

PORTUGAL TELECOM INTERNATIONAL FINANCE B.V.

(a private company with limited liability incorporated under the laws of The Netherlands and having its statutory seat in Amsterdam)

EUR750,000,000

4.125 per cent. Exchangeable Bonds due 2014

**Exchangeable for new and/or existing Ordinary Shares of
PORTUGAL TELECOM, SGPS, S.A.**

(Incorporated with limited liability in the Republic of Portugal)

Issue Price: 100.00 per cent.

The EUR750,000,000 4.125 per cent. Exchangeable Bonds due 2014 (the **Bonds**) of Portugal Telecom International Finance B.V. (the **Issuer**) will be exchangeable (subject as provided herein) for new and/or existing fully paid ordinary shares (the **Ordinary Shares**) of Portugal Telecom, SGPS, S.A. (**Portugal Telecom**), having at the Closing Date (as defined below) a nominal value of €0.03 each, at the then applicable Exchange Price at any time on or after 3 January 2009 and up to the close of business on 18 August 2014. The initial Exchange Price will be EUR13.9859 per Ordinary Share and will be subject to adjustment in certain circumstances described in “*Terms and Conditions of the Bonds – Exchange of Bonds*”. Notwithstanding the above, the Bonds shall be exchangeable, at the option of the Bondholders, prior to 3 January 2009 in the event of a Change of Control (as defined herein).

The Bonds do not constitute obligations of, nor are they guaranteed by, Portugal Telecom. However, each of Portugal Telecom and PT Comunicações, S.A. (**PTC** and, together with Portugal Telecom, the **Keep Well Providers** and each a **Keep Well Provider**) has entered into a separate Keep Well Agreement with the Issuer which are also for the benefit of the Trustee on behalf of the Bondholders (together, the **Keep Well Agreements** and each a **Keep Well Agreement**).

Application has been made to admit the Bonds to the official list of the Luxembourg Stock Exchange (the **Luxembourg Stock Exchange**) and application has been made to admit the Bonds to trading on the Luxembourg Stock Exchange’s Euro MTF Market (the **Euro MTF Market**). The existing Ordinary Shares are admitted to trading on Eurolist by Euronext Lisbon (**Euronext**). Eurolist is a regulated market for the purposes of Directive 93/22/EEC (the **Investment Services Directive**). The Issuer has agreed to use its best endeavours to ensure that the new Ordinary Shares issued or delivered upon exchange of any Bonds will be admitted to listing on Euronext.

The Bonds will bear interest from and including 28 August 2007 (the **Closing Date**) at the rate of 4.125 per cent. per annum. Interest on the Bonds is payable semi-annually in equal instalments in arrear on 28 February and 28 August in each year (each an **Interest Payment Date**), commencing on 28 February 2008. Unless previously purchased and cancelled, redeemed or exchanged, the Bonds will be redeemed at 100 per cent. of their principal amount on 28 August 2014.

The Bonds may be redeemed at the option of the Issuer in whole (but not in part) at their principal amount at such time, together with accrued interest (a) at any time on or after 11 September 2010 if the Parity Value (as defined herein), on each of at least 20 dealing days in any period of 30 consecutive dealing days ending not earlier than 14 days prior to the Issuer giving notice of the redemption, shall have exceeded 130 per cent. of the principal amount of a Bond on each such dealing day or (b) if exchanges and/or purchases and cancellations and/or redemptions have occurred in respect of 90 per cent. or more in principal amount of the Bonds originally issued.

An investment in the Bonds involves risks. See “Risk Factors” for a discussion of certain factors that should be carefully considered by investors.

None of the Bonds or the Ordinary Shares to be delivered upon exchange of the Bonds have been or will be registered under the United States Securities Act of 1933 (the **Securities Act**) or with any securities regulatory authority of any other jurisdiction. The Bonds are being offered and sold in offshore transactions outside the United States in reliance on Regulation S (**Regulation S**) under the Securities Act and, except in a transaction exempt from the registration requirements of the Securities Act, may not be offered, sold or delivered within the United States or to or for the benefit of U.S. persons.

The Bonds will initially be represented by interests in a global certificate in registered form without coupons attached (the **Global Certificate**) which will be deposited with a common depositary for, and registered in the name of a common nominee of, Euroclear Bank S.A./N.V. (**Euroclear**) and Clearstream Banking, société anonyme (**Clearstream, Luxembourg**) on or about 28 August 2007.

The Bonds have been rated BBB- by Standard & Poor’s and Baa2 by Moody’s. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

Joint Lead Managers

**BANCO ESPÍRITO SANTO
DE INVESTIMENTO, S.A.**

**MERRILL LYNCH
INTERNATIONAL**

**MORGAN STANLEY & CO.
INTERNATIONAL PLC**

Each of the Joint Lead Managers is acting for the Issuer and no one else in connection with the Offering and will not regard any other person (whether or not as a recipient of this document) as its client in relation to the Offering and will not be responsible to anyone other than the Issuer for providing the protections afforded to clients of the Joint Lead Managers, or for providing advice in relation to the Offering, the contents of this document or any transaction or arrangement or other matter referred to in this document.

The Issuer and each Keep Well Provider, having made all reasonable enquiries, confirm that this Offering Circular contains, or incorporates by reference, all information with respect to the Issuer, PTC, Portugal Telecom and its subsidiaries and affiliates taken as a whole (the **Group**), the Bonds and the Ordinary Shares available on exchange of the Bonds which is material in the context of the issue and offering of the Bonds (the **Offering**), the statements contained in this Offering Circular relating to the Issuer, each Keep Well Provider and the Group are true and accurate in all material respects and not misleading, the opinions, intentions and expectations expressed in this Offering Circular with regard to the Issuer, each Keep Well Provider and the Group are honestly held, have been reached after considering all relevant circumstances and are based on reasonable assumptions, there are no other facts in relation to the Issuer, each Keep Well Provider and the Group, the Bonds, the Ordinary Shares or the Keep Well Agreements, the omission of which would, in the context of the issue and offering of the Bonds, make any statement in this Offering Circular misleading, this Offering Circular does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements herein, in the light of the circumstances under which they were made, not misleading and all reasonable enquiries have been made by the Issuer and each Keep Well Provider to ascertain the facts, information and statements contained in this Offering Circular and to verify the accuracy of all such facts, information and statements. Each of the Issuer and each Keep Well Provider accepts responsibility accordingly. The Joint Lead Managers assume no responsibility for the accuracy or completeness of this Offering Circular.

This Offering Circular should be read and construed with any documents incorporated herein by reference.

This Offering Circular does not constitute an offer of, or an invitation by or on behalf of, the Issuer, either of the Keep Well Providers, or any of the Joint Lead Managers (as described herein), to subscribe for or purchase any of the Bonds or the Ordinary Shares. The distribution of this Offering Circular and the offering of the Bonds and the Ordinary Shares in certain jurisdictions may be restricted by law. No action has been or will be taken by the Issuer, the Keep Well Providers or the Joint Lead Managers to permit a public offering of the Bonds or the possession or distribution of this document (or any other offering or publicity materials or application form(s) relating to the Bonds) (i) in the United Kingdom, other than to (a) persons who have professional experience in matters relating to investments who fall within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the Order), (b) high net worth entities and other persons to whom it may otherwise lawfully be communicated falling within Article 49(1) of the Order or (c) persons to whom it may otherwise lawfully be communicated or (ii) in any other jurisdiction, where action for that purpose may be required. Persons into whose possession this Offering Circular comes are required by the Issuer, the Keep Well Providers and the Joint Lead Managers to inform themselves about and to observe any such restrictions. For a description of certain further restrictions on offers and sales of the Bonds and the Ordinary Shares and distribution of this Offering Circular, see "*Subscription and Sale*" below.

No person is authorised to give any information or to make any representation not contained in this Offering Circular and any information or representation not so contained must not be relied upon as having been authorised by or on behalf of the Issuer, either Keep Well Provider or any of the Joint Lead Managers. Neither the delivery of this Offering Circular nor any offer, sale or delivery made in connection with the issue of the Bonds shall, under any circumstances, constitute a representation that there has been no change or development likely to involve a change in the condition (financial or otherwise) of the Issuer, either Keep Well Provider or the Group since the date hereof or create any implication that the information contained herein is correct as of any date subsequent to the date hereof or the date as of which that information is stated herein to be given.

The investors acknowledge that: (i) they have not relied on the Joint Lead Managers or any person affiliated with the Joint Lead Managers in connection with any investigation of the accuracy of any information contained in this Offering Circular or their investment decision; and (ii) no person has been authorised to give any information or to make any representation concerning the Issuer, the Keep Well Providers, the Group or the Bonds (other than as contained in this Offering Circular) and, if given or made, any such other information or representation should not be relied upon as having been authorised by the Issuer, the Keep Well Providers or the Joint Lead Managers.

Neither the Issuer, the Keep Well Providers nor any of the Joint Lead Managers is providing any advice or recommendation in this Offering Circular on the merits of the purchase, subscription for, or investment in, the Bonds or the Ordinary Shares or the exercise of any rights conferred by the Bonds or the Ordinary Shares.

No representation or warranty, express or implied, is made by any of the Joint Lead Managers as to the accuracy, completeness or sufficiency of the information set out or incorporated in this Offering Circular, and nothing set out or incorporated in this Offering Circular is, or shall be relied upon as, a promise, representation or warranty by any of the Joint Lead Managers whether as to the past or the future. This Offering Circular (including the information incorporated by reference herein) is not intended to provide the basis of any credit or other evaluation and should not be considered as a recommendation by the Issuer, the Keep Well Providers, the Trustee or either of the Joint Lead Managers that any recipient of this Offering Circular should purchase the Bonds. Each potential purchaser of Bonds should determine for itself the relevance of the information set out or incorporated by reference in this Offering Circular and its purchase of Bonds should be based upon such investigations as it deems necessary.

None of the Issuer, the Keep Well Providers, the Joint Lead Managers or any of their respective representatives is making any representation to any offeree or purchaser of the Bonds regarding the legality of an investment in the Bonds by such offeree or purchaser under the laws applicable to such offeree or purchaser. Each investor should consult with his or her own advisors as to the legal, tax, business, financial and related aspects of a purchase of the Bonds.

