobile phone with a competitive package of minutes;

"Roaming Zone", a roaming service package for post paid customers;

"Biz Office", a mobile office service launched in 2003;

"K" services, including "Kolmi", a service whereby prepaid customers may send a free message asking the receiver to call back, and "Karga", a service whereby prepaid customers may transfer credit from their mobile phones to other mobile phones;

"Key user" services, providing on-line phone card management for TMN customers;

"I9-Inove", a multimedia mobile portal that provides faster, cheaper and easier access to a wide range of services and content (June 2003); and

"Pakots SMS", a pre-paid SMS package, and "SMS Express", offering competitive tariffs to customers who have high levels of SMS usage.

TMN is also developing services in wireline to mobile convergence, such as a voicemail service, which allows mobile telephone users to retrieve voicemail messages from their fixed-line telephones through mobile telephone handsets with PT Comunicações. TMN also offers a range of Internet-access and multimedia services, such as Internet access service through WAP mobile handsets. This service, available to every TMN subscriber, including users of all prepaid services, allows subscribers to access the Internet through their handsets. In August 2001, TMN launched the "MyTMN" platform, offering personalized Internet and data services, enriched with content and services supplied by new partners. MyTMN allows users to customize a wide range of WAP, SMS and voice-based services. WAP customers can access webmail, agenda, stock exchange information, location-based services, easy messaging, on-line tickets and chat services. TMN invoices its customers for the use of TMN services

and remits to its partners a percentage of the total fees collected that corresponds to the content and services supplied by such partners.

MyTMN's new range of offerings has introduced new services such as Logos & Ring Tones (also polyphonic), Multimedia Messaging (including the ability to send to customers of other operators), Java Games and My Message 4u (a service that allows customers to personalize the welcome message or other voice messages with music, dedications or jokes). At MyTMN, customers can also create their own MMS Album, with holiday souvenirs, cards and similar items.

We expect data-service usage to grow considerably as customers become increasingly familiar with MyTMN, as service offerings are further expanded and as access speed is increased through the introduction of GPRS. We also expect higher data speeds to improve performance and the attractiveness of the MyTMN package of products, which we expect will result in a higher contribution of data services to overall revenues in the future.

In June 2003, TMN launched the multimedia portal I9-Inove, which optimizes the current capabilities of the GSM-GPRS systems to provide customers with faster, cheaper and easier access to a wide range of services and content, such as Java games; the three national free-to-air TV channels; messaging services; goals from the Portuguese football league in video (which is exclusive to TMN); TV Cabo's programming guide; and the Lusomundo cinema ticketing service, the first m-commerce service in Portugal. As of December 31, 2003, I9-Inove had reached 25,153 TMN customers.

TMN introduced its GPRS system at the end of 2000 in Lisbon and Oporto and launched it at the beginning of October 2001 in all other areas of Portugal. See "*Network and Capital Investment*". GPRS provides higher speed data communications than GSM networks. TMN expects the introduction of GPRS to improve its existing WAP services. In addition, GPRS allows TMN to provide "always on" connection to Internet services. To use this service, subscribers must purchase new mobile handsets that are able to carry GPRS services. TMN's allocation of such handsets has been sufficient to meet demand during the initial roll out of its GPRS service. TMN has made capital expenditures in building out its GPRS system of €10.9 million in 2000, €11.7 million in 2001, €5.5 million in 2002, and €0.3 million in 2003.

At the end of 2000, the Portuguese government opened a tender for four licenses for third generation mobile services, also known as universal mobile telecommunications services, or UMTS. TMN received one of these licenses and paid an up-front fee of €100 million. Licenses were also awarded to Oniway, a new entrant in the Portuguese mobile market, Vodafone Portugal and Optimus. However, subsequent to an agreement with the other three mobile operators in Portugal, including TMN, Oniway decided not to participate in the provision of third generation mobile services and as a result requested that the Portuguese government repeal the license granted to it in December 2000. The Portuguese government granted this request by ministerial order on January 13, 2003. The other three recipients of third generation licenses, including TMN, requested that the additional frequency that had been allocated to Oniway be reallocated to them. This request was granted by a special ministerial order in January 2003. See "*Regulation Portugal Third Generation Mobile Services Licenses*". Under the agreement entered into with Oniway referred to above, TMN, Vodafone Portugal and Optimus agreed to pay Oniway an amount of €33 million each for certain intangibles held by Oniway related to UMTS launch preparations upon the reallocation to them of the frequency that had been allocated to Oniway.

We expect the development of third generation services to require certain additional investments by TMN. TMN made direct investments of €12.4 million in 2001, €38 million in 2002 and €67.2 million in 2003 in building out its third generation network.

