

PORTUGAL TELECOM SGPS SA
Form 20-F
June 30, 2003

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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, 2002

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
Ordinary shares, nominal value €1 each

New York Stock Exchange
New York Stock Exchange*

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

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

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.

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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, 2002. 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.

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PART I

ITEM 1 IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

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

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ITEM 2 OFFER STATISTICS AND EXPECTED TIMETABLE

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

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ITEM 3 KEY INFORMATION

Selected Consolidated Financial Data

The selected consolidated balance sheet data as of December 31, 2001 and 2002 and selected consolidated statement of income and cash flow data for each of the years ended December 31, 2000, 2001 and 2002 have been derived from our audited consolidated financial statements included herein. The selected consolidated balance sheet data as of December 31, 1998, 1999 and 2000 and selected consolidated statement of income and cash flow data for each of the years ended December 31, 1998 and 1999 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 "Item 5 Operating and Financial Review and Prospects Portuguese GAAP Compared with U.S. GAAP" and Notes 38, 39 and 40 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 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 with "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, in Brazil. 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), 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 Brasilcel. 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 Mobile Businesses Joint Venture with Telefónica Móviles in Brazil." and "Item 4 Information on the Company Strategic Alliances Alliance with Telefónica".

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

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and cash flow data will proportionally consolidate 50% of Brasilcel's income and cash flows from January 1, 2003.

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, 2001 and 2002 presented below reflects 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 are reflected in our consolidated balance sheet through our proportional consolidation of Brasilcel. Global Telecom's statements of income and cash flows will in the future be reflected in our consolidated statements of income and cash flows through our proportional consolidation of Brasilcel's statements of income and cash flows.

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.

Information provided in U.S. dollars for the year ended December 31, 2002 has been calculated on the basis of the Euro/U.S. dollar exchange rate on that date of €0.9537 = US\$1.00. See " *Presentation of Financial Information*" and " *Key Information Exchange Rates*", below.

	Year Ended December 31,					
	2002	2002	2001	2000	1999	1998
	US\$	EUR	EUR	EUR	EUR	EUR
STATEMENT OF PROFIT AND LOSS DATA:						
Amounts in accordance with Portuguese GAAP						
Operating revenues:						
Services rendered	5,191.0	4,950.9	4,976.3	4,329.8	2,832.4	2,648.7
Sales of merchandise and products	515.9	492.0	613.5	684.7	213.1	141.5
Telephone directory	145.9	139.1	136.8	131.7	126.1	121.0
Total operating revenues	5,852.8	5,582.0	5,726.6	5,146.2	3,171.6	2,911.2
Operating costs and expenses:						
Wages and salaries	728.5	694.8	668.6	578.1	520.8	515.5
Post retirement benefits	192.1	183.2	140.7	103.4	95.5	96.1
Costs of telecommunications	653.1	622.9	715.1	470.7	161.9	167.3
Depreciation and amortization	1,009.5	962.8	956.2	1,021.5	636.7	612.4
Subsidies	(33.0)	(31.5)	(36.8)	(38.1)	(38.5)	(43.9)
Maintenance and repairs	135.6	129.2	120.1	105.7	68.9	61.3
Own work capitalized	(119.6)	(114.0)	(179.3)	(133.9)	(120.8)	(98.7)
Raw materials and consumables	101.9	97.2	139.1	97.3	85.4	76.3
Costs of products sold	485.1	462.7	619.8	658.0	238.4	148.4
Telephone directories	96.5	92.0	89.2	87.1	82.2	78.5
Marketing and publicity	114.1	108.8	142.0	157.5	68.5	71.3
Concession rent	18.8	18.0	14.5	22.7	22.2	21.6
Other general and administrative	968.7	923.9	997.1	847.0	386.7	343.2
Provision for doubtful receivables, inventories & other	139.2	132.8	130.7	188.6	63.5	61.1
Other net operating income	(47.5)	(45.3)	(45.3)	(51.9)	(47.5)	(40.9)
Taxes other than income taxes	81.6	77.8	87.1	95.7	34.5	30.8
Total operating costs and expenses	4,524.6	4,315.3	4,558.8	4,209.5	2,258.4	2,100.3
Operating income	1,328.1	1,266.7	1,167.8	936.8	913.2	810.9
Other expenses, net	570.2	543.9	1,063.5	423.8	261.5	132.3
Work force reduction program costs	56.3	53.7	183.9	252.7	457.7	71.7
Extraordinary items	16.4	15.6	281.1	(496.4)	(540.5)	(89.2)
Income before income taxes	685.2	653.5	(360.7)	756.7	734.5	696.1
Provision for income taxes	(353.4)	(337.1)	(174.6)	(258.6)	(241.9)	(252.4)
Consolidated net income before minority interests	331.8	316.4	(535.3)	498.1	492.6	443.7
Loss (income) applicable to minority interests	78.2	74.6	342.7	42.3	2.1	(2.6)
Consolidated net income	410.0	391.1	(192.6)	540.3	494.7	441.1