IN CONNECTION WITH THIS ISSUE OF THE BONDS, MERRILL LYNCH INTERNATIONAL (THE STABILISING MANAGER) OR ANY PERSON ACTING ON BEHALF OF THE STABILISING MANAGER, MAY OVER-ALLOT AND EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE BONDS AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL. HOWEVER, THERE IS NO ASSURANCE THAT THE STABILISING MANAGER(S) (OR PERSONS ACTING ON BEHALF OF A STABILISING MANAGER) WILL UNDERTAKE STABILISATION ACTION. ANY STABILISATION ACTION SHALL BEGIN ON OR AFTER THE DATE ON WHICH ADEQUATE PUBLIC DISCLOSURE OF THE FINAL TERMS OF THE OFFER OF THE BONDS IS MADE AND, IF BEGUN, MAY BE ENDED AT ANY TIME, BUT IT MUST END NO LATER THAN THE EARLIER OF 30 DAYS AFTER THE CLOSING DATE AND 60 DAYS AFTER THE DATE OF THE ALLOTMENT OF THE BONDS. ANY STABILISATION ACTION OR OVER-ALLOTMENT MUST BE CONDUCTED BY THE RELEVANT STABILISING MANAGER(S) (OR PERSON(S) ACTING ON BEHALF OF ANY STABILISING MANAGER(S)) IN ACCORDANCE WITH ALL APPLICABLE LAWS AND RULES.

Unless otherwise specified or the context requires, references to (i) “EUR” “Euro” “euro” and “€” refer to the currency introduced at the start of the third stage of European economic and monetary union pursuant to the Treaty establishing the European Community, as amended and (ii) the “Company” or “PT” refers to Portugal Telecom.

TABLE OF CONTENTS

Documents Incorporated by Reference	4
Summary of the Bonds	6
Risk Factors	9
Terms and Conditions of the Bonds	23
Summary of Provisions relating to the Bonds while represented by a Global Certificate.....	56
Use of Proceeds	58
Relationship of the Issuer with Portugal Telecom SGPS, S.A. and PT Comunicações, S.A.	59
Portugal Telecom, SGPS, S.A.	65
Portugal Telecom International Finance B.V.....	135
PT Comunicações, S.A.	137
Description of Constitution and Share Capital of Portugal Telecom.....	140
Share Price History.....	148
Taxation.....	150
Subscription and Sale	156
General Information.....	159

DOCUMENTS INCORPORATED BY REFERENCE

Each document incorporated herein by reference is current only as at the date of such document, and the incorporation by reference of such documents shall not create any implication that there has been no change in the affairs of the Issuer, the Keep Well Providers or the Group, as the case may be, since the date thereof or that the information contained therein is current as at any time subsequent to its date. Any statement contained therein shall be deemed to be modified or superseded for the purposes of this Offering Circular to the extent that a subsequent statement contained herein modifies or supersedes that statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Offering Circular.

The documents set out below are incorporated herein by reference:

- (i) the annual report of the Issuer for the financial years ended 31 December 2005 and 31 December 2006;
- (ii) the annual report of Portugal Telecom for the financial years ended 31 December 2005, and 31 December 2006;
- (iii) the auditors report and audited annual financial statements of PTC for the financial years ended 31 December 2005 and 31 December 2006; and
- (iv) the report on Form 20 – F dated 29 June 2007 filed by PT with the United States Securities and Exchange Commission (the **Commission**).

The documents listed at (i) – (iii) above contain financial information on each of the Issuer and each of the Keep Well Providers, as described in the table below. Other information contained in such documents is incorporated by reference into this Offering Circular for information purposes only.

The document listed at (iv) above is incorporated by reference into this Offering Circular for information purposes only.

	Issuer	PT	PTC
Profit and Loss Account	<i>2005</i> Issuer Annual Report, page 6;	<i>2005</i> PT Annual Report, page 44;	<i>2005</i> PTC Financial Statements, page 4 – 5;
	<i>2006</i> Issuer Annual Report, page 5;	<i>2006</i> PT Annual Report, page 42;	<i>2006</i> PTC Annual Report, page 4 – 5;
Balance Sheet	<i>2005</i> Issuer Annual Report, page 5;	<i>2005</i> PT Annual Report, page 45;	<i>2005</i> PTC Financial Statements, pages 2 – 3;
	<i>2006</i> Issuer Annual Report, page 4;	<i>2006</i> PT Annual Report, page 43;	<i>2006</i> PTC Financial Statements, pages 2 – 3;
Cash Flow	<i>2005</i> N/A	<i>2005</i> PT Annual Report, page 47;	<i>2005</i> PTC Financial Statements, page 6
	<i>2006</i> N/A	<i>2006</i> PT Annual Report, page 45;	<i>2006</i> PTC Financial Statements, page 6;
Accounting policies and explanatory notes	<i>2005</i> Issuer Annual Report, pages 7 -12;	<i>2005</i> PT Annual Report, pages 48 -115;	<i>2005</i> PTC Financial Statements, pages 7 – 54;
	<i>2006</i> Issuer Annual Report, pages 6 -14;	<i>2006</i> PT Annual Report, pages 46 – 115;	<i>2006</i> PTC Financial Statements, pages 7 – 60;
Other Information	<i>2005</i> Issuer Annual Report, page 13;	<i>2005</i> PT Annual Report, pages 116-126;	<i>2005</i> N/A
	<i>2006</i> Issuer Annual Report, page 15;	<i>2006</i> PT Annual Report, page 116 – 126;	<i>2006</i> N/A
Audit reports	<i>2005</i> Issuer Annual Report, page 14;	<i>2005</i> PT Annual Report, page 129-131;	<i>2005</i> PTC Audit Report, pages 1-2
	<i>2006</i> Issuer Annual Report, pages 16-17;	<i>2006</i> PT Annual Report, page 129 – 130;	<i>2006</i> PTC Audit Report, pages 1-2;

Documents incorporated by reference into this Offering Circular will, for so long as any Bonds are outstanding, be available free of charge at the specified office of the Principal Paying, Transfer and Exchange Agent, at the registered offices of the Issuer and on the website of the Luxembourg Stock Exchange at *www.bourse.lu*.

Prospective investors are advised to obtain and read the documents incorporated by reference herein before making their investment decision in relation to the Bonds.

SUMMARY OF THE BONDS

The following is a summary of the principal features of the Bonds and the offering. Terms defined under "Terms and Conditions of the Bonds" or elsewhere in this Offering Circular shall have the same respective meanings in this summary. The following summary is qualified in its entirety by the more detailed information appearing elsewhere in this Offering Circular.

Issuer	Portugal Telecom International Finance B.V.
Keep Well Providers	Portugal Telecom, SGPS, S.A. and PT Comunicações, S.A.
The Bonds	EUR750,000,000 4.125 per cent. Exchangeable Bonds due 2014 exchangeable into Ordinary Shares of Portugal Telecom.
Keep Well Agreements	The Issuer's obligations in respect of the Bonds have not been guaranteed by, and do not constitute obligations of, either Keep Well Provider. However, each Keep Well Provider has entered into a separate Keep Well Agreement with the Issuer for the benefit of the Trustee, on behalf of the Bondholders (see " <i>Relationship of the Issuer with Portugal Telecom SGPS, S.A. and PT Comunicações, S.A.</i> "). The Keep Well Agreements do not provide the same rights as a guarantee, nor do they entitle the Trustee or Bondholders to make a claim against the relevant Keep Well Provider with regard to payments due in respect of the Bonds.
The Offering	The Bonds are being offered and sold by the Joint Lead Managers outside the United States in accordance with Regulation S under the Securities Act.
Issue Price	100 per cent. of the principal amount.
Denomination	EUR 50,000.
Closing Date	28 August 2007 (the Closing Date).
Interest Rate	The rate of interest payable on the Bonds will be 4.125 per cent. per annum. Interest will be payable on the Bonds semi-annually in equal instalments in arrear on 28 February and 28 August in each year (each an Interest Payment Date), commencing on 28 February 2008.
Status of the Bonds	The Bonds constitute direct, unconditional, unsubordinated and (subject to Condition 2) unsecured obligations of the Issuer and rank <i>pari passu</i> among themselves and (save for certain obligations required to be preferred by law) equally with all other unsecured obligations (other than subordinated obligations if any) of the Issuer from time to time outstanding.
Exchange Rights	Unless previously redeemed or purchased and cancelled, Bondholders will have the right to exchange each EUR50,000 principal amount of the Bonds for new and/or existing Ordinary Shares of Portugal Telecom at the then applicable Exchange Price at any time on or after 3 January 2009 and up to the close of business on 18 August 2014. The Bonds shall be exchangeable, at the option of the Bondholders, prior to 3 January 2009 in the event of a Change of Control (as defined herein).
Final Redemption	Unless previously redeemed or exchanged, the Bonds will be redeemed on 28 August 2014 (the Final Maturity Date) at 100 per cent. of their principal amount.
Optional Redemption by the Issuer	The Issuer will be entitled to redeem the outstanding Bonds, in whole but not in part, at their principal amount plus accrued interest due to the date fixed for redemption if (a) at any time on or