ANACOM reviewed the situation regarding the availability of handsets and related software for UMTS services during the third quarter of 2002 and initially postponed the mandatory initiation of third generation services for all holders of UMTS licenses until December 31, 2003. In February 2004,

ANACOM issued a decision requiring the initiation of third generation services in 2004. However, UMTS license holders will not be required to initiate UMTS services commercially until June 30, 2004. On April 19, 2004, TMN became the first mobile operator to launch UMTS in Portugal, with a service that allows customers to make video calls. The 3G handsets function both on GSM/GPRS and UMTS, allowing customers to use all the voice, multimedia and data services already offered by TMN. For data access exclusively, TMN also offers a 3G access card. TMN is providing initial UMTS coverage in Lisbon and Oporto, and plans to extend this coverage progressively to cover the whole of Portugal. We expect to be able to make further decision about the deployment of new services based on commercial grounds as well as on applicable ANACOM requirements.

Subscribers and Traffic. TMN is the market leader in mobile services in Portugal. At December 31, 2003, TMN had approximately 4.9 million subscribers, representing an increase of 10.4% from December 31, 2002. At December 31, 2003, TMN's subscribers represented 52.3% of the total mobile subscribers in Portugal. During 2002 and 2003, TMN also captured a greater proportion of the market increase in terms of net subscriber additions than its competitors, enabling it to maintain its position as the market leader. During 2003, TMN's share of new mobile subscribers (net additions) was 56.7%, according to ANACOM. Over the course of 2003, TMN's churn rate, which means the percentage of TMN mobile subscribers that ended their use of TMN's mobile services either by terminating their service or by changing their mobile handset and card number without terminating their existing TMN service, was 23.5%. TMN's churn rate was 25.3% in 2002.

In addition to the increase in the number of subscribers, mobile usage grew during 2003. TMN's voice traffic in terms of minutes grew by 5.3% to 6,752 billion minutes in 2003, compared to 6,413 billion minutes in 2002. Average monthly usage per subscriber decreased 5.7% to 123.1 minutes in 2003, compared to 130.5 minutes in 2002. Traffic from data transmission, such as SMS and GSM WAP services, increased by 13.5% and decreased by 15.9%, respectively, during 2003 in terms of number of calls. Traffic from GPRS WAP services increased by 1,386% in 2003. There was an average of 25.2 SMS messages per month per user in 2003, 1.7% more than the average of 24.8 SMS messages per month per user in 2002.

Prices and Revenue Breakdown. We believe that mobile services in Portugal are priced lower than the European average and are among the lowest in Europe. Mobile telephone charges are not regulated. Traffic charges, sales of handsets and connection and subscription fees represented approximately 88.3%, 9.1% and 2.6%, respectively, of TMN's revenues in 2003, and approximately 87.4%, 9.6% and 3.0%, respectively, of TMN's revenues in 2002. Since May 2003, monthly subscription fees range from €10.00 to €39.96, excluding VAT. TMN no longer charges an initial connection fee. TMN currently has many different price plans for its mobile telephone services.

Products and Marketing. TMN offers a variety of innovative subscriber-oriented products. It was the first operator in the world to offer pre-paid services. TMN's prepaid and discount products have been popular. We estimate that at the end of 2003, approximately 84.1% of its subscribers were using TMN's prepaid products. TMN has been expanding its subscriber base through increased advertising and the use of its own distribution network. TMN markets its services through more than 1,950 points of sale, including our group's and TMN's sales forces, Portugal Telecom retail shops, TMN shops, supermarket chains and independent dealers. TMN has been trying to encourage the use of mobile services more broadly in the middle and high end of the market and to increase subscriber retention in this market segment. By focusing on the business segment of the market, TMN experienced a 6.7% increase in the number of postpaid subscribers in 2003.

Network and Capital Investment. In recent years, TMN has made significant investments in base stations throughout Portugal for its GSM 900 and GSM 1800 services. As a result of its investments, TMN has a technologically advanced high capacity network that provides extensive coverage across Portugal. As of the end of 2003, TMN's digital network had 3,869 base stations, including 70 base stations added during 2003. These stations covered more than 95% of continental Portugal and 98% of

the Portuguese population. The addition of the GSM 1800 band has substantially increased TMN's network capacity in heavily used areas. By the end of December 2003, TMN had installed GSM 1800 technology in 771 base stations. TMN has offered GPRS services, which allow for "always on" data access, such as an Internet connection through a mobile handset, on its mobile network since it introduced such services at the end of 2000 in Lisbon and Oporto and October 2001 in all other areas of Portugal. TMN also is focusing on improving its indoor coverage in larger metropolitan areas. In 2002, TMN introduced MMS.