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Year Ended December 31,

Earnings per ordinary share, A share and ADS(1)	0.33	0.31	(0.15)	0.45	0.47	0.46
Cash dividends per ordinary share, A share and ADS(1)(2)(3)	0.17	0.16	0.10		0.20	0.20
Amounts in accordance with U.S. GAAP						
Operating revenues	6,299.1	6,007.7	6,042.8	5,199.9	4,107.3	3,502.9
Operating income as restated(6)	401.8	383.2	696.1	395.8	592.7	883.1
Net income before change in accounting principles as restated(6)	1,379.1	1,315.3	208.1	66.8	532.8	400.1
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	(1,089.3)	(1,038.9)				
Net income after change in accounting principles as restated(6)	289.8	276.4	150.6	(59.8)	532.8	400.1
Earnings per ordinary share, A share and ADS as restated(4)(6)	0.23	0.22	0.12	(0.05)	0.54	0.42
Diluted net income per share as restated(5)(6)	0.23	0.21	0.12	(0.05)	0.53	0.42
On a pro-forma basis(7)						
Net income before change in accounting principles SAB 101 as restated(6)	289.8	276.4	150.6	66.8	532.8	400.1
Net income after change in accounting principles SAB 101 as restated(6)	289.8	276.4	150.6	(59.8)	528.5	394.0
Earnings per ordinary share, A share and ADS after change in accounting principles SAB 101 as restated(4)(6)	0.23	0.22	0.12	(0.05)	0.53	0.41
Diluted net income per share after change in accounting principles SAB 101 as restated(5)(6)	0.23	0.21	0.12	(0.05)	0.52	0.41

- (1) Based on 950,000,000 ordinary and A shares issued in the year ended December 31, 1998 (as adjusted to give effect to the five-for-one share split effected in October 1999), 1,045,000,000 ordinary and A shares issued in the year ended

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December 31, 1999, 1,201,750,000 ordinary and A shares issued in the year ended December 31, 2000, 1,254,285,000 ordinary and A shares issued in the year ended December 31, 2001 and 2002.

- (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, 1998, 1999, 2001 and 2002 in US\$ were US\$ 0.24, US\$ 0.20, US\$ 0.10 and US\$ 0.17, respectively.
- (4) Based on the weighted average number of shares as of the date given and taking into consideration the number of shares issued pursuant to capital increases and all treasury shares, there were 950,000,000 shares for the year ended December 31, 1998, 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 and 1,253,880,328 shares for the year ended December 31, 2002.
- (5) The weighted average number of shares is computed as a weighted average as of the date given and taking into consideration 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 and 2001, 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

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discussed in Note 38 y) to our audited consolidated financial statements.

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The pro-forma information shows the application of SAB 101, as if it had been applied in the years ended December 31, 1998 and 1999.

	Year Ended December 31,					
	2002	2002	2001	2000	1999	1998
	US\$	EUR	EUR	EUR	EUR	EUR
CASH FLOW DATA:						
Amounts in accordance with Portuguese GAAP						
Cash flows from operating activities	2,193.8	2,092.3	1,475.4	1,357.6	1,109.6	1,160.5
Cash flows from investing activities	(1,058.6)	(1,009.6)	(2,528.5)	(2,343.2)	(741.3)	(3,683.6)
Cash flows from financing activities	(509.6)	(486.1)	1,839.9	1,131.0	(1,425.6)	3,681.8

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	Year Ended December 31,					
	2002	2002	2001	2000	1999	1998
	US\$	EUR	EUR	EUR	EUR	EUR
(in millions, except number of ordinary shares)						

BALANCE SHEET DATA:						
Amounts in accordance with Portuguese GAAP						
Current assets	5,086.2	4,850.9	3,628.1	2,032.6	1,205.1	2,166.8
Investments, net	394.6	376.4	2,000.3	1,295.3	1,498.2	1,307.2
Fixed assets, net	4,797.7	4,575.8	5,491.3	5,446.2	3,855.9	3,677.0
Intangible assets post retirement benefits			761.9	495.0	399.1	342.8
Intangible assets Other, net	3,112.7	2,968.7	4,934.4	3,878.8	1,492.3	1,737.3
Other non-current assets, net	1,000.6	954.3	820.3	68.3	67.1	46.3
Total assets	14,391.8	13,726.1	17,636.3	13,216.2	8,517.7	9,277.4
Current liabilities	3,101.5	2,958.0	3,240.0	3,154.2	1,535.6	4,935.6
Long-term debt	5,472.2	5,219.1	5,428.3	2,815.2	2,649.6	1,016.9
Accrued post retirement liability	1,113.0	1,061.5	1,810.0	1,488.0	1,228.0	829.8
Deferred income investment subsidies	53.5	51.1	63.1	113.7	153.4	194.1
Deferred income post retirement benefits			23.0	26.2	28.5	38.9
Other non-current liabilities	920.6	878.0	1,685.1	143.7	85.4	66.9
Total liabilities	10,660.8	10,167.6	12,249.5	7,741.0	5,680.5	7,082.2
Net assets	3,731.1	3,558.5	5,386.7	5,475.2	2,837.2	2,195.2
Minority interests	468.9	447.2	1,220.0	1,113.1	78.2	30.0
Total shareholders' equity	3,262.2	3,111.3	4,166.8	4,362.1	2,759.0	2,165.2

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Year Ended December 31,

Total liabilities and shareholders' equity	14,391.8	13,726.1	17,636.3	13,216.2	8,517.7	9,277.4
Number of ordinary shares	1,254,284,500	1,254,284,500	1,254,284,500	1,201,749,500	935,750,000	142,500,000
Amounts in accordance with U.S. GAAP						
Total assets as restated(1)	13,163.1	12,554.2	16,747.8	14,534.6	11,958.7	11,967.0
Total liabilities as restated(1)	10,661.0	10,167.9	11,902.5	9,019.4	7,121.8	8,038.5
Total shareholders' equity as restated(1)	2,457.4	2,343.7	3,736.5	4,191.8	3,342.3	2,548.9

(1) 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 38 y) to our audited consolidated financial statements.