	<p>after 11 September 2010, the Parity Value on each of at least 20 dealing days in any period of 30 consecutive dealing days ending not earlier than 14 days prior to the Issuer giving notice of the redemption shall have exceeded 130 per cent. of the principal amount of a Bond on each such dealing day or (b) exchanges and/or purchases and cancellations and/or redemptions have occurred in respect of 90 per cent. or more in principal amount of the Bonds originally issued (including, for the avoidance of doubt, any Optional Bonds and any further Bonds consolidated and forming a single series with the Bonds at such date).</p>
Withholding Taxes	<p>Payments of interest by the Issuer under the Bonds shall be reduced by any withholding tax. See “<i>Taxation</i>”.</p>
Negative Pledge	<p>The Bonds will contain a negative pledge provision in respect of the Issuer and the Keep Well Providers as further described in “<i>Terms and Conditions of the Bonds – Negative Pledge</i>”.</p>
Cross Default	<p>The Bonds will contain a cross default provision, subject to a threshold of €20,000,000. See Condition 9 (<i>Events of Default and Enforcement</i>).</p>
Other Events of Default	<p>For a description of certain events that will permit acceleration of the Bonds, see Condition 9 (<i>Events of Default and Enforcement</i>). Upon acceleration for any such event, the Bonds will become immediately due and repayable at their principal amount, together with accrued but unpaid interest to such date.</p>
Governing Law	<p>The Bonds and the Trust Deed will be governed by, and construed in accordance with, English law.</p>
Trustee	<p>Citicorp Trustee Company Limited</p>
Principal Paying Agent	<p>Citibank N.A.</p>
Principal Transfer and Exchange Agent	<p>Citigroup Global Markets Deutschland AG & Co. KGaA</p>
Luxembourg Paying Agent, Luxembourg Transfer & Exchange Agent and Luxembourg Listing Agent	<p>Dexia Banque Internationale à Luxembourg</p>
Form of the Bonds and Delivery	<p>The Bonds will be in registered form without coupons attached and will be represented by a Global Certificate registered in the name of a nominee of, and deposited with a common depository for, Euroclear Bank S.A./N.V. (Euroclear) and Clearstream Banking, société anonyme (Clearstream Luxembourg) on or about the Closing Date.</p>
Sales Restrictions	<p>There are restrictions on offers and sales of the Bonds, <i>inter alia</i>, in the United States, the United Kingdom, the Netherlands and Portugal. See “<i>Subscription and Sale</i>”.</p>
Listing	<p>Application has been made to admit the Bonds to the official list of the Luxembourg Stock Exchange and to trading on the Euro MTF Market. The existing Ordinary Shares are listed on Euronext. The Issuer has agreed to use its best endeavours to ensure that the new Ordinary Shares issued or delivered upon exchange of any Bonds will be admitted to listing on Euronext.</p>
Lock up	<p>Portugal Telecom has agreed that for a period of 90 days commencing on 3 July, 2007 it will not and will; procure that none of its subsidiaries will (subject to certain exceptions) directly</p>

or indirectly, issue, offer, sell or otherwise transfer or dispose of any Ordinary Shares or any securities convertible into or exercisable or exchangeable for Ordinary Shares, or sell or grant options, rights or warrants with respect to any Ordinary Shares, or enter into agreements with the same economic results without the prior written consent of the Joint Lead Managers. See “*Subscription and Sale*”.

Ratings

The Bonds have been rated BBB- by Standard & Poor’s and Baa2 by Moody’s. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

ISIN

XS0309600848

Common Code

030960084

Use of Proceeds

The net proceeds of the issue of the Bonds will be used by Portugal Telecom and other entities in the Group for the Group’s general corporate purposes.

RISK FACTORS

The Issuer and each of the Keep Well Providers believe that the following factors may affect their respective ability to fulfil their respective obligations under the Bonds and/or the value of the Bonds and Ordinary Shares. All of these factors are contingencies which may or may not occur and neither the Issuer nor either of the Keep Well Providers is in a position to express a view on the likelihood of any such contingency occurring.

Factors which the Issuer and the Keep Well Providers believe may be material for the purpose of assessing the market risks associated with Bonds are also described below.

The Issuer and each Keep Well Provider believe that the factors described below represent the principal risks inherent in investing in the Bonds, but neither the Issuer nor the Keep Well Providers represent that the statements below regarding the risks of holding any Bonds are exhaustive. Prospective investors should also read the detailed information set out elsewhere in this Offering Circular (including any documents deemed to be incorporated by reference herein) and reach their own views prior to making any investment decision.

Terms used below but not defined shall have the meaning set out under “Terms and Conditions of the Bonds”.

Risks Relating to the Issuer and the Keep Well Providers

The Issuer is a funding vehicle for the PT Group

The Issuer is a funding vehicle for the Portugal Telecom group (**PT Group**). As such it raises finance in the international capital markets and finances the PT Group through the subscription of debt issued by entities belonging to the PT Group, namely Portugal Telecom, SGPS, S.A. In the event that such entities fail to meet their obligations under the debt issued, the Issuer may not be able to meet its payment obligations under the Bonds issued by it.

The Portuguese State holds all of PT's A shares

All of PT's 500 A shares are held by the Portuguese State. Under PT's articles of association, the Portuguese State, as the holder of all of PT's A shares, may veto a number of actions of PT's shareholders, including the following:

- authorization for the acquisition of ordinary shares representing more than 10 per cent. of the share capital by shareholders that directly or indirectly perform competing activities with those of the companies within a control relationship with Portugal Telecom, SGPS S.A;
- amendments to the by-laws and share capital increases, as well as the limitation or suppression of pre-emptive rights and the establishing of standards for share capital increases to be resolved by the Board of Directors;
- issuing of bonds or other securities, establishing the issue value for these securities to be resolved by the Board of Directors and limitation or suppression of pre-emptive rights in the issuing of bonds convertible into shares, as well as establishing the standards for the issuing of bonds of such nature to be resolved by the Board of Directors;
- the passing of resolutions on the application of the financial year results, in the event of a dividend distribution to the shareholders in a percentage superior to 40 per cent. of distributable profits;
- election of the chairman of the audit committee and the statutory auditor as well as the members of the General Meeting Board;
- approval of the general goals and fundamental principles of the Company's policies;
- definition of the general policy of shareholdings in companies, as well as, in the cases where authorized by a prior General Shareholders' Meeting, the passing of resolutions on the respective acquisitions and sales; and
- moving the Company's registered offices within the municipality of Lisbon or to a neighbouring municipality.

In addition, the election of one-third of the total number of directors, including the Chairman of the Board of Directors, requires the votes issued by the State, in its capacity as holder of Class A shares.

In April 2006, the European Commission sent to the Portuguese State a formal request to abandon the special rights it held as the sole owner of PT's A shares. The European Commission believes that the special powers granted to the Portuguese State through the sole ownership of PT's A shares act as a disincentive for investment by companies from other EU Member States in a manner that violates European Community Treaty rules. Should the Portuguese State not take satisfactory steps to remedy this alleged infringement of EU Law, the European Commission may decide to refer the case to the European Court of Justice.

PT's recent Ratings Downgrades and any Future Downgrades may impair PT's ability to obtain financing and may significantly increase its cost of debt

Immediately after the announcement by Sonaecom on 6 February 2006 of the tender offer for Portugal Telecom, Standard & Poor's placed PT's credit rating on CreditWatch with negative implications, while Moody's placed PT's credit rating on review for possible downgrade, due to the possible increased leverage that would result from the transaction. Following the presentation by PT's Board of Directors of an alternative shareholders' remuneration plan, increasing PT's indebtedness, Standard & Poor's and Moody's downgraded PT's ratings to BBB+ and Baa1, respectively, on 8 March 2006. On 3 August 2006, Standard & Poor's and Moody's downgraded PT's ratings to BBB- and Baa2, respectively, following the announcement of a further step-up in the shareholder remuneration plan. After the failure of the tender offer, the rating agencies confirmed PT's credit ratings as BBB- (Standard & Poor's) and Baa2 (Moody's), both with stable outlook.

PT has four loans from the European Investment Bank (EIB), totaling €364 million as of 30 June 2007, that contain a provision under which the EIB has the right to require PT to provide a guarantee acceptable to EIB in the event PT's ratings were downgraded to BBB/Baa2. In that circumstance, and after notice from the EIB, PT would have 60 days to present an acceptable guarantee. If PT fails to provide EIB with the required guarantee, the EIB would have the right to accelerate the repayment of the loans. As a result of PT's ratings downgrade on 3 August 2006 to BBB- by S&P, Baa2 by Moody's and BBB by Fitch, PT negotiated with EIB revised terms and conditions for these loans. The agreement with the EIB, signed on 23 February 2007, allows PT to present the guarantee mentioned above only in the case of a downgrade from the current rating (BBB- by S&P, Baa2 by Moody's and BBB by Fitch).

PT's recent ratings downgrades could adversely affect its ability to obtain future financing to fund its operations and capital needs. The downgrades could affect the marketability of any new debt securities PT may wish to issue. As part of the agreement with EIB described above, the spreads on PT's EIB loans increased by between 1 and 28 basis points, increasing its interest expenses. In addition, the downgrades could affect the pricing terms PT is able to obtain in any new bank financing or issuance of debt securities. In addition, any further downgrade of PT's ratings could have even more significant effects on its ability to obtain financing and consequently on its liquidity.

Portugal Telecom may not achieve its announced shareholder remuneration goals

In February 2007, in connection with its response to the tender offer by Sonaecom, Portugal Telecom announced a shareholder remuneration package comprised of a €2.1 billion share buyback, a €0.475 per share dividend related to the year 2006, a €0.575 per share dividend related to years 2007 and 2008, and the spin-off of PT Multimédia. As of 26 July 2007, PT has entered into equity swap agreements with several financial institutions in connection with its share buyback program for 69,689,692 shares, representing 6.17 per cent. of its share capital. In addition, shareholders of PT approved the spin-off of PT Multimédia at the annual general shareholders' meeting on 22 April 2007. However, the spin-off has not yet been completed and is subject to conditions.

The completion of the remaining shareholder remuneration goals will depend on PT's ability to continue to generate cash flow in its domestic businesses, assumes that PT is able to obtain regulatory relief for its domestic wireline business and that it is able to continue to streamline its operations to reduce our costs. In addition, the announced shareholder remuneration package assumes that the

exchange rate between the Euro and the Brazilian Real will remain stable. The Brazilian Real has fluctuated significantly in relation to the Euro in recent years. See “– *Macroeconomic Factors in Brazil – Fluctuations in the Real and increases in interest rates*”.

If any of the assumptions described in the preceding paragraph proves not to be the case or if any other circumstances (including any risks described in this “Risk Factors” section) impedes PT’s ability to generate cash and distributable reserves, investors may not receive the full remuneration PT has announced which could adversely affect the prevailing market price of the Ordinary Shares and the Bonds.