Roaming. Roaming agreements between operators allow their subscribers to make and receive voice calls automatically, send and receive data, or access other services when traveling outside the geographical coverage area of the home network, by using a visited network. As of the end of 2003, TMN had entered into roaming agreements with a total of 262 operators in 159 countries or regions. Since November 2000, it has been possible for Telesp Celular subscribers to use TMN's network in Portugal and TMN's roaming partners' networks. At the same time, TMN's subscribers can use Telesp Celular's network in Brazil and TCP's Brazilian roaming partners' networks, in each case with a handset and mobile telephone card that is compatible with the network. In April 2002, TMN entered into a GPRS roaming agreement with Telefónica.

Equipment Sales. TMN sells mobile phones and related equipment in Portugal. Equipment sales generated operating revenues of €133.5 million in 2003, €133.9 million in 2002 and €164.0 million in 2001.

Brazilian Mobile Business

Until recently, our mobile operations in Brazil, a country with a population of about 177 million people, had been active only in the states of São Paulo, Paraná and Santa Catarina. On January 23, 2001, we entered into a strategic agreement with Telefónica Móviles to aggregate all of our combined mobile assets in Brazil to the extent permitted under Brazilian law. The strategic agreement was approved by the European Commission on March 13, 2001. ANATEL advised us in May 2001 that the joint venture could be formed provided that neither we nor Telefónica Móviles could transfer to the mobile joint venture company more than 19.99% of the ordinary shares with voting rights of the mobile service companies controlled by each of us in Brazil. This limitation was applicable until such time as the mobile service companies to be contributed to the mobile joint venture company migrated from the former SMC mobile services licensing regime to the new SMP mobile services licensing regime. See "*Regulation Brazil*." On December 10, 2002, ANATEL formally approved the migration of our Brazilian mobile subsidiaries from the SMC regime to the SMP regime and the transfer of all of our direct and indirect interests in Brazilian mobile services companies to the mobile joint venture company.

On December 27, 2002, PT Móveis, which holds our interests in Brazilian mobile services companies, and Telefónica Móviles transferred their direct and indirect interests in Brazilian mobile services companies to the joint venture company, operating under the brand name Vivo. Portugal Telecom and Telefónica Móviles transferred to Vivo all their interests in:

TCP, which controls Telesp Celular (the band A operator in the state of São Paulo), Global Telecom (the band B operator in the states of Paraná and Santa Catarina) and Tele Centro Oeste Participações, S.A., or TCO (a band A operator in the Midwestern and Northern regions of Brazil), and was contributed by PT, which had a controlling position, and by Telefónica Móviles;

Tele Sudeste Celular Participações, S.A., which controls Telerj Celular, S.A. (the band A operator in the state of Rio de Janeiro) and Telest Celular, S.A. (the band A operator in the state of Espírito Santo), and was contributed by Telefónica Móviles;

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Tele Leste Celular Participações, S.A., which controls Telebahia Celular, S.A. (the band A operator in the state of Bahia) and Telerpipe Celular, S.A. (the band A operator in the state of Sergipe), and was contributed by Telefónica Móviles; and

Celular CRT Participações, S.A., which controls CRT Celular, S.A. (the band A operator in the state of Rio Grande de Sul), and was contributed by Telefónica Móviles (which had a controlling position) and by us.

Vivo is the leading mobile company in Brazil, based on a total of 20.7 million active mobile telephones at December 31, 2003. The joint venture operates in 20 states in Brazil, including the Federal district of Brasília, which provide more than 83% of Brazil's GDP. In its areas of operation, Vivo had an estimated market share of approximately 56.2% at the end of 2003. We believe that the joint venture will facilitate our ability to serve our Brazilian subscribers on a seamless basis throughout Brazil. We expect to benefit from synergies in various areas, including marketing, promotional activities, distribution networks, call center management, network management and operations, information technology, procurement and support functions, as well as the deployment of new mobile data services for business users. We believe that the joint venture will enable us to respond more effectively to increased competition from existing operators, such as Telecom Itália Mobiles, Telecom Americas, Oi and Brasil Telecom, and from other mobile operators in the markets we serve.

We have described the arrangements by which we and Telefónica Móviles own and manage the joint venture and related issues below in "*Strategic Alliances Alliance with Telefónica*". We have described certain regulatory restrictions applicable to Vivo and its subsidiaries which result from their relationship with Telefónica, including the inability of Vivo and its subsidiaries to provide wireline long distance services in Brazil, below in "*Regulation Brazil SMP Regulation*". See also "*Item 3 Key Information Risk Factors The Conditions Applying to Vivo's Subsidiaries Under the New SMP Licensing Regime may Result in Reducing Our Revenues and Results of Operations*".

Although we transferred all of our interests in mobile telecommunications companies in Brazil to Vivo on December 27, 2002, our consolidated statements of income and cash flows for the year ended December 31, 2002 continued to fully consolidate TCP's results. However, our balance sheet as of December 31, 2002 proportionally consolidates all the assets and liabilities of Vivo. Both our consolidated statements of income and cash flow for the year ended December 31, 2003 and our balance sheet as of December 31, 2003 proportionally consolidate the results of Vivo.