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Exchange Rates

Euro

Effective January 1, 1999, Portugal and ten other member countries of the European Union adopted the Euro as their common currency. The Euro was traded on currency exchanges and was available for non-cash transactions during the transition period between January 1, 1999 and December 31, 2001. During this transition period, the national currencies remained legal tender in the participating countries as denominations of the Euro, and public and private parties paid for goods and services using either the Euro or the participating countries' existing currencies. On January 1, 2002, the Euro entered into cash circulation. Between January 1, 2002 and 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.

For the years ended December 2001 and 2002, 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 Reals and certain of our liabilities 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 other such 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. Unless otherwise noted, 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 26, 2003, the Euro/U.S. dollar exchange rate was €0.8750 per US\$1.00.

Year ended December 31,	Average Rate(1)
	(EUR per US\$1.00)
1998(2)	
1999	0.9954
2000	1.0747
2001	1.1342
2002	1.0531

- (1) The average rate is calculated as the average of the noon buying rate on the last day of each month during the period.
- (2) The Euro was not introduced until January 1, 1999.

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Period	High	Low
	(EUR per US\$1.00)	
December 31, 2002	0.9569	0.9521
January 31, 2003	0.9328	0.9230
February 28, 2003	0.9321	0.9253
March 31, 2003	0.9278	0.9152
April 30, 2003	0.9041	0.8939
May 31, 2003	0.8495	0.8484

None of the 15 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 legal exchange markets in Brazil:

the commercial rate exchange market; and

the floating rate exchange market.

The commercial rate exchange market is reserved primarily for foreign trade transactions and transactions that generally require prior approval from Brazilian monetary authorities, such as the purchase and sale of registered investments by foreign persons and related remittances of funds abroad. Purchases and sales of foreign exchange in the commercial rate exchange market may be carried out only through a financial institution in Brazil authorized to buy and sell currency in that market. The rate of exchange on the floating rate exchange market applies to transactions to which the rate of exchange on the commercial rate exchange market does not apply. Prior to the implementation of the Real Plan, which was introduced by the Brazilian Government in March 1995 to establish a trading band for the Real against the U.S. dollar and which resulted in the overall devaluation of the Real relative to the U.S. dollar, the prevailing selling rate for Brazilian currency into U.S. dollars on the commercial rate exchange market and the prevailing selling rate for Brazilian currency into U.S. dollars on the floating rate exchange market differed significantly at times. Since the introduction of the Real Plan, the two rates have not differed significantly, although there can be no assurance that the two rates will not differ significantly in the future. The rates of exchange on the commercial rate exchange market and the floating rate exchange market are freely negotiated but are strongly influenced by the Brazilian Central Bank.

Between March 1995 and January 1999, the Brazilian Central Bank maintained a band within which the exchange rate between the Real and the U.S. dollar fluctuated, and the Brazilian Central Bank intervened in the foreign exchange market from time to time. From January 20, 1998 through December 31, 1998, the Brazilian Central Bank maintained the band between R\$1.12 and R\$1.22 per US\$1.00. In January 1999, the Brazilian Central Bank attempted a controlled devaluation of the Real by widening the band within which the Real was permitted to trade, but subsequent Brazilian Central Bank intervention failed to keep the rate within the new band. On January 15, 1999 the Brazilian Central Bank announced that the Real would be permitted to float, with Brazilian Central Bank intervention to take place only in times of extreme volatility.

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 26, 2003, the Real/U.S. dollar exchange rate was R\$2.9000 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)
1998	1.1640
1999	1.8640
2000	1.8650
2001	2.3530
2002	2.9945

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

Period	High	Low
	(R\$ per US\$1.00)	
December 31, 2002	3.535	3.531
January 31, 2003	3.566	3.474
February 28, 2003	3.573	3.549
March 31, 2003	3.385	3.320
April 30, 2003	2.915	2.869
May 31, 2003	2.971	2.971

Escudo

As of January 1, 2002, we ceased to use the Escudo. Because, for the years ended December 31, 2001 and 2002, the majority of our revenues, assets and expenses were denominated in Euros, revenues, assets and expenses for years prior to the year 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 2002, approximately 36% of our consolidated revenues were derived from services provided by our fixed telephone business unit. 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 introduction of 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 activated 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 PT Comunicações*".

A Growing Percentage of Our Revenue Is Derived From Businesses That Require Substantial Investments by Us and Are Increasingly Competitive

During 2002, approximately 64% of our consolidated revenues were derived from businesses other than our wireline telephone services, wholesale and other traditional businesses in Portugal. These businesses include mobile telecommunications, multimedia and Internet services, and data and business solutions, particularly in Portugal and Brazil. To ensure the continued growth and success of these businesses, we have to make significant investments of both capital and personnel.

We believe that the development of mobile telecommunications, multimedia, Internet and data and business solutions services presents our company with appreciable growth opportunities. However, the success of our mobile telecommunications, multimedia and Internet businesses is subject to increasing competition and rapid and sometimes unpredictable changes in technology. 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 obtain the financing to fund the requisite investments in these new businesses;

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 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 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 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 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 such 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.