Competition from mobile Telephony and from other wireline operators

During 2006, approximately 30.1 per cent. of PT’s consolidated revenues were derived from services provided by PT’s wireline business in Portugal. As a result of the trend toward the use of mobile services instead of fixed telephone services, combined with the increase in competition from other wireline operators, PT has experienced, and may continue to experience, erosion of market share of both access lines and of outgoing domestic and international traffic. The number of active mobile telephone cards in Portugal has overtaken the number of wireline main lines, and more than 58 per cent. of the total Portuguese voice traffic is originated in mobile networks. Some of PT’s wireline customers are using mobile services as an alternative to wireline telephone services. Mobile operators can bypass PT’s international wireline network by interconnecting directly with wireline and mobile networks either in PT’s domestic network or abroad. Competition is also forcing down the prices of PT’s wireline telephone services for long distance and international calls. Lowering PT’s international call prices has caused a significant decline in PT’s revenues from international wireline telephone services.

The decrease in wireline traffic and lower tariffs resulting from competition has significantly affected PT’s overall revenues, and PT expects these factors to continue to negatively affect PT’s revenues.

After the Completion of the Proposed Spin-off of PT Multimédia, the Competitive Strategy of PT Multimédia could adversely affect PT’s Revenues and Cash Flows

Following the spin-off of PT Multimédia, PT Multimédia may develop a business strategy that could conflict with the strategies of PT’s wireline and domestic mobile businesses. In an attempt to gain market share in voice services, for example, PT Multimédia could pursue a price strategy that could place downward pressure on prices and adversely affect the revenues and cash flows of PT’s wireline and domestic mobile businesses. PT Multimédia has significant market share in its businesses, and it could be a strong competitor of PT’s wireline and domestic mobile businesses in Internet access and voice telephony after the completion of the proposed spin-off.

Development of Voice over Internet Protocol services

As existing Voice over Internet Protocol (“VoIP”) technology develops and new technologies emerge, competition from VoIP services is likely to intensify. VoIP has a significantly more advantageous cost structure when compared to Public Switched Telephony Networks (“PSTN”). Currently, some VoIP-based providers are able to offer cost-free calls between VoIP users, as well as call prices to PSTN and mobile networks at significant discounts to PT’s tariffs. Competition from VoIP-based operators is likely to increase price pressure on voice tariffs and reduce wireline and mobile traffic, which could harm significantly PT’s voice telephony revenues.

In addition, in November 2005, ANACOM began a period of consultation regarding regulation of these services, and issued a report on the subject in February 2006. Since then, some operators, including affiliates of Portugal Telecom, have launched fixed and roaming VoIP commercial services.

Reduced Interconnection Rates

In February 2005, ANACOM declared all mobile operators to have significant market power in call termination in the mobile networks market. ANACOM has accordingly imposed price controls on interconnection rates for the termination of calls on mobile networks. In 2005, interconnection rates (both fixed-to-mobile and mobile-to-mobile) were reduced by an average of 23.5 per cent. compared with 2004 rates. In 2006, these rates were further reduced by an average of 18.5 per cent. compared

to the 2005 rates. These reductions have had a significant impact on TMN's interconnection revenues and consequently its earnings. Both fixed-to-mobile and mobile-to-mobile interconnection rates reached €0.11 per minute in October 2006 and have not decreased since then. ANACOM is in the process of determining who has significant market power in call origination in the mobile networks market. PT cannot predict the outcome of this process, and ANACOM's decision could negatively impact PT's revenues and results of operations.

ANACOM's price controls on fixed-to-mobile interconnection have also negatively affected PT's wireline retail revenues because PT is required to reflect the reduction in these interconnection charges in its retail prices for calls from PT's fixed line network. PT expects that the reduction in interconnection charges will continue to have a significant impact on its wireline retail revenues.

In addition, the lower interconnection rates have also reduced revenues for PT's wholesale wireline business because PT's wholesale wireline unit records revenue from incoming operating calls through its network that terminate on the networks of mobile operators. The prices PT charges to international operators (and hence its revenues) depend on the interconnection fees charged by mobile operators for international incoming calls terminating on their networks, and these fees have been decreasing. PT expects that the lower interconnection rates in 2006 will continue to have a negative impact on its wholesale wireline revenues.

ANACOM issued a decision in December 2006 requiring PT's wireline business to offer flat rate interconnection, which PT believes will negatively affect its wholesale wireline revenues in the future.

Increased competition in the Portuguese mobile markets

PT operates in the highly competitive Portuguese mobile telecommunications market. PT believes that its existing mobile competitors, Vodafone and Optimus (owned by Sonae and France Telecom) will continue to market their services aggressively. In mid-2005, Optimus introduced a low-cost brand "Rede 4" in response to PT's new brand "Uzo". Vodafone also launched a product called Directo in mid-2005 targeting the same market as Uzo and Rede 4.

In addition, the commercial introduction in Portugal of third generation mobile services has heightened competition and reduced the profitability of providing third generation services. Moreover, ANACOM may open the mobile market to mobile virtual network operators ("MVNOs"), which do not have their own network infrastructure and thus would not have the fixed cost burdens facing PT's current GSM (Global System for Mobile Communications) and UMTS (Universal Mobile Telecommunications System) services. PT expects competition from VoIP-based operators also to place increasing price pressure on voice tariffs and lead to reductions in mobile traffic. Competition from companies providing wireless local-area network ("WLAN") services, which can deliver wireless data services more cheaply than UMTS in concentrated areas, may also affect the market and pricing for third generation services.

The broadband market in Portugal is highly competitive

At the end of 2006, PT had 685 thousand retail broadband subscribers using ADSL lines in PT's wireline business, which represented a growth of 17.1 per cent. over the number of broadband subscribers at the end of 2005. Some of PT's competitors have been improving their commercial offer in broadband Internet, with most of them offering triple-play bundled packages (voice telephony, broadband Internet and pay-TV subscription), including TV Cabo, a subsidiary of PT Multimédia, whose triple-play service will compete against that of PT's wireline business, especially after the completion of the proposed spin-off of PT Multimédia. PT believes that with competition in Internet broadband access intensifying, and with the development of existing technologies such as broadband wireless access and mobile broadband through UMTS, PT may face loss of market share in the broadband market, which could result in a loss of subscribers and a loss in revenues.

Regulatory Restrictions

The Portuguese electronic communications sector is now fully open to competition. However, many regulatory restrictions and obligations are still imposed on PT. ANACOM is conducting a market analysis to determine the regulatory obligations that should be imposed on operators with significant market power in the provision of electronic communications pursuant to a new EU

regulatory framework for electronic communications networks and services. In all but one of the 16 markets for which ANACOM has completed its analysis, the PT Group has been found by ANACOM to have significant market power and consequently is subject to regulatory restrictions and obligations. Not all of these obligations and restrictions have been imposed on other telecommunications operators and service providers. The substantial resources PT must commit to fulfill these obligations could adversely affect its ability to compete.

The European Commission's Review of Roaming Charges may lead to a reduction in Domestic Mobile Revenues

PT receives approximately 7.1 per cent. of its domestic mobile revenues from incoming and outgoing roaming charges. The European Commission has determined that roaming prices in Europe should be reduced and has published new regulations that have been effective since 30 June 2007. These regulations set maximum roaming charges that may be charged in the wholesale market and the retail market. In the wholesale market, a maximum roaming charge of €0.30 per minute will apply from the date two months after the effective date of the regulations through the first anniversary of the effective date, a maximum roaming charge of €0.28 per minute will apply in the second year, and a maximum roaming charge of €0.26 per minute will apply thereafter.

In the retail market, maximum roaming charges of €0.24 per minute (for received calls) and €0.49 per minute (for outgoing calls) will apply in the first year, maximum roaming charges of €0.22 per minute (for received calls) and €0.46 (for outgoing calls) will apply in the second year, and maximum roaming charges of €0.19 per minute (for received calls) and €0.43 per minute (for outgoing calls) will apply thereafter. Under the new regulations, operators must inform their customers of these charges within one month from the effective date of the regulations and give their customers a two month period to choose whether to be subject to these maximum charges or to an alternative pricing scheme offered by the operator.

PT believes these regulations will have an adverse effect on the revenues of its domestic mobile business and on the company as a whole.

In addition, within the EU regulatory framework for electronic communications approved in 2002, the Portuguese telecommunications regulator has been analysing concentrations of market power in various telecommunications markets in Portugal. Among the markets that the regulator has not yet analysed is the market for roaming charges, and it is expected to do so after the European Commission's decision on the regulation of roaming prices. This decision could lead to the introduction of further price controls, both in the retail and in the wholesale market, which could adversely affect the revenues and results of PT's domestic mobile business and of the company as a whole.

Regulatory investigations and litigation

PT is regularly involved in litigation and regulatory inquiries and investigations involving its operations. ANACOM, the European Commission and the Autoridade da Concorrência, the Portuguese competition authority, can make inquiries and conduct investigations concerning PT's compliance with applicable laws and regulations. Current inquiries and investigations include several complaints before the Autoridade da Concorrência relating to alleged anti-competitive practices in PT's wireline and multimedia businesses, including against:

- PT.com (this complaint was formerly against Telepac, which was merged into PT.com in December 2004) and TV Cabo regarding alleged anti-competitive practices in the broadband Internet market; and
- PTC for alleged anti-competitive practices in the public wireline telephone market and for granting discriminatory discounts on leased lines.

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

PT's wireline concession and licenses and authorisations for data, mobile and cable TV services

PT provides a significant number of services under a concession granted to PT by the Portuguese government and under licenses and authorisations granted to PT by ANACOM. The concession runs until 2025. The Portuguese government can revoke the concession after 2010 if it considers the revocation to be in the public interest. It can also terminate PT's concession at any time if PT fails to comply with its obligations under it. The Portuguese government can also terminate PT's licenses under certain circumstances. If the Portuguese government took such action, PT would not be able to conduct the activities authorised by the concession or the relevant licenses. This loss would eliminate an important source of PT's revenues.

Through TMN, we hold a renewable, non-exclusive license to provide traditional and GSM digital mobile telephone services throughout Portugal. The authorization for the use of GSM radio spectrum was renewed in December 2006 and is now valid until 2021.

Under the new regulatory framework set out in Law No. 5/2004, of February 10, 2004, the provision of cable television networks and services is subject only to a general authorization regime, which depends on the compliance with the rules provided for in the law and regulations. That is, the new framework does not require specific authorizations or licenses from ANACOM.