On December 27, 2002, TCP purchased the remaining 51% of the voting shares of Global Telecom. In our consolidated statements of income and cash flows for the year ended December 31, 2002, we continued to account for the results of operations of Global Telecom based on the equity method of accounting. However, TCP's balance sheet as of December 31, 2002, fully consolidates all the assets and liabilities of Global Telecom and accordingly our balance sheet proportionally consolidates all the assets and liabilities of Global Telecom. Both our consolidated statements of income and cash flows for the year ended December 31, 2003 and our balance sheet as of December 31, 2003 proportionally consolidate the results of Global Telecom. See "*TCP and Telesp Celular*", below.

On April 25, 2003, TCP acquired a controlling interest in TCO. As a result, TCO's assets and liabilities as of December 31, 2003 are reflected in our consolidated balance sheet as of December 31, 2003 through our proportional consolidation of Vivo, and TCO's income and cash flows from May through December 2003 are reflected in our consolidated statements of income and cash flows for the year ended December 31, 2003 through our proportional consolidation of Vivo's statements of income and cash flows. See "*TCP and Telesp Celular*" and "*Tele Centro Oeste Participações*" below.

The diagram below presents, in a simplified way, the ownership structure of Vivo:

*

These percentages correspond to the proportion of voting shares owned, directly or indirectly, by Vivo.

Regions. Vivo provides telecommunications services in Brazil through the following subsidiaries and in the regions described below:

Telesp Celular provides mobile telecommunications services on band A in the state of São Paulo, covering approximately 248,209 square kilometers, representing approximately 2.9% of Brazil's territory. This area includes more than 39.3 million people, representing 22.0% of Brazil's population, and 63 municipalities with populations in excess of 100,000, including the City of São Paulo, Brazil's largest city, with more than ten million people.

Global Telecom provides mobile telecommunications services on band B in the states of Paraná and Santa Catarina. This area is composed of 294,661 square kilometers, representing approximately 3.5% of Brazil's territory, with a population of approximately 15.6 million people, representing 8.8% of Brazil's population, and 22 municipalities with populations in excess of 100,000 people.

Tele Sudeste Celular provides mobile telecommunication services on band A in the states of Rio de Janeiro and Espírito Santo, covering 96% of the population of Vivo's authorization areas.

Tele Leste Celular provides mobile telecommunication services on band A in the states of Bahia and Sergipe, covering 68% of the population of Vivo's authorization areas.

CRT Celular provides mobile telecommunication services on band A in the state of Rio Grande do Sul, covering 96% of the population of Vivo's authorization areas.

TCO provides mobile telecommunications services in Brazil's Federal District and in 11 Brazilian states, including Acre, Goiás, Tocantins, Mato Grosso, Mato Grosso do Sul and Rondônia on band A and Pará, Amazonas, Amapá, Roraima, and Maranhão on band B. These areas are composed of 5.8 million kilometers and 31.8 million people, representing 68.0% of Brazil's territory and 18.0% of Brazil's population, and 34 municipalities with populations in excess of 100,000 people.

TCP and Telesp Celular

	<u>2001</u>	<u>2002</u>	<u>2003</u>
<i>Telesp Celular Operating information</i>			
Cellular lines in service at year-end (in thousands)	5,104	6,060	7,495
Customer growth during year	18.6%	18.7%	23.7%
Prepaid lines in service at year-end (in thousands)	3,735	4,634	6,019
Churn(1)	20%	17%	22%
Estimated population of authorization area at year-end (million)(2)	37.7	38.3	39.0
Estimated covered population at year-end (millions)(3)	36.7	37.2	38.4
Percentage of population covered(4)	97.3%	97.1%	98.4%
Penetration at year-end(5)	21.0%	23.8%	30.3%
<i>TCP Financial information(6)</i>			
Net operating revenues (in millions of Reais)	2,946.2	3,415.0	6,046.4
Net Income (loss)(in millions of Reais)	(1,113.6)	(1,140.8)	(640.2)
Total assets (in millions of Reais)	6,872.2	9,654.4	13,473.3

- (1) Churn is the number of customers that leave Telesp Celular during the year, calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the Instituto Brasileiro de Geografia e Estatística IBGE and Target 2002 "Brasil em Foco".
- (3) Number of people within the region that can access the cellular telecommunications signal.
- (4) Percentage of the population in the region that can access the cellular telecommunications signal.
- (5) Number of cellular lines in service in the region, including competitors, divided by the population of the region.
- (6) Data taken from TCP's consolidated financial statements prepared under Brazilian GAAP, which include (i) the results of Global Telecom for 2001 and 2002 recorded by the equity method of accounting and Global Telecom's income and cash flows for 2003 fully consolidated and (ii) TCO's income and cash flows from May through December 2003 fully consolidated.