Litigation over Claims for Municipal Taxes and Fees Could Result in Liabilities for Back Taxes

The Portuguese municipality of Oporto has claimed that as of December 31, 2001 we owe them €0.6 million in taxes and fees because our infrastructure uses their public rights-of-way. The municipality of Lisbon had also brought claims relating to similar issues which are not currently being pursued. In contesting our obligation to pay the taxes and fees claimed by the municipality of Oporto, we and the Portuguese government have relied on provisions of our wireline concession from the Portuguese government and a law enacted in 1997, which the Portuguese government intended to exempt us from this type of tax or fee.

If the pending claims by Oporto were to be resolved against our interest, other municipalities might seek to make or renew claims against us. Portuguese law would prevent municipalities from claiming taxes for periods more than four years before the claim. If they were to make claims and prevail in lawsuits against us or the Portuguese government, we might have to pay substantial back taxes. See "*Item 8 Financial Information Legal Proceedings Claims for Municipal Taxes and Fees*".

Litigation by a Consumer Protection Association Could Result in Liabilities for Charges

A Portuguese consumer protection association, known as DECO, has brought claims against us relating to the call set-up charges we charged to customers in 1999. In November 2002, we appealed to the Supreme Judicial Court against an adverse ruling of the Lisbon District Court. We are unable to estimate the amount of any liability should we lose the case in the Supreme Judicial Court because we

cannot predict the number of subscribers who would bring a claim, the number of calls in respect of which such subscribers would claim, or whether such subscribers would be able to produce any necessary evidence in respect of such a claim. Nevertheless, if the pending case in the Supreme Judicial Court were to be resolved against our interest and subscribers representing a large number of calls were to bring claims and provide the necessary evidence, we might have to pay a substantial amount in repayment of the call set-up charges for calls in 1999. See "*Item 8 Financial Information Legal Proceedings Claims by a Consumer Protection Association*".

The Portuguese Government Holds All of Our A Shares and Such Shares Afford It Certain 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 the shareholders of our company, 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, 2002, cumulative foreign currency transaction adjustments related to investments in Brazil were negative €2,259.2 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*"

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and "*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, including in telecommunications operators, such as Telesp Celular and Global Telecom, which were contributed to Brasilcel (the 50/50 joint venture with Telefónica Móviles for mobile operations in Brazil). The major factors that could have a material adverse effect on our investments in Brazil, including Brasilcel, and on our results of operations in Brazil, including Brasilcel's, 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 and by 12.8% in 2001. During 2002, the Real continued to undergo significant devaluation due in part to the political uncertainty in connection with the elections and the global economic slowdown. In 2002, the Real devalued against the

Euro by 81.4%. In the period leading up to, and after 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 differed 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. Although the new government has not yet departed in any material way from previous policy, we believe that it is premature to determine what policies might be implemented by the new government, whether these policies will be effective, and how investors and the capital markets will react to them. The Real has appreciated during 2003 and there are 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 further 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.

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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. The 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 rate costs because part of the interest on our debt, primarily Reais-denominated based on the commercial rate exchange market, is floating.

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 26.4% in 2002 compared to 10.4% in 2001 and 9.8% in 2000. If Brazil continues to experience significant inflation, Brasilcel 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.

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, Brasilcel, with Telefónica Móviles. On December 27, 2002, PT Móveis - Serviços de Telecomunicações, SGPS, S.A. or PT Móveis, which holds our interests in international mobile telecommunications companies, and Telefónica Móviles transferred their direct and indirect interests in Brazilian mobile operators to the joint venture company, named Brasilcel, with headquarters in the Netherlands.

As in any joint venture, it is possible that Telefónica Móviles and we will not agree on Brasilcel's strategy, operations or other matters. Any inability of Telefónica Móviles and us to jointly operate Brasilcel could have a negative impact on Brasilcel'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 Brasilcel 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 Brasilcel's Results

Our mobile business in Brazil is subject to 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 telecommunication sector may have a negative impact on Brasilcel's revenues and results of operations. Moreover, Brasilcel'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

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rates by the Brazilian government increase their costs. Such circumstances may have a material adverse effect on Brasilcel's results of operations.

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

In September 2000, ANATEL introduced a new mobile services licensing regime, or SMP. The new regime permits existing mobile service providers operating under concessions to migrate to the new regime and become SMP license holders. Each of Brasilcel's subsidiaries has migrated to the new 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 Brasilcel'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 Brasilcel's subsidiaries. As a result, Brasilcel's subsidiaries no longer receive revenues from long distance services but receive revenues from interconnection fees paid by wireline long distance operators for long distance traffic originating and terminating on their networks. The interconnection fees may not compensate for the loss of long distance revenues and as a result overall revenues of Brasilcel's subsidiaries may be significantly reduced. 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 Brasilcel'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 Brasilcel's subsidiaries and the wireline operators after June 30, 2004. Because a significant number of mobile subscribers use prepaid mobile services and typically receive more calls than they make, Brasilcel'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.