Currently, TV Cabo and its subsidiaries Cabo TV Açoreana and Cabo TV Madeirense, hold nine cable television authorizations to provide cable television services in 125 counties in continental Portugal and the Madeira and Azores Islands. All of these authorizations expire in May 2009 and will not be renewed, allowing the new regulatory framework to take effect.

Exchange Rate and interest rate fluctuations

PT is exposed to exchange rate fluctuation risks, mainly due to the significant level of PT's investments in Brazil. These investments are not hedged against exchange rate fluctuations. PT is required to make adjustments to its equity on its balance sheet in response to fluctuations in the value of foreign currencies in which PT has made investments. For example, as of 31st December 2006, cumulative foreign currency translation adjustments related to investments in Brazil were positive €652.3 million. A devaluation in the Brazilian Real in the future could result in negative adjustments to PT's balance sheet.

PT is also exposed to interest rate fluctuation risks. PT has entered into financial instruments to reduce the impact on its earnings of an increase in market interest rates, but these financial instruments may not prevent unexpected and material fluctuations of interest rates from having a material adverse effect on PT's earnings.

In addition, the purchase and sale of foreign currency in Brazil is subject to governmental control. In the past, the Central Bank has centralised certain payments of principal on external obligations. Many factors could cause the Brazilian government to institute a more restrictive exchange control policy, including, without limitation, the extent of Brazilian foreign currency reserves, the availability of sufficient foreign exchange, the size of Brazil's debt service burden relative to the economy as a whole and political constraints to which Brazil may be subject. A more restrictive policy could affect the ability of Brazilian debtors (including Vivo) to make payments outside of Brazil to meet foreign currency denominated obligations.

Macroeconomic factors in Brazil

A material portion of PT's 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. The major factors that could have a material adverse effect on PT's investments and results of operations in Brazil include:

Adverse political and economic conditions. The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. The Brazilian government has utilised salary and price controls, currency devaluation and foreign exchange controls as tools in its previous attempts to stabilise 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 PT's 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 PT's business.

Fluctuations in the Real and increases in interest rates. The Brazilian currency has historically experienced frequent devaluations. The Real devalued against the Euro by 12.8 per cent. in 2001 and by 81.4 per cent. in 2002. During 2002, the Real underwent significant devaluation due in part to political uncertainty in connection with the elections and the global economic slowdown. In the period leading up to, and after, the general election in 2002, there was substantial uncertainty relating to the policies that the new government would pursue, including the potential implementation of macroeconomic policies that would differ significantly from those of the prior administration. This uncertainty resulted in a loss of confidence in the Brazilian capital markets and the continued devaluation of the Real until the end of 2002. The Real appreciated against the Euro by 1.4 per cent. and 31.7 per cent. in 2004 and 2005 respectively, and depreciated against the Euro by 1.97 per cent in 2006. In the first six months of 2007 the Real appreciated against the Euro by 7.4 per cent. Any substantial negative reaction to the policies of the Brazilian government could have a negative impact, including devaluation. The devaluation of the Real could negatively affect the stability of the Brazilian economy and accordingly could negatively affect the profitability and results of PT's operations. It would also increase costs associated with financing PT's 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. PT's operations in Brazil rely on imported equipment and, as a result of such devaluation, such equipment would be more expensive to purchase.

During 2004 and 2005, the Brazilian Central Bank tightened its monetary policy to contain inflationary pressures resulting from high international prices for oil and other commodities, and increased the SELIC basic interest to 17.75 per cent. at the end of 2004 and to 18.00 per cent. at the end of 2005. Since then, the Brazilian Central Bank has eased its monetary policy, decreasing the SELIC basic interest rate to 13.25 per cent. at the end of 2006. However, an increase in interest rates could negatively affect PT's profitability and results of operations and would increase the costs associated with financing PT's operations in Brazil. In addition, an increase would raise PT's interest costs because most of the interest on Vivo's debt 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 organisation, reflected inflation of 3.8 per cent. in 2006, compared to 1.2 per cent. in 2005, 12.1 per cent. in 2004, 7.7 per cent. in 2003 and 26.4 per cent. in 2002. If Brazil experiences significant inflation, Vivo may be unable to increase service rates to its customers in amounts that are sufficient to cover its increasing operating costs, and its business may be adversely affected, which could in turn have an adverse effect on PT's results of operations.

PT could be required to record impairment charges relating to goodwill for PT's investment in Vivo. Under IFRS, PT is required to test PT's goodwill for impairment at least annually. If the carrying value of the goodwill exceeds the related recoverable amount, PT is required to write down PT's goodwill. The recoverable amount is the higher of the estimated selling price of the asset less the related selling costs and value in use. An increase in interest rates or other macroeconomic events (or an adverse event affecting the operations of Vivo) could decrease the estimated future cash flows from PT's investment in Vivo. An event that causes PT to reduce PT's estimates of the future cash flows of Vivo could require PT to record an impairment of this goodwill and, depending on the size of the impairment, this could have a material adverse effect on PT's balance sheet and PT's results of operations.

PT's joint venture with Telefónica

The successful implementation of PT's strategy for PT's mobile operations in Brazil depends on the development of PT's mobile services joint venture company with Telefónica Móviles. On 27 December 2002, PT and Telefónica Móviles (which has since merged into Telefónica) transferred their direct and indirect interests in Brazilian mobile operators to the mobile services joint venture company Brasilcel, operating under the brand name Vivo, with headquarters in the Netherlands.

As in any joint venture, it is possible that Telefónica and PT will not agree on Vivo's strategy, operations or other matters. Any inability of Telefónica and PT to operate Vivo jointly could have a negative impact on Vivo's operations, which could have a negative impact on PT's strategy in Brazil and could have a material adverse effect on PT's results of operations. In addition, PT cannot be sure that Vivo will be able to take advantage of its position in the Brazilian market to increase the scope and scale of its operations or that any anticipated benefits of the joint venture will be realised.

Regulation in Brazil

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

Brazilian Tax Reforms may affect Vivo's prices

The Brazilian government has proposed tax reforms that are currently being considered by the Brazilian Congress. If Vivo experiences a higher tax burden as a result of the tax reform, it may have to pass the cost of that tax increase on to its customers. This increase may have a material negative impact on the dividends paid by Vivo's subsidiary to it and on its revenues and operating results.

Conditions applying to Vivo's subsidiaries under the SMP licensing regime

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

In 2003, SMP operators were required to implement long distance carrier selection codes to allow customers to choose their carrier for domestic long distance services (for both "VC2" and "VC3" calls) and international cellular calls. VC2 calls are calls made to parties outside a caller's area code but inside the same state, and VC3 calls are calls made to parties outside the caller's state. As a result, Vivo's subsidiaries no longer receive revenues from long distance services but instead receive revenues from interconnection fees paid by wireline long distance operators for wireline long distance traffic originating and terminating on their networks. The interconnection fees do not fully compensate, however, for the loss of long distance revenues that Vivo's subsidiaries formerly received from VC2 and VC3 calls, and this has had a negative impact on the overall revenues of Vivo's subsidiaries. If Vivo were able to offer wireline long distance services in addition to mobile services, it might be able to mitigate the impact of carrier selection codes on its revenues. However, because ANATEL considers Vivo's subsidiaries to be affiliated with Telefónica, which provides wireline long distance services in the state of São Paulo and was awarded a licence to provide such services nationwide, ANATEL will not award a wireline long distance licence to any of Vivo's subsidiaries.

Interconnection fees and regulated adjustments to interconnection fees

Under the new SMP regime, interconnection fees for the termination of calls on mobile networks are determined through free negotiation between Vivo's subsidiaries and other

telecommunications operators. If the parties do not reach an agreement, the matter is determined through arbitration, which is conducted by ANATEL. Interconnection agreements must be approved by ANATEL and may be rejected if they are contrary to the principles of free competition and applicable regulations relating to traffic capacity, use of the interconnection infrastructure by requesting parties and other matters.

In 2005, ANATEL approved provisional agreements among the local fixed line and mobile operators to determine the interconnection fees for local calls (known as “VC1” calls). These agreements provide for a 4.5 per cent. annual adjustment of interconnection fees for these calls. In March 2006, ANATEL approved a provisional agreement for interconnection fees for VC2 and VC3 long distance calls that also provides for a 4.5 per cent. annual adjustment to interconnection fees. The annual adjustments under these agreements may not be sufficient to cover Vivo’s costs and preserve its margins from interconnections with Vivo’s network. In particular, because a significant number of mobile subscribers use prepaid mobile services and generally receive more calls than they make, Vivo’s subsidiaries derive an important part of their revenues from the interconnection fees paid to them by the wireline operators for traffic originating on wireline networks and terminating on the subsidiaries’ mobile networks.

In addition, ANATEL may further modify the regulatory regime governing interconnection fees. ANATEL has proposed to replace the partial Bill & Keep regime with a model based on the costs of mobile operators. ANATEL has proposed to implement this new model in mid-2007. PT cannot predict whether this proposed model will be implemented and whether it will have an adverse effect on PT’s operations. If this model were to result in lower annual adjustments to interconnection fees than under the provisional agreements reached in 2005 described above, PT’s revenues and results of operations could be adversely affected. In July 2006, the partial Bill & Keep regime was discontinued, and now Vivo is under a “full billing” regime.

ANATEL has also published specific proposals for regulations regarding interconnection charges that could adversely affect Vivo’s revenues and results of operations. These proposals include (1) a proposal that two SMP operators controlled by the same economic group receive only one interconnection charge for calls originated and terminated on their networks rather than the current two charges, (2) a proposal for new negotiation rules for interconnection charges under which ANATEL would have a role in determining the charges rather than the current free negotiation of the charges and (3) a proposal for interconnection charge unification among SMP providers of the same economic group having significant market power according to criteria still to be defined. If new regulations along these lines take effect, they could have an adverse effect on Vivo’s results of operations because (A) interconnection charges could drop significantly, thereby reducing Vivo’s revenues, (B) ANATEL may allow favourable prices for economic groups without significant market power and (C) the prices Vivo charges in some regions in which it operates are higher than those in some other regions, and consolidation of those prices, competitive pressures and other factors could reduce Vivo’s average prices and its revenues.