Telesp Celular is part of our mobile joint venture with Telefónica and is 100% owned by TCP. Telesp Celular is the leading mobile telephone operator in the Brazilian state of São Paulo and in Brazil. São Paulo has a population of approximately 39 million people and is the most economically developed state in Brazil. The state of São Paulo contributes around 34.9% of Brazil's GDP. As of December 31, 2003, mobile penetration in the state of São Paulo was 30%, compared to an average of 28% in the rest of Brazil. Telesp Celular's operating revenues were R\$3,993.2 million in 2003, R\$3,415.0 in 2002 and R\$2,946.2 million in 2001.

On March 11, 2002, TCP announced its intention to undertake an overall capital increase of its common and preferred shares, including preferred shares underlying its ADSs. As part of this overall capital increase, TCP offered holders of its preferred shares rights to subscribe for new preferred shares, holders of its ADSs rights to subscribe for new ADSs and holders of its common shares rights to subscribe for new common shares. TCP successfully completed its rights offering in September 2002, which generated proceeds of R\$2,403 million.

Portugal Telecom subscribed to a total of 247,224 million common shares and 326,831 million preferred shares in this rights offering. As a result, as of September 2002, we owned 93.7% of TCP's common shares and 49.8% of TCP's preferred shares, representing an economic interest of 65.12%. In October 2002, in connection with the formation of the joint venture, we sold a 14.68% stake in TCP to

Telefónica Móviles, reducing our economic interest in TCP to 50.44%. On December 27, 2002, we transferred the rest of our interest in TCP to Vivo. We now hold our interest in TCP, as well as our interest in the other mobile services companies that were transferred to Vivo, indirectly, on a 50/50 basis with Telefónica Móviles.

In February and July 2001, TCP acquired an 81.61% indirect economic interest in Global Telecom, through the acquisition of 49% of the voting shares and 100% of the non-voting shares of each of three holding companies that controlled Global Telecom. The total purchase price was R\$902.6 million. On December 11, 2002, after all of the TCP operators had switched over to the new SMP regulatory licensing regime, ANATEL approved TCP's acquisition of the remainder of the shares and, on December 27, 2002, TCP acquired the remaining 51% of the voting shares of the three holding companies that owned Global Telecom for US\$82.0 million. TCP now owns 100% of the voting and non-voting shares of Global Telecom.

On April 25, 2003, TCP acquired 61.1% of TCO's voting capital stock from the Brazilian company, Fixcel. The purchase price was R\$1,529 million, which corresponded to R\$19.5 per each lot of 1,000 common shares acquired. On November 18, 2003, TCP acquired an additional 25.5% of the common shares of TCO in a tender offer to TCO minority shareholders for R\$538.8 million. Following the tender offer, TCP now holds 86.6% of the voting capital stock and 28.9% of the total capital stock of TCO, including treasury shares held by TCO. On October 31, 2003, TCP attempted to acquire the remaining share capital of TCO by means of a merger of TCO shares into TCP shares. The exchange ratio was fixed at 1.27 TCP shares for each TCO share held. This merger was cancelled on January 12, 2004 following the issuance of an opinion by the Brazilian Securities and Exchange Commission that the merger did not fully comply with current Brazilian law.

Global Telecom

	<u>2001</u>	<u>2002</u>	<u>2003</u>
Cellular lines in service at year-end (in thousands)	862	1,177	1,691
Customer growth during year	86%	36.5%	43.7%
Prepaid lines in service at year-end (in thousands)	539	924	1,409
Churn(1)	23%	20%	18%
Estimated population of authorization area at year-end (millions)(2)	15.1	15.3	15.6
Estimated covered population at year-end (millions)(3)	10.6	11.0	11.9
Percentage of population covered(4)	71%	74%	76%
Penetration at year-end(5)	17%	19%	24%
Net operating revenues (in millions of Reais)(6)	425.9	512.2	669.0
Net Income (in millions of Reais)(6)	(856.1)	(771.1)	(436.0)
Total assets (in millions of Reais)(6)	2,632.8	2,383.6	2,128.5

- (1) Churn is the number of customers that leave Global Telecom during the year, calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the Instituto Brasileiro de Geografia e Estatística IBGE and Target 2002 "Brasil em Foco".
- (3) Number of people within the region that can access the cellular telecommunications signal.
- (4) Percentage of the population in the region that can access the cellular telecommunications signal.
- (5) Number of cellular lines in service in the region, including competitors, divided by the population of the region.
- (6) Data taken from financial statements prepared under Brazilian GAAP.