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

Several licenses have been granted for mobile telecommunications services in the areas where Brasilcel's subsidiaries operate since the opening of the Brazilian market for mobile telecommunications services in 1998. 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 Brasilcel's subsidiaries or if some brand names become better known than others. Brasilcel'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 Brasilcel'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 Brasilcel's coverage areas and competing operators, see "*Item 4 Information on the Company Competition Competition Facing Our Mobile Businesses Telesp Celular 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, as well as in other international markets. Our service offering covers a full range of:

fixed line telephone services for retail and wholesale customers, leased lines, interconnection and distribution of programming for TV and radio broadcasters;

data and business solutions, such as data communications, business-to-business e-commerce and data and networking solutions, solutions using Internet protocol, or IP, as well as outsourcing telecommunications systems;

mobile telecommunications services, such as voice, data and Internet-related services, as well as sales of mobile equipment in Portugal, Brazil and other international markets;

multimedia services, such as cable and satellite television services and TV programming, film distribution and screening, newspaper publishing and distribution, radio programming and Internet access, portal and e-commerce services; and

sales of telecommunications equipment in Portugal.

In Portugal, we are the leading provider of all of these services. The provision of fixed line telephone services in Portugal continues to account for a large proportion of our revenues (27% during 2002) 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 a new mobile telecommunications services company in Brazil, Brasilcel, on December 27, 2002. See " *Joint Venture with Telefónica Móviles in Brazil*", 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 and Brazil, such as the mobile voice and data services, multimedia and Internet services and data and business solutions listed above.

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:

exploit new growth opportunities in service areas, such as mobile services, multimedia and Internet services and data and business solutions in Portugal, Brazil and other international markets;

continue to leverage our experience as the leading provider of all these services in Portugal and pursuing opportunities for growth in Brazil and in other international markets; and

capitalize on our leading position in the Portuguese market for fixed line services to preserve the profitability and cash flow of these businesses.

Our Businesses

Business Units

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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 are currently in the process of integrating different functions across the board, with particular emphasis on information systems (PT Sistemas de Informação), research and development capabilities (PT Inovação) and back office activities (PT Pro). Additionally, we have created a central purchasing unit, PT Compras, which will be operated as a separate company responsible for all purchasing of the PT group. See "*Item 5 Operating and Financial Review and Prospects Overview Our Business Reorganization and Revenue Reporting Categories*".

The diagram below presents our corporate structure, taking into account our reorganization:

The business unit subsidiaries hold subsidiaries through which they operate in Portugal, Brazil and other countries. In our discussions of these businesses below, we have provided diagrams of the organizational structures of PT Prime, SGPS, S.A., or PT Prime, PT Multimedia - Serviços de Telecomunicações e Multimedia, SGPS, S.A., or PT Multimedia, and PT Móveis.

PT Comunicações

PT Comunicações holds and operates our fixed line network. We provide 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 of September 9, 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 includes the 2002 Concession rental payment of €16.6 million. Since then, PT Comunicações owns the basic telecommunications network.

Our fixed line services are based on the use of the fixed line network. They consist of:

fixed line telephone services for retail customers, including public domestic and international call services;

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

telecommunications equipment sales and other revenues.

Fixed Line Telephone Services General. Our group's largest business is providing public fixed line telephone services in Portugal to retail customers. This business area provided €1,512.1 million, €1,712.8 million and €1,541.2 million to our consolidated operating revenues during 2002, 2001 and 2000, respectively. Subscribers to our public fixed line telephone services are charged for network access on the basis of a monthly line rental as well as rates based on amount and type of usage in addition to an initial installation fee. Since January 1, 2000, public switched fixed line telephone services in Portugal have been fully open to competition.

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As a result of the introduction of competition, combined with 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 PT Comunicações.*"

Our consolidated financial statements do not classify our telephone services revenues according to type of service or traffic. However, we distinguish two principal types of telephone services:

Domestic Fixed Line Telephone Services: these include domestic telephone services provided by PT Comunicações directly to subscribers that originate or terminate calls on its fixed line network; and

International Fixed Line Telephone Services: these include international telephone services provided by PT Comunicações directly to users that originate calls on its fixed line network or receive incoming calls from outside Portugal and also include calls which pass through but do not terminate or originate on its network, or transit traffic.

Traffic. Measured in minutes, total fixed line traffic originating on PT Comunicações' fixed line network decreased by 5.5% during 2002, compared with 2001. 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. During the five-year period from 1998 through 2002, total traffic originating on the network increased by an average of 6.0% 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

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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,				
1998	1999	2000	2001	2002
(%)	(%)	(%)	(%)	(%)

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Year ended December 31,

	Millions of minutes		Millions of minutes		Millions of minutes		Millions of minutes		Millions of minutes	
Domestic	10,633	82.1	9,972	69.4	8,933	53.7	7,431	43.0	6,480	39.6
International	384	3.0	410	2.8	413	2.5	411	2.4	402	2.5
Fixed-to-Mobile	743	5.7	1,083	7.5	1,290	7.8	1,215	7.0	1,119	6.8
Internet	1,100	8.5	2,800	19.5	5,630	33.8	6,920	40.0	6,581	40.3
Other	96	0.7	114	0.8	379	2.2	1,319	7.6	1,758	10.8
Total	12,956	100.0	14,379	100.0	16,645	100.0	17,296	100.0	16,340	100.0

During 2002, Internet-related traffic accounted for approximately 40% of the total traffic originated on the fixed line network compared with 40% during 2001. We estimate that in 2002, each Internet access call on the fixed line network averaged approximately 17.5 minutes. This compared with only 2.6 minutes for the average voice telephone call. However, PT Comunicações receives less revenue for Internet traffic than voice traffic on a per-minute basis. Internet-related traffic generates €0.0075 of revenue per minute as compared with voice-related traffic which generates €0.0828 of revenue per minute. According to an ANACOM administrative decision of February 21, 2001, PT Comunicações changed its billing structure for Internet service. The present 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. For additional information, see "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 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 its network in its fixed line telephone services unit. Traffic originating on other networks but terminating on PT Comunicações' 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 retained revenue to its fixed line telephone service revenue. As a result of this change, PT Comunicações' absolute margins have not changed, but its percentage margins decreased. See "Wholesale Services Traffic", below.