Vivo’s competition

Competition may continue to intensify for Vivo as a result of the strategies of existing competitors, the possible entrance of new competitors and the rapid development of new technologies, products and services. Vivo’s ability to compete successfully will depend on its marketing techniques and on its ability to anticipate and respond to various competitive factors affecting the industry, including new services that may be introduced, changes in consumer preferences, demographic trends, economic conditions and discount pricing strategies by its competitors. If Vivo does not keep pace with technological advances, or if it fails to respond timely to changes in competitive factors in its industry, it could continue to lose market share, and Vivo and PT could suffer a decline in PT’s revenue. Competition from other SMP communications service providers in the regions in which Vivo operates has also affected, and may continue to affect, its financial results by causing, among other things, a decrease in its customer growth rate, decreases in prices and increases in selling expenses.

These factors have already contributed to a negative effect on Vivo’s market share and results of operations and could have a material adverse effect on PT’s results of operations in the future. As

a result of competitive pressures, for example, Vivo's market share in the regions where it operates decreased from 40.4 per cent. as of 30 June 2006 to 37.3 per cent. as of 30 June 2007.

Recently, there has been consolidation in the Brazilian telecommunications market. In this regard, on 2 August 2007 Vivo signed a stock purchase agreement with Telpart Participações S.A. to acquire control of Telemig Celular Participações S.A. and Tele Norte Celular Participações S.A. (see "*Portugal Telecom, SGPS, S.A – Brazilian Mobile Business*"). The conclusion of the transaction is subject to the approval of ANATEL and ratification by the general shareholders' meetings of Vivo and Telpart, among other customary closing conditions, and there can be no certainty that such approvals and ratifications will be granted and that the closing conditions will be satisfied.

PT believes that this trend of consolidation may continue, and notwithstanding Vivo's proposed acquisition, consolidation may result in increased competitive pressures within Vivo's market. Vivo may be unable to respond adequately to pricing pressures resulting from consolidation, which would adversely affect its business, financial condition and results of operations and could adversely affect PT's results of operations.

Vivo's customer growth decreases and customer turnover increases

Vivo's rate of acquisition of new customers has declined significantly, primarily due to competition and increased market penetration. For example, Vivo's net additions of customers decreased to a loss of 752,000 customers in 2006, as compared to a gain of 3,262,000 customers in 2005. This negative evolution was mainly due to a decrease in the rate of addition of new prepaid customers, with a loss of 517,373 customers in 2006, compared to the addition of 2,703,995 new prepaid customers in the prior year. This decrease in the rate of new additions of customers has negatively affected Vivo's results of operations and could continue to do so in the future. In addition, if Vivo's rate of customer turnover were to increase significantly, its results of operations and or competitive position could be adversely affected. Several factors in addition to competitive pressures could influence Vivo's rate of acquisition of new customers and rate of customer turnover, including limited network coverage, lack of sufficient reliability of services and economic conditions in Brazil.

Risks Relating to PT Multimédia

The risks relating to PT Multimédia below relate to PT Multimédia's ongoing operations prior to the completion of the proposed spin-off of PT Multimédia.

The spin-off proposal approved by the shareholders grants the Board of Directors the authority to determine all the terms and conditions of the spin-off to the extent not otherwise contained in the shareholder approval. These terms and conditions are expected to include non-opposition from the competent regulatory authorities, including the Portuguese Securities Commission (*Comissão do Mercado de Valores Mobiliários – CMVM*), and Portugal Telecom cannot assure investors that these conditions will be met or that they will be met on a timely basis. In addition, the implementation of the proposal will be subject to market conditions and the financial and accounting situation of Portugal Telecom. The spin-off also involves the suppression of the special rights attributed to the class A shares of PT Multimédia held by Portugal Telecom by means of their conversion into ordinary shares or by other means, but Portugal Telecom cannot provide any assurance that this condition will be met.

PT Multimédia's success depends on its ability to offer new products and services and to keep up with advances in technology

PT Multimédia has introduced and continues to introduce new products and services, such as high speed Internet access via cable and TV services, including improving channel offer and introducing services through digital signal transmission. If it is not successful in marketing and selling such products and services, its business, financial position and results of operations may be harmed. In addition, PT Multimédia cannot be sure that there will be adequate demand for its system upgrades or new product and service offerings. Because technology changes very rapidly, it is not possible to ensure that the technology PT Multimédia uses or will use in offering its products and services will not be rendered obsolete by new and superior technology. In addition, many of the new products and services that PT Multimédia intends to offer may also be offered by its competitors.

Therefore, these new products and services may fail to generate revenue or attract and retain the level of customers that PT currently anticipates.

PT Multimédia is subject to competition in each of its business areas, which is expected to intensify

PT Multimédia faces competition in all its business areas. As existing technology develops and new technologies emerge, competition is likely to intensify in all these areas, particularly with regard to products and services related to subscription TV and Internet. PT Multimédia's cable and satellite TV services face competition from broadband local loop access based on broadband wireless access. In 2005, AR Telecom (formerly Jazztel), a direct competitor of Portugal Telecom's wireline business, launched broadband wireless access service in Lisbon and Oporto and is expected to invest considerably in its network in the coming years. Video over ADSL is also expected to be a competitor of PT Multimédia's television services. Sonaecom, a direct competitor of Portugal Telecom's wireline business, has launched an IP television offer that competes with PT Multimédia's television services. When licenses are granted in the future, terrestrial digital television will be a direct competitor of PT Multimédia's subscription TV business. In its audiovisuals business, PT Multimédia also faces competition at the film distribution, film rights marketing and film screening levels. If PT Multimédia is unable to compete successfully, its business, financial position and results of operations could be significantly harmed. See "*Portugal Telecom, SGPS, S.A – Competition – Competition Facing PT Multimédia's Pay TV and Broadband Internet Business*" and "*– Competition Facing PT Multimédia's Audiovisuals Business*".

Regulatory investigations may lead to fines or other penalties

In September 2005, the Autoridade da Concorrência brought allegations against PT Multimédia and TV Cabo for practices allegedly in violation of Article 4 of Law 18/2003 (the Portuguese Competition Law) following the execution in 2000 of a partnership agreement among PTM, TV Cabo and SIC-Sociedade Independente de Comunicação, S.A. (SIC) in connection with SIC's acquisition of Lisboa TV-Informação e Multimédia, S.A. In response to this accusation, PT Multimédia and TV Cabo contested the allegations of the Autoridade da Concorrência. However, in August 2006, the Autoridade da Concorrência imposed a fine of €2.5 million on PT Multimédia. PT Multimédia and TV Cabo appealed to the Commerce Court of Lisbon on 8 September 2006, and consequently the decision of Autoridade da Concorrência was suspended. On 14 August 2007, PTM was notified of the Commerce Court's decision pursuant to the appeal procedure. According to such decision, the Commerce Court declared the decision of the Autoridade da Concorrência null and void and, accordingly, declared that the Autoridade da Concorrência should commence new proceedings solely.

Risks Relating to the Bonds

Bonds may not be a suitable investment for all investors

Each potential investor in any Bonds must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- (i) have sufficient knowledge and experience to make a meaningful evaluation of the Bonds, the merits and risks of investing in the Bonds and the information contained or incorporated by reference in this Offering Circular;
- (ii) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Bonds and the impact such investment will have on its overall investment portfolio;
- (iii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the Bonds;
- (iv) understand thoroughly the terms of the Bonds; and
- (v) be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

A potential investor should not invest in the Bonds, which are complex financial instruments, unless it has the expertise (either alone or with the help of a financial adviser) to evaluate how the

Bonds will perform under changing conditions, the resulting effects on the value of such Bonds and the impact this investment will have on the potential investor's overall investment portfolio.

Risks Attached to the Exercise of Exchange Rights

Investors should be aware that the Bonds, which are exchangeable into Ordinary Shares, bear certain additional risks. Depending on the performance of the underlying Ordinary Shares, the value of Ordinary Shares may be substantially lower than when the Bonds were initially purchased. In addition, the value of the Ordinary Shares to be delivered upon conversion of Bonds may vary substantially between the date on which exchange rights are exercised under the Bonds and the date on which such Bonds and Ordinary Shares are delivered. Although the Issuer may deliver or procure the delivery of existing issued Ordinary Shares upon exercise of Exchange Rights, rather than newly issued Ordinary Shares, there is no obligation on the Issuer to do so.

In view of the requirements under Portuguese law for completing various formalities required in connection with an issue of share capital, Bondholders should be aware that it may take approximately 60 days, following the exercise of Exchange Rights, for newly issued Ordinary Shares to be delivered to the relevant Bondholder. As a result, Bondholders exercising Exchange Rights may not be able to sell or otherwise transfer or dispose of, or exercise any rights in relation to, the Ordinary Shares to which they are entitled upon such exercise for a material period following such exercise. However, there can be no assurances that if newly issued Ordinary Shares are to be delivered to a holder upon exercise of Exchange Rights that those Ordinary Shares will be issued and delivered, and, consequently the Registration Date will occur, within a 60 day period following such exercise. See "*Terms and Conditions of the Bonds – Exchange of Bonds*".

There is a Limited Period for, and Costs Associated with, the Exercise of Exchange Rights

A Bondholder will, subject as more fully described herein under "Terms and Conditions of the Bonds", have the right to exchange his or her Bonds into Ordinary Shares. Exchange Rights may be exercised, subject as provided herein, at any time on or after 3 January 2009 up to the close of business on 18 August 2014. If the Exchange Rights are not exercised by Bondholders during the Exchange Period, the Bonds will be redeemed at their principal amount, together with accrued but unpaid interest to such date on 28 August 2014, unless the Bonds are previously purchased and cancelled or redeemed in accordance with the Conditions.

Bondholders Have Limited Anti-dilution Protection

The Bonds are exchangeable into Ordinary Shares. The Exchange Price at which the Bonds may be exchanged into Ordinary Shares will be adjusted in the event that there is a consolidation, reclassification or subdivision, capitalisation of profits, distribution, rights issue or grant of other subscription rights or other adjustment, including a spin-off event which affects the Ordinary Shares, but only in the situations and only to the extent provided under "Terms and Conditions of the Bonds – Conversion of Bonds". There is no requirement that there should be an adjustment for every corporate or other event that may affect the value of the Ordinary Shares. Events in respect of which no adjustment is made may adversely affect the value of the Ordinary Shares and, therefore, adversely affect the value of the Bonds.