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Under the terms of Global Telecom's authorization from ANATEL, it operates in the states of Paraná and Santa Catarina. These two states have a combined population of approximately 15.6 million and together generate approximately 10% of Brazil's gross domestic product. As of December 31, 2003, mobile phone penetration in Global Telecom's authorization areas was 24%, as compared with an average of 28% in the rest of Brazil. As of December 31, 2003, Global Telecom's service area reached more than 76% of the urban population of those areas and Global Telecom had 1,691,012 subscribers, representing an estimated market share of 45%, as compared to 41% at year end 2002. Global Telecom introduced pre-paid products in 2000 and made significant investments in 2001, 2002 and 2003 to expand the coverage of its network service, as well as to offer mobile data services with potential speeds of up to 14.4 kb per second.

Tele Sudeste Celular Participações

	<u>2001</u>	<u>2002</u>	<u>2003</u>
Cellular lines in service at year-end (in thousands)	3,028	3,455	3,709
Customer growth during year	21.0%	14.1%	7.4%
Prepaid lines in service at year-end (in thousands)	2,023.3	2,368.2	2,552
Churn(1)	17.9%	18.2%	29.5%
Estimated population of authorization area at year-end (millions)(2)	17.9	18.0	18.1
Estimated covered population at year-end (millions)(3)	15.3	15.8	17.4
Percentage of population covered(4)	85.9%	87.4%	96.0%
Penetration at year-end(5)	27.7%	32.7%	41.0%
Net operating revenues (in millions of Reais)(6)	1,703.3	1,847.6	1,892.5
Net Income (in millions of Reais)(6)	162.9	140.4	156.2
Total assets (in millions of Reais)(6)	2,690.6	2,793.8	2,823.4

- (1) Churn is the number of customers that leave Telerj Celular and Telest Celular, taken together, during the year, calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the Instituto Brasileiro de Geografia e Estatística IBGE and Target 2002 "Brasil em Foco".
- (3) Number of people within the region that can access the cellular telecommunications signal.
- (4) Percentage of the population in the region that can access the cellular telecommunications signal.
- (5) Number of cellular lines in service in the region, including competitors, divided by the population of the region.
- (6) Data taken from financial statements prepared under Brazilian GAAP.

Tele Sudeste Celular Participações, or Tele Sudeste, holds 100% of Telerj Celular, the leading mobile telephone operator in the state of Rio de Janeiro, and 100% of Telest Celular, the leading mobile operator in the state of Espírito Santo. These states have a combined population of approximately 18 million people and together contribute around 13.5% of Brazil's GDP. As of December 31, 2003, mobile penetration in Tele Sudeste's authorization areas was 41%, compared to an average of 28% in the rest of Brazil. At December 31, 2003, Telerj Celular and Telest Celular had approximately 3.7 million cellular lines in service, of which approximately 2.6 million were prepaid. Tele Sudeste's consolidated operating revenues were R\$1,893 million in 2003, R\$1,848 million in 2002 and R\$1,703 million in 2001.

Tele Leste Celular Participações

	<u>2001</u>	<u>2002</u>	<u>2003</u>
Cellular lines in service at year-end	822	973	1,126
Customer growth during year	22.0%	18.3%	15.8%
Prepaid lines in service at year-end	499	673	835
Churn(1)	19.8%	25.5%	33.0%
Estimated population of authorization area at year-end (million)(2)	15.1	15.1	15.4
Estimated covered population at year-end (million)(3)	9.3	9.5	10.5
Percentage of population covered(4)	62%	63%	68%
Penetration at year-end(5)	8.9%	10.6%	13.4%
Net operating revenues (in millions of Reais)(6)	386.3	431.4	441.3
Net Income (loss) (in millions of Reais)(6)	(6.0)	(5.1)	(42.7)
Total assets (in millions of Reais)(6)	861.5	956.7	831.7

- (1) Churn is the number of customers that leave Telebahia Celular and Telergipe Celular during the year calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the Instituto Brasileiro de Geografia e Estatística IBGE and Target 2002 "Brasil em Foco".
- (3) Number of people within the region that can access the cellular telecommunications signal.
- (4) Percentage of the population in the region that can access the cellular telecommunications signal.
- (5) Number of cellular lines in service in the region, including competitors, divided by the population of the region.
- (6) Data taken from the financial statements prepared under Brazilian GAAP.

Tele Leste Celular Participações, or Tele Leste, holds 100% of Telebahia Celular, the leading mobile telephone operator in the state of Bahia and 100% of Telergipe Celular, the leading mobile operator in the state of Sergipe. These states have a combined population of approximately 15.4 million people and together contribute around 5% of Brazil's GDP. As of December 31, 2003, mobile penetration in Tele Leste's authorization areas was 13%, compared to 28% in the rest of Brazil. At December 31, 2003, Tele Leste had approximately 1.1 million cellular lines in service, of which approximately 0.8 million were prepaid. Tele Leste's operating revenues were R\$441 million in 2003, R\$431 million in 2002 and R\$386 million in 2001.