Fixed Line Network. PT Comunicações maintained approximately 4.1 million main lines in service at December 31, 2002, excluding external supplementary lines, direct extensions and active multiple numbers. 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 826,000 equivalent ISDN lines. Of the total number of main lines, approximately 67%

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were used for residential subscribers, 32% were used for business subscribers and 1% were used for public pay phones.

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

	As of December 31,				
	1998	1999	2000	2001	2002
Fixed line main lines in service (thousands)					
Traditional main lines	3,803	3,753	3,650	3,501	3,317
ISDN main line equivalents	314	477	653	800	826

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As of December 31,

	As of December 31,				
Total	4,117	4,230	4,303	4,301	4,143
PTC fixed line main lines per 100 inhabitants	40.6	41.5	41.9	42.3	41.9
Public pay phones (thousands)	40.0	42.5	44.6	45.5	43.8

Over past years, PT Comunicações made significant investments to meet subscriber demand for lines and to modernize its fixed line network. As a result, the number of PTC's main lines per 100 inhabitants more than doubled from 20.9 fixed line main lines at the end of 1989 to approximately 41.9 fixed line main lines at the end of 2002.

In September 1999, the number of activated 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. PT Comunicações is addressing this trend by encouraging increased use of its fixed line network for Internet and other data services.

All of PT Comunicações' 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 PT Comunicações 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 2002, PT Comunicações was providing approximately 1,222,000 voicemail boxes.

PT Comunicações' fixed line network includes ISDN lines, which transmit voice and data at higher rates than analog lines. PT Comunicações has offered ISDN services commercially since 1994. It offers a basic-rate service, which provides two communications channels. PT Comunicações also offers a primary-rate service which provides up to 30 communications channels. At the end of December 2002, PT Comunicações had 269,000 subscribers to the basic-rate ISDN service and 9,600 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:

By the end of 2002, ISDN lines represented 19.9% of PT Comunicações' total equivalent fixed line main lines, as compared with 18.6% 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.

PT Comunicações has started to deploy higher-speed ADSL lines and has launched ADSL service on a wholesale basis in Lisbon and Oporto, covering 78% and 68% of those cities, respectively. In 2002, ADSL services were made available in the rest of Portugal, increasing total coverage throughout Portugal to 60.7%.

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PT Comunicações' had 0.3 billing complaints per 1,000 bills and 10.2 reported faults per 100 main lines in the year ended December 31, 2002. The percentage of faults repaired in less than 12 working hours was 88.1% in the year ended December 31, 2002, compared with 76.3% in 2001. This increase in the percentage of faults repaired was due in part to heavy rainfall and floods in Portugal in the beginning of 2001 that caused customers to experience a greater number of faults in 2001 than in 2002. PT Comunicações offers residential customers detailed billing on request without extra charge.

Fixed Line Telephone Services Marketing. PT Comunicações is increasing its marketing efforts towards customers loyalty and promoting increased usage of its wireline telephone services:

Promotional Efforts and Market Analysis. PT Comunicações has increased its promotional and marketing campaigns. It wants the public to recognize that it provides better service and more attractive billing packages than its competitors. PT Comunicações is aggressively promoting the sale of minutes of fixed line network time for traditional voice services as well as connection to the Internet through:

the launch of the ADSL wholesale service;

the offering of special tariffs on "PT Days" (Mother's Day, Father's Day, Valentine's Day) and on special occasions and holidays such as Christmas;

the launch and promotion of innovative products and services, such as the voice portal, "FM Voice Mail Service," a fixed-mobile convergence service, the multilingual "Hello CardPT", "PT Cyberlan Free", integrated Internet/Intranet and fax solutions services designed for small and medium-sized enterprises, "PT Netbiz", "PT NetBox", "PT Confort", "PT Free", "PT Cyberkit RDIS Plus", "PT Central Free" and "PT Centralphone";

the promotion of Voice Mail, Voice Mail Familiar and other service facilities such as call forwarding or call waiting;

the promotion of special pricing packages, namely "Local+", "PT 1ª Vez," "Family and Friends" and "Poupadinha Domingo," addressed both to the residential and business markets and designed to promote domestic and international traffic, the launch of PT Option plans; and

the launch of "the netPoint", a new public phone cabin which allows the use of Internet services and the making of calls simultaneously.

Internet customers can also profit from special programs created by PT Comunicações that provide special conditions to access and use of PT Comunicações' network. PT Comunicações also plans to sell 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.

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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.