Modification, waivers and substitution

The Conditions contain provisions for calling meetings of Bondholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Bondholders including Bondholders who did not attend and vote at the relevant meeting and Bondholders who voted in a manner contrary to the majority.

The Conditions also provide that the Trustee may, without the consent of Bondholders, agree to any modification of, or to the waiver or authorisation of any breach or proposed breach of, any of the provisions of the Bonds, in the circumstances described in Condition 13.2 of the Conditions.

Change of law

The Conditions are based on English law in effect as at the date of this Offering Circular. No assurance can be given as to the impact of any possible judicial decision or change to English law or administrative practice after the date of this Offering Circular.

Risks related to the market generally

The Bonds may not have an active trading market

Although it is expected that the Bonds will be listed on the Luxembourg Stock Exchange and traded on the Euro MTF Market on or after the Closing Date, there may be little or no secondary market for the Bonds. Even if a secondary market for the Bonds develops, it may not provide significant liquidity and it is expected that transaction costs in any secondary market may be high. As a result, the difference between bid and ask prices for the Bonds in any secondary market could be substantial.

Limited Liquidity on Euronext

The principal trading market for the Ordinary Shares is Euronext. Euronext is less liquid than major markets in Western Europe and the United States. As a result, Bondholders may have difficulty assessing the past performance of the Ordinary Shares based on the Portugal Telecom's prior trading record on Euronext. Portugal Telecom cannot provide assurances about the future liquidity of the market for the Ordinary Shares.

Credit ratings may not reflect all risks

Standard & Poor's and Moody's have assigned credit ratings to the Bonds. The ratings may not reflect the potential impact of all risks related to structure, market, additional factors discussed above, and other factors that may affect the value of the Bonds. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time.

Further issues or sales of Ordinary Shares

There can be no certainty as to the effect, if any, that future issues or sales of Ordinary Shares, or the availability of such Ordinary Shares for future issue or sale, would have on the market price of the Ordinary Shares prevailing from time to time and therefore on the price of the Bonds. Although Portugal Telecom has agreed not to, and Portugal Telecom will procure that none of its Subsidiaries or any other party acting on its behalf will, subject to certain exceptions, directly or indirectly, issue, offer, sell or otherwise transfer or dispose of any Ordinary Shares or any securities convertible into or exercisable or exchangeable for Ordinary Shares, or sell or grant options, rights or warrants with respect to any Ordinary Shares, or enter into agreements with the same economic results, without the prior written consent of the Joint Lead Managers (see "Subscription and Sale"), for a period of 90 days from 3 July 2007, sales of substantial numbers of Ordinary Shares in the public market, or a perception in the market that such sales could occur, could adversely affect the prevailing market price of the Ordinary Shares and the Bonds.

Exchange rate risks and exchange controls

The Issuer will pay principal and interest on the Bonds in Euro. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the **Investor's Currency**) other than Euro. These include the risk that exchange rates may significantly change (including changes due to devaluation of Euro or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to Euro would decrease (1) the Investor's Currency-equivalent yield on the Bonds, (2) the Investor's Currency-equivalent value of the principal payable on the Bonds and (3) the Investor's Currency-equivalent market value of the Bonds.

Government and monetary authorities may impose (as some have done in the past) exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal.

Interest rate risks

Investment in the Bonds involves the risk that subsequent changes in market interest rates may adversely affect the value of the Bonds.

Legal investment considerations may restrict certain investments

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (1) the Bonds are legal investments for it, (2) the Bonds can be used as collateral for various types of borrowing and (3) other restrictions apply to its purchase or pledge of the Bonds. Financial institutions should consult their legal advisors or the appropriate regulators to determine the appropriate treatment of the Bonds under any applicable risk-based capital or similar rules.

TERMS AND CONDITIONS OF THE BONDS

The following, subject to completion and amendment, and save for the paragraphs in italics, is the text of the Terms and Conditions of the Bonds which will be endorsed on each Bond in definitive form.

The issue of the €750,000,000 4.125 per cent. Exchangeable Bonds due 2014 (the **Bonds**, which expression shall, unless otherwise indicated, include any Further Bonds) was authorised by a resolution of the management board of Portugal Telecom International Finance B.V. (the **Issuer**) passed on or prior to 28 August 2007. The Bonds are constituted by a trust deed dated 28 August 2007 (the **Trust Deed**) between the Issuer, Portugal Telecom, SGPS, S.A. (**Portugal Telecom**), PT Comunicações, S.A. (**PTC**) and Citicorp Trustee Company Limited (the **Trustee**, which expression shall include all persons for the time being appointed as the trustee or trustees under the Trust Deed) as trustee for the holders (as defined below) of the Bonds. The statements set out in these Terms and Conditions (the **Conditions**) are summaries of, and are subject to, the detailed provisions of the Trust Deed, which includes the forms of the Bonds. The Bondholders (as defined below) are entitled to the benefit of, and are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and those provisions applicable to them which are contained in the Paying, Transfer and Exchange Agency Agreement dated 28 August 2007 (the **Agency Agreement**) relating to the Bonds between, *inter alia*, the Issuer, Portugal Telecom, the Trustee, Citibank, N.A. (the **Principal Paying Agent**, which expression shall include any successor as principal paying agent under the Agency Agreement), Citigroup Global Markets Deutschland AG & Co. KGaA (the **Principal Transfer and Exchange Agent**, which expression shall include any successor as principal transfer and exchange agent under the Agency Agreement), the paying agents and the transfer and exchange agents for the time being (such persons, together with the Principal Paying Agent and the Principal Transfer and Exchange Agent, being referred to below as the **Agents**, which expression shall include their successors as Agents under the Agency Agreement) and Citigroup Global Markets Deutschland AG & Co. KGaA in its capacity as registrar (the **Registrar**, which expression shall include any successor as registrar under the Agency Agreement). Copies of each of the Trust Deed and the Agency Agreement are available for inspection at the office of the Trustee at 14th Floor, Citigroup Centre, Canada Square, Canary Wharf, London E14 5LB, and at the specified offices of the Agents and the Registrar.

The Bonds have the benefit of a Keep Well Agreement between the Issuer and Portugal Telecom dated 28 August 2007 and a Keep Well Agreement between the Issuer and PTC dated 28 August 2007 (together, the **Keep Well Agreements**). References herein to the **Keep Well Providers** shall mean both Portugal Telecom and PTC and Keep Well Provider shall mean either of them.

Capitalised terms used but not defined in these Conditions shall have the meanings attributed to them in the Trust Deed unless the context otherwise requires or unless otherwise stated.

1. FORM, DENOMINATION, TITLE AND STATUS

1.1 Form and Denomination

The Bonds are in registered form, serially numbered, in principal amounts of €50,000 or integral multiples thereof (**authorised denominations** and each an **authorised denomination**).

1.2 Title

Title to the Bonds will pass by transfer and registration as described in Condition 4. The holder (as defined below) of any Bond will (except as otherwise required by law or as ordered by a court of competent jurisdiction) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest in it or its theft or loss (or that of the related certificate, as appropriate) or anything written on it or on the certificate representing it (other than a duly executed transfer thereof)) and no person will be liable for so treating the holder.

1.3 Status of the Bonds

The Bonds constitute direct, unconditional, unsubordinated and (subject to Condition 2) unsecured obligations of the Issuer and rank *pari passu* among themselves and (subject as aforesaid and save for certain obligations required to be preferred by law) equally with all other unsecured obligations (other than subordinated obligations if any) of the Issuer from time to time outstanding.

1.4 Keep Well Agreement

In each of the Keep Well Agreements, the relevant Keep Well Provider has covenanted and agreed with the Issuer, and also for the benefit of the Trustee on behalf of the Bondholders (i) to cause the Issuer to maintain a Tangible Net Worth (as defined below), as determined in accordance with generally accepted accounting principles in the Netherlands applied on a consistent basis as shown on the Issuer's most recent audited balance sheet (commencing with the Issuer's audited balance sheet at 31 December 2006), of at least €1; and (ii) that if the Issuer at any time shall have insufficient funds or other liquid assets to meet its payment obligations (including in respect of the Bonds) or to repay borrowings then maturing or subsequently to mature, then upon receipt of notice from the Issuer to such effect, the relevant Keep Well Provider shall make available to the Issuer, before the due date of such payment obligations or borrowings, funds sufficient to enable the Issuer to meet such payment obligations or to repay such borrowings, as the case may be, in full as they fall due. In addition, Portugal Telecom has covenanted and agreed with the Issuer, and also for the benefit of the Trustee on behalf of the Bondholders to take all steps possible to cause the Issuer to exchange the Bonds pursuant to the terms hereof into Ordinary Shares.

2. NEGATIVE PLEDGE

So long as any of the Bonds remain outstanding (as defined in the Trust Deed) neither the Issuer nor the Keep Well Providers will create or, save only by operation of law, have outstanding any mortgage, lien, pledge or other charge (each a **Security Interest**) other than any Permitted Security (as defined below) upon the whole or any part of its undertaking or assets, present or future (including any uncalled capital), to secure any Loan Stock of any Person (as defined below) or to secure any obligation of any Person under any guarantee of or indemnity or purchase of indebtedness undertaking in respect of any Loan Stock of any other Person without at the same time or prior thereto at the option of the Issuer or the relevant Keep Well Provider, as applicable, either (i) securing the Bonds equally and rateably therewith or (ii) providing such other security for or other arrangement in respect of the Bonds as either (a) in any such case the Trustee shall in its absolute discretion deem not materially less beneficial to the interests of the Bondholders or (b) shall be approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Bondholders.

For the purposes of these Terms and Conditions:

Loan Stock means indebtedness having an original maturity of more than one year which is in the form of, or represented or evidenced by, bonds, notes, debentures, loan stock or other debt securities (not comprising, for the avoidance of doubt, preference shares or other equity securities) which, with the consent of the Issuer or either Keep Well Provider, as the case may be, are quoted, listed, ordinarily dealt in or traded on any stock exchange and/or quotation system or by any listing authority, over-the-counter or other established securities market other than any such indebtedness where the majority thereof is initially placed with investors domiciled in Portugal and who purchase such indebtedness in Portugal.