CRT Celular

	<u>2001</u>	<u>2002</u>	<u>2003</u>
Cellular lines in service at year-end (in thousands)	1,785	2,078	2,523
Customer growth during year	22.9%	16.4%	21.4%
Prepaid lines in service at year-end (in thousands)	1,206	1,466	1,836
Churn(1)	17%	16%	21%
Estimated population of authorization area at year-end (millions)(2)	10.0	10.5	10.6
Estimated covered population at year-end (millions)(3)	8.2	8.6	10.2
Percentage of population covered(4)	82%	82%	96%
Penetration at year-end(5)	26%	30%	39%
Net operating revenue (in millions of Reais)(6)	840.4	896.3	1,032.7
Net Income (in millions of Reais)(6)	102.9	147.6	189.4
Total assets (in millions of Reais)(6)	1,417.3	1,678.7	1,739.5

- (1) Churn is the number of customers that leave CRT Celular during the year, calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the Instituto Brasileiro de Geografia e Estatística IBGE and Target 2002 "Brasil em Foco".
- (3) Number of people within the region that can access the cellular telecommunication signal.
- (4) Percentage of the population in the region that can access the cellular telecommunication signal.
- (5) Number of cellular lines in service in the region, including competitors, divided by the population of the region.
- (6) Data taken from financial statements prepared under Brazilian GAAP.

CRT Celular is the leading mobile telephone operator in the state of Rio Grande do Sul. The state of Rio Grande do Sul has a population of approximately 10.6 million people and contributes around 8% of Brazil's GDP. As of December 31, 2003, mobile penetration in CRT Celular's authorization area was 39%, compared to 28% in the rest of Brazil. At December 31, 2003, CRT Celular had approximately 2.5 million cellular lines in service, of which approximately 1.8 million were prepaid. CRT Celular's operating revenues were R\$1,033 million in 2003, R\$896 million in 2002 and R\$840 million in 2001.

Tele Centro Oeste Participações

	<u>2001</u>	<u>2002</u>	<u>2003</u>
Cellular lines in service at year-end (in thousands)	2,412	3,067	4,112
Customer growth during year	42.2%	27.2%	34.1%
Prepaid lines in service at year-end (in thousands)	1,717	2,207	3,162
Churn(1)	23.4%	20.5%	23.8%
Estimated population of authorization area at year-end (millions)(2)	30.7	31.2	31.8
Estimated covered population at year-end (millions)(3)	21.6	23.0	24.2
Percentage of population covered(4)	70%	74%	76%
Penetration at year-end(5)	12.8%	16.3%	23.3%
Net operating revenues (in millions of Reais)(6)	1,248.1	1,572.1	1,958.9
Net Income (in millions of Reais)(6)	208.1	329.2	463.4
Total assets (in millions of Reais)(6)	2,052.1	2,364.7	2,654.2

- (1) Churn is the number of customers that leave the mobile operating subsidiaries of TCO during the year, calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the Instituto Brasileiro de Geografia e Estatística IBGE and Target 2002 "Brasil em Foco".
- (3) Number of people within the region that can access the cellular telecommunications signal.
- (4) Percentage of the population in the region that can access the cellular telecommunications signal.
- (5) Number of cellular lines in service in the region, including competitors, divided by the population of the region.
- (6) Data taken from financial statements prepared under Brazilian GAAP.

Certain mobile operating subsidiaries of TCO use a frequency range known as band A that covers 49% of the municipalities in the Brazilian states of Acre, Distrito Federal, Goiás, Mato Grosso, Mato Grosso do Sul, Rondônia and Tocantins and 89% of the population of those states. Another mobile operating subsidiary uses a frequency range known as band B that covers 27% of the municipalities in the Brazilian states of Amazonas, Amapá, Maranhão, Pará and Roraima and 65% of the population of those states. At December 31, 2003, the mobile operating subsidiaries of TCO had 4.1 million cellular lines in service, which represented a 34.1% net increase from December 31, 2002, and a market share of approximately 55.6% in the states in which it operates.

Services. Vivo provides mobile telecommunications services using both digital and analog technologies. Vivo's network provides both CDMA digital service and AMPS, or analog services, through TCP, Tele Sudeste and Tele Leste. TCO and CRT Celular provide mobile telecommunications services using CDMA/TDMA digital technology and AMPS analog technology. All Vivo's services are provided in the 850 MHz frequency range.

Vivo offers voice service, ancillary services, including voicemail and voicemail notification, call forwarding, three-way calling, caller identification, short messaging, limitation on the number of used minutes, mobile chat room, and data services, such as WAP, through which clients can access WAP sites and portals. At December 31, 2003, 56% of Vivo's total subscribers already had WAP-enabled handsets. Vivo offers high speed data services that (i) provide direct access to the Internet through either PCMCIA cards designed to connect compatible PDA's and laptops to 2.5G service or through 2.5G mobile phones by cable connection and (ii) offer corporate subscribers secure access to their intranet and office resources.