Fixed Line Telephone Services Domestic. PT Comunicações estimates that domestic fixed line telephone services generated operating revenues of €1,291.8 million in 2002, €1,502.3 million in 2001 and €1,289.2 million in 2000. PT Comunicações estimates that in 2002, 51.3% of these domestic fixed line telephone service revenues came from traffic charges and 48.7% came from fixed charges, compared to an estimated 57.5% of these domestic fixed line telephone services revenues coming from traffic charges and 42.5% coming from fixed charges in 2001. Fixed charges include installation charges, a monthly subscription charge and telephone set rental charges.

Traffic. PT Comunicações estimates that, as measured in number of minutes, total originating traffic generated by its domestic fixed line telephone services decreased by 5.6% in 2002 over 2001. This decreased usage was driven by decreased voice usage. PT Comunicações estimates that there was a decrease in total domestic traffic on its fixed line network of 3.8% in 2002 compared with 2001. In terms of minutes, its estimated market share reduced by 2.9 percentage points to 89.3% in 2002. This reduction in its market share was in line with its expectations. PT Comunicações believes this reflects the overall impact of competition on our business. See " *Competition Competition Facing PT Comunicações*".

Prices. PT Comunicações charges its domestic fixed line telephone subscribers a one-time installation charge, monthly line rental fees and traffic fees for calls. As of December 31, 2002, the installation charge was €71.83. The standard line rental fee is €11.85 per month for standard lines and €23.89 per month for ISDN basic lines, in each case excluding value-added tax. In 1999, its 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 1998 and the end of 2002, weighted average prices for domestic fixed line telephone services decreased by 6.1% per year in nominal terms. Compared with 2001 over the course of 2002, domestic prices decreased a further 0.9% in nominal and annual terms. PT Comunicações is committed to change its prices annually in accordance with our pricing convention. See " *Regulation Portugal Pricing of Fixed Line Services*".

The chart below illustrates changes in PT Comunicações' prices and fees from 1998 through 2002. The call prices from 1998 through 2002 are for a three-minute call at peak rates in 2002 constant prices. All prices are in Euros and exclude VAT.

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Principal Prices and Fees for Domestic Fixed Line Telephone Services(1)

	As at December 31,				
	1998	1999	2000(2)	2001	2002
Local call prices	0.10	0.10	0.13	0.12	0.12
Regional call prices	0.34	0.31	0.31	0.24	0.23
National call prices	0.77	0.66	0.42	0.35	0.33
Installation fee	81.78	79.94	77.69	74.41	71.83
Line rental per month	11.41	11.66	12.08	12.27	11.85

(1) Amounts rounded to nearest hundredth.

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

Prices for local, regional and national calls did not change in 2002. The average annual reduction in 2002 for the basket of prices was about 0.13% in nominal terms. PT Comunicações' pricing structure has come more into line with pricing structures in the rest of the EU over the last eight years. The following table compares its 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, 2002.

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

	As of December 31, 2002	
	EU Average	Portugal
Local call prices	0.039	0.040
Regional call prices	0.064	0.078
National call prices	0.071	0.111

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.

Fixed Line Telephone Services International. PT Comunicações estimates that operating revenues from international fixed line telephone services were €220.3 million in 2002 compared with €210.5 million in 2001 and €223.2 million in 2000 (which, consistent with our current method of accounting, excludes the amount of €28.7 million related to incoming traffic in 2000 that was included at that time in fixed line telephone services revenues). 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. The other primary source of revenue from international fixed line telephone services is receipts from the calls of other international telecommunications operators that PT Comunicações carries and that terminate with PT Comunicações' customers on a joint or correspondent basis. Payments between PT Comunicações and other international operators for incoming and outgoing calls are made in accordance with bilateral settlement arrangements referred to as "accounting rates" in the telecommunications industry. These arrangements include agreements on rates payable for incoming and outgoing calls. See "Accounting Rates" below. In 2002, 2001 and in 2000, PT Comunicações' revenues from international fixed line telephone services decreased while international traffic continued to grow. This decrease in revenues resulted from decreases in

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international accounting rates and decreases in prices for outgoing international calls. PT Comunicações expects these decreases to continue.

Traffic. The table below shows the total incoming and outgoing international traffic and international transit traffic carried by PT Comunicações during the period 1998 through 2002.

**International Traffic and Transit Traffic
(millions of minutes, except as indicated)**

	Year ended December 31,				
	1998	1999	2000	2001	2002
Outgoing traffic	470	539	620	721	745
Growth in total outgoing traffic (% per annum)	20	15	15	16	3
Incoming traffic	712	797	897	1,000	1,013
Growth in total incoming traffic (% per annum)	13	12	13	12	1
Ratio of incoming to outgoing	1.51	1.48	1.45	1.39	1.36
Switched transit traffic	39	30	35	32	64
Growth (decrease) in switched transit traffic (% per annum)	(11)	(25)	17	(11)	103

PT Comunicações believes that the total amount of international traffic has grown in recent years principally because it has reduced traffic charges, developed new services and increased the capacity and quality of international services. International prices decreased on average by 0.4% over the course of 2002. With the introduction of full competition in the Portuguese fixed line telephone services market at the beginning of 2000, competitors may now provide international connections without using PT Comunicações' network. PT Comunicações has been encountering competitive pricing from new entrants to the international fixed line telephone services market. In 2002, the share of the market of our wireline businesses (including both PT Comunicações and PT Prime) in international traffic was approximately 76.7% compared with 76.3%

in 2001.