Permitted Security means:

- (i) in the case of a consolidation or merger of the Issuer or either Keep Well Provider, as the case may be, with or into another company (the **Combining Company**), any Security Interest over assets of the Issuer or such Keep Well Provider, as the case may be (if it is the surviving company) or the company (if other than the Issuer, such Keep Well Provider or such Material Subsidiary, as the case may be,) surviving or formed by such

consolidation or merger provided that: (i) such Security Interest was created by the Combining Company over assets owned by it, (ii) such Security Interest is existing at the time of such consolidation or merger, (iii) such Security Interest was not created in contemplation of such consolidation or merger and (iv) the amount secured by such Security Interest is not increased thereafter; and

- (ii) any Security Interest on or with respect to the assets (including but not limited to receivables) of the Issuer or either Keep Well Provider, as the case may be, which is created pursuant to any securitisation or like arrangement in accordance with normal market practice and whereby the indebtedness secured by such Security Interest or the indebtedness in respect of any guarantee or indemnity which is secured by such Security Interest is limited to the value of such assets.

Person means any individual, company, corporation, firm, partnership, joint venture, association, organisation, state, agency of a state or other entity, whether or not having separate legal personality.

3. DEFINITIONS

In these Conditions, unless otherwise provided:

Additional Ordinary Shares has the meaning provided in Condition 6.3.

Bondholder and **holder** mean the person in whose name a Bond is registered in the Register (as defined in Condition 4.1).

business day means, in relation to any place, a day (other than a Saturday or Sunday) on which commercial banks and foreign exchange markets are open for business in that place.

Capital Distribution means any Non-Cash Dividend (as defined in Condition 6.2(c) below).

a **Change of Control** occurs when any person or persons, acting together, acquire(s) control of Portugal Telecom (other than as a result of an Exempt Newco Scheme).

control means the acquisition or control of more than 50 per cent. of the Voting Rights of the issued share capital of Portugal Telecom, whether obtained directly or through a Subsidiary, and whether obtained by ownership of share capital, the holding of Voting Rights or pursuant to the terms of a shareholders' agreement and "controlled" shall be construed accordingly. For the purpose of this definition of "control" only, **Subsidiary** means any company in which the entity in question holds, directly or through another Subsidiary, more than 50 per cent. of the share capital or voting rights.

Change of Control Notice has the meaning provided in Condition 6.7.

Change of Control Period means the period commencing on the date on which a Change of Control occurs and ending 60 calendar days following such date or, if later, 60 calendar days following the date on which a Change of Control Notice is given as required by Condition 6.7.

Change of Control Put Date has the meaning provided in Condition 7.3.

Change of Control Put Exercise Notice has the meaning provided in Condition 7.3.

Closing Date means 28 August 2007.

Current Market Price means, in respect of an Ordinary Share at a particular date, the average of the Volume Weighted Average Price of an Ordinary Share for the five consecutive dealing days ending on the dealing day immediately preceding such date; provided that if at any time during the said five-dealing-day period the Volume Weighted Average Price shall have been based on a price ex-Dividend (or ex- any other entitlement) and during some other part of that period the Volume Weighted Average Price shall have been based on a price cum-Dividend (or cum- any other entitlement), then:

- (a) if the Ordinary Shares to be issued or transferred do not rank for the Dividend (or entitlement) in question, the Volume Weighted Average Price on the dates on which the Ordinary Shares shall have been based on a price cum-Dividend (or cum- any other entitlement) shall for the purpose of this definition be deemed to be the amount thereof

reduced by an amount equal to the Fair Market Value of any such Dividend or entitlement per Ordinary Share as at the date of first public announcement of such Dividend (or entitlement); or

- (b) if the Ordinary Shares to be issued or transferred do rank for the Dividend (or entitlement) in question, the Volume Weighted Average Price on the dates on which the Ordinary Shares shall have been based on a price ex-Dividend (or ex- any other entitlement) shall for the purpose of this definition be deemed to be the amount thereof increased by an amount equal to the Fair Market Value of any such Dividend or entitlement per Ordinary Share as at the date of the first public announcement of such Dividend (or entitlement),

and provided further that if on each of the said five dealing days the Volume Weighted Average Price shall have been based on a price cum-Dividend (or cum- any other entitlement) in respect of a Dividend (or other entitlement) which has been declared or announced but the Ordinary Shares to be issued do not rank for that Dividend (or other entitlement) the Volume Weighted Average Price on each of such dates shall for the purposes of this definition be deemed to be the amount thereof reduced by an amount equal to the Fair Market Value of any such Dividend or entitlement per Ordinary Share as at the date of the first public announcement of such Dividend or entitlement,

and provided further that, if the Volume Weighted Average Price of an Ordinary Share is not available on one or more of the said five dealing days (disregarding the proviso to the definition of Volume Weighted Average Price), then the average of such Volume Weighted Average Prices which are available in that five-dealing-day period shall be used (subject to a minimum of two such prices) and if only one, or no, such Volume Weighted Average Price is available in the relevant period the Current Market Price shall be determined in good faith by an Independent Financial Adviser.

CVM means Central de Valores Mobiliários.

dealing day means a day on which the Relevant Stock Exchange or relevant stock exchange or securities market is open for business (other than a day on which the Relevant Stock Exchange or relevant stock exchange or securities market is scheduled to or does close prior to its regular weekday closing time).

Dividend means any dividend or any form of distribution to Shareholders (including a Spin-Off) whether of cash, assets or other property, and whenever paid or made and however described (and for these purposes a distribution of assets includes without limitation an issue of Ordinary Shares, or other Securities credited as fully or partly paid up by way of capitalisation of profits or reserves) provided that:

- (a) where a cash Dividend is announced which is to be, or may at the election of a Shareholder or Shareholders be, satisfied by the issue or delivery of Ordinary Shares or other property or assets, or where a capitalisation of profits or reserves is announced which is to be, or may at the election of a Shareholder or Shareholders be, satisfied by the payment of a cash Dividend, then for the purposes of this definition the Dividend in question shall be treated as a cash Dividend of the greater of (i) such cash Dividend and (ii) the Fair Market Value (on the date of the first public announcement of such Dividend or capitalisation (as the case may be) or if later, the date on which the number of Ordinary Shares (or amount of property or assets, as the case may be) which may be issued or transferred or delivered is determined), of such Ordinary Shares or other property or assets;
- (b) any issue of Ordinary Shares falling within Condition 6.2(b) shall be disregarded;
- (c) a purchase or redemption or buy back of share capital of Portugal Telecom by Portugal Telecom or any Subsidiary of Portugal Telecom shall not constitute a Dividend unless, in the case of purchases, redemptions or buy backs of Ordinary Shares by or on behalf of Portugal Telecom or any of its Subsidiaries, the volume weighted average price per Ordinary Share (before expenses) on any one day (a **Specified Share Day**) in respect of such purchases, redemptions or buy backs (translated, if not in euro, into euro at the spot

rate ruling at the close of business on such day as determined in good faith by an Independent Financial Adviser (or if no such rates available on that date, the equivalent rate on the immediately preceding date on which such rate is available) exceeds by more than (i) 5% (in the case of a redemption of share capital of Portugal Telecom by Portugal Telecom or any Subsidiary of Portugal Telecom) or (ii) 7.5% (in the case of a purchase or buy back of share capital of Portugal Telecom or any Subsidiary of Portugal Telecom) the average of the closing prices of the Ordinary Shares on the Relevant Stock Exchange (as published by or derived from the Relevant Stock Exchange) on the five dealing days immediately preceding the Specified Share Day or, where an announcement (excluding, for the avoidance of doubt for these purposes, any general authority for such purchases, redemptions or buy backs approved by a general meeting of Ordinary Shareholders of Portugal Telecom or any notice convening such a meeting of Ordinary Shareholders) has been made of the intention to purchase, redeem or buy back Ordinary Shares at some future date at a specified price, on the five dealing days immediately preceding the date of such announcement, in which case such purchase, redemption or buy back shall be deemed to constitute a cash Dividend in euro to the extent that the aggregate price paid (before expenses) in respect of such Ordinary Shares purchased by Portugal Telecom or, as the case may be, any of its Subsidiaries (translated where appropriate into euro as provided above) exceeds the product of (i)(a) in the case of a redemption of share capital of Portugal Telecom by Portugal Telecom or any Subsidiary of Portugal Telecom, 105 per cent. or (i)(b) in the case of a purchase or buy back of share capital of Portugal Telecom or any Subsidiary of Portugal Telecom, 107.5 per cent., in each case, of the average closing price of the Ordinary Shares determined as aforesaid and (ii) the number of Ordinary Shares so purchased; and

- (d) if Portugal Telecom or any of its Subsidiaries shall purchase any receipts or certificates representing Ordinary Shares, the provisions of paragraph (c) shall be applied in respect thereof in such manner and with such modifications (if any) as shall be determined in good faith by an Independent Financial Adviser.

equity share capital means in relation to a company, its issued share capital excluding any part thereof which, neither as regards dividends, nor as regards capital, carries any right to participate beyond a specified amount in a distribution.

Euronext Lisbon means Euronext by Euronext Lisbon managed by *Euronext, Lisbon-Sociedade Gestora de Mercados Regulamentados S.A.*

Exchange Date has the meaning provided in Condition 6.8.

Exchange Notice has the meaning provided in Condition 6.8.

Exchange Period has the meaning provided in Condition 6.1.

Exchange Price has the meaning provided in Condition 6.1.

Exchange Right has the meaning provided in Condition 6.1.

Exempt Newco Scheme means a Newco Scheme where immediately after completion of the relevant scheme of arrangement the ordinary shares or units (or equivalent) of Newco are (1) admitted to trading on the Euronext Lisbon or (2) admitted to listing on such other regulated, regularly operating, recognised stock exchange or securities market as Portugal Telecom or Newco may determine.

Fair Market Value means, with respect to any property on any date, the fair market value of that property as determined in good faith by an Independent Financial Adviser provided, that (a) the Fair Market Value of a cash Dividend paid or to be paid shall be the amount of such cash Dividend; (b) the Fair Market Value of any other cash amount shall be the amount of such cash; (c) where Spin Off Securities (other than PTM Spin-Off Securities (as defined below)), options, warrants or other rights are publicly traded in