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In 2003, Vivo launched MMS and MExE (Mobile Execution Environment) that enable customers to download and execute applications through their mobile handsets. Also, Vivo launched a user-friendly interface, with icons on individual mobile handsets that identify the main services provided, such as Voice Mail, Downloads and SMS.

Vivo offers roaming services through agreements with local mobile service providers throughout Brazil and other countries that allow its subscribers to make and receive calls while out of its concession areas. Also Vivo provides reciprocal roaming services to subscribers of those mobile service providers while they are in its concession areas. See " *Roaming*".

Subscribers and Traffic. At the end of 2003, there were approximately 45.7 million wireless subscribers in Brazil, and there was an estimated market penetration rate of approximately 28% in the areas where Vivo operates. In 2003, the Brazilian market experienced a 30% increase in the number of wireless subscribers and a 33% increase in those areas where Vivo operates. The greatest increase in subscribers was in the Brazilian states of São Paulo, Rio de Janeiro, Rio Grande do Sul and the Cento Oeste region. As of December 31, 2003, Vivo had approximately 20.7 million wireless subscribers, with an estimated market share of 56% in its areas of operation and 45% in Brazil.

The subscriber growth in Vivo's operating companies was supported by (i) the launch of new products and services, including prepaid products and new messaging services, (ii) the growth of the digital capacity of the network, (iii) the improvement in CRM systems, (iv) marketing campaigns and promotions, and (v) the restructuring and expansion of sales networks.

Marketing. Vivo closely follows developments in the markets where it operates and often launches new segment-specific promotions through direct marketing, including mailing and telemarketing campaigns, as well as promotions to its competitors' major customers. Efforts to acquire new customers for the pre-paid and post-paid services were mostly made through voice and data services promotions designed to increase on-net traffic and stimulate the use of data services. With the simultaneous goal of maintaining its existing customer base, Vivo's promotions were also open to existing customers who wanted to change their mobile handsets. Vivo's operators were actively involved in a high-value customer loyalty program, offering competitive discounts on mobile phones through direct marketing actions.

Customer Service. As part of its strategy to standardize customer service provided by Vivo's operators, Vivo has outsourced 100% of its customer service while maintaining full management control. Customer service is available on a 24-hour basis from Vivo's call centers and through its website.

Customer satisfaction is evaluated regularly. In 2003 more than 8,700 Vivo customers were interviewed across Brazil in 2003 to gather their opinions about customer assistance, technical assistance, products and services. Vivo's average overall satisfaction mark was 8.25 on a scale of 1 to 10. Vivo continues to search for ways to increase further customer satisfaction.

Vivo has trained or qualified staff to assist and provide explanations to customers in connection with any requests or doubts they may have concerning services provided. Vivo attempts to respond to all customer requests.

Vivo was ranked first in 2003 in a nationwide poll conducted by the IBRC (Brazilian Institute of Customer Relations) on "companies that most respect consumers", the results of which were published in the Consumidor Moderno (Modern Consumer) magazine.

Network and Capital Expenditures. Vivo's networks are connected primarily through fiber-optic transmission systems leased from incumbent wireline operators in the areas in which it operates, consisting of mobile switches, base stations and other network elements, such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point, PDSN and

gateways. Vivo's main suppliers are NEC do Brasil S.A., Nortel Networks, Motorola do Brasil Ltda., Lucent Technologies do Brasil, Ind. e Com. Ltda. and Ericsson Telecomunicações S.A.

Vivo's operating companies' networks use analog and digital technology. Digitalization offers certain advantages, such as greater network capacity and additional revenue through the sale of value-added services. Digital mobile telecommunications service also reduces the risk of fraud. Vivo continues to increase network capacity and coverage to improve the quality of service and to meet customer demand.

Before November 1998, TCP's network used only AMPS analog technology. After its privatization in 1998, TCP began to use CDMA digital technology. At December 31, 2003, Telesp Celular's telecommunications network, which provides both CDMA digital and AMPS analog services, covered 77% of the municipalities in the state of São Paulo, or 98% of the population, in its authorization area.

Global Telecom only offers services through CDMA digital technology. At December 31, 2003, Global Telecom's telecommunications network covered 29% of the municipalities, or 76% of the population, in its authorization areas.

At December 31, 2003, Tele Sudeste's telecommunications network, which provides CDMA digital and AMPS analog services, covered 100% of the municipalities, or 96% of the population, in its authorization areas.

At December 31, 2003, Tele Leste's telecommunications network, which provides CDMA digital and AMPS analog services, covered 31% of the municipalities, or 68% of the population, in its authorization areas.

At December 31, 2003, CRT Celular's telecommunications network, which provides CDMA digital, TDMA digital and AMPS analog services, covered 68% of the municipalities, or 96% of the population, in its authorization areas.

At December 31, 2003, TCO's telec