In percentage terms, PT Comunicações estimates that fixed line traffic accounted for approximately 54% of the Portugal Telecom group's total outgoing international traffic and approximately 63% of total incoming international traffic in 2002, as compared to 57% and 65% in 2001 and 67% and 71% in 2000, respectively. These reductions, which PT Comunicações expects to continue, are due to the growth of international mobile traffic and traffic originated on other fixed line operators in substitution for PT Comunicações' international fixed line telephone services. To the extent that PT Comunicações transmits outgoing or incoming calls for mobile networks, operating revenues from such international mobile traffic is accounted for in its wholesale services category. The costs of payments to other international operators are accounted for as costs of telecommunications. The increase in international mobile traffic contributed substantially in 2000, 2001 and 2002 to increases in wholesale operating revenues and the costs of telecommunications. See "Item 5 Operating and Financial Review and Prospects Results of Operations".

Accounting Rates. Historically, 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 2002 decreased by a weighted average of approximately 0.2% for incoming traffic and decreased by 25.4% for outgoing traffic as compared to the end of 2001.

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With the opening of competition in the Portuguese market 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 PT Comunicações' fixed line network. The revenues PT Comunicações receives from such services are interconnection fees and thus fall into the wholesale business category of its fixed line businesses. As a result, while its share of the international market has declined, increases in PT Comunicações' wholesale business have, to a substantial extent, offset this decline.

Prices. PT 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 1998 and the end of 2002, PT Comunicações experienced aggregate reductions in real terms of 42% in international traffic. These included an average reduction in nominal terms of 0.4% for international calls over the course of 2002.

The table below shows changes in prices for our international fixed line telephone services to selected destinations since 1998. The prices for 1998 through 2002 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,				
	1998	1999	2000	2001	2002
EU(2)	0.43	0.38	0.29	0.28	0.27
Other European countries(3)	0.78	0.70	0.67	0.63	0.61
United States	0.53	0.38	0.30	0.29	0.28
Canada	0.53	0.39	0.30	0.29	0.28
Brazil	0.95	0.70	0.67	0.59	0.57

(1) Euro amounts rounded to nearest hundredth.

(2)

Including Switzerland.

(3)

Excluding Norway and Iceland.

Wholesale Services. PT Comunicações' wholesale services consist of:

domestic and international interconnection telephone services that it provides 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 it began to provide to ISPs in Portugal, including ISPs in our group, in June 2001.

Consolidated operating revenues from PT Comunicações' wholesale services provided to companies outside our group were €269.2 million in 2002, €268.1 million in 2001 and €218.1 million in 2000.

Interconnection. Interconnection traffic comprises about 40% of PT Comunicações' wholesale business in terms of revenues. The service providers who purchase interconnection services include mobile telephone network operators, data communications providers, Internet service providers and

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value-added service providers. Providing interconnection services means allowing third parties to connect their networks to PT Comunicações' network, and vice versa. This interconnection is necessary, for example, to allow calls or data signals that originate on another network to terminate on PT Comunicações' network, and vice versa. Since the introduction of full competition into the Portuguese telecommunications market on January 1, 2000, PT Comunicações has 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 €0.82, single transit rates equal to €1.20 and double transit rates equal to €1.76, each based on a three-minute call made during peak hours. PT Comunicações also classifies value-added services, including audiotext services, on an interconnection basis. PT Comunicações published the latest version of its reference offer for unbundled access to our local loops on December 27, 2002, and since then has made available to its competitors, where technical and space conditions are available, all of the local switches, 14 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 its 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 Internet Interconnection*".

Leased Lines. PT Comunicações leases lines to other telecommunications providers for mobile and data communications services, including our 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 service involves 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 digital lines and higher to third parties in Portugal.

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The three current mobile telephone operators, our subsidiary TMN, Vodafone and Optimus, are among PT Comunicações' largest leased line customers. PT Comunicações leases lines to TMN and to our other subsidiaries PT Prime, Telepac and TV Cabo on a basis that does not discriminate against other customers. PT Comunicações expects that the opening of the Portuguese telecommunications market to competition and the entrance of new service providers will significantly increase its leased line services in the next few years. PT Comunicações also expects to face more competition from new leased line providers. This increased competition will probably cause it to reduce its leased line prices further.

PT Comunicações leased approximately 57,700 lines on a wholesale basis at the end of 2002 to other telecommunications service providers in Portugal, including other companies in our group. Compared with about 58,800 lines at the end of 2001, this represents a decrease of approximately 1.8%. PT Comunicações had 1,421,000 64 Kbps equivalent leased lines at the end of 2002, a decrease of 3.6% compared with 2001. The largest portion of wholesale leased lines is provided to mobile operators and data and Internet service providers. Of the total wholesale leased lines at the end of 2002, 98.6% were digital in terms of capacity.

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Traffic. Wholesale services traffic is generated by the interconnection portion of PT Comunicações' wholesale business. Its revenues from leased lines and television signal transmission do not depend on traffic levels. Domestic traffic generated by PT Comunicações' wholesale interconnection services increased by 3.2% in 2002 compared with 2001. This increase was primarily due to increases in indirect access traffic. The following table sets forth the total amount of wholesale services domestic traffic on PT Comunicações' fixed line network during the period 1998 through 2002.

Wholesale Services Domestic Traffic (millions of minutes)

	Year ended December 31,				
	1998	1999	2000	2001	2002
Mobile	763	1,192	1,172	1,061	998
Internet	1,100	2,800	5,630	6,916	6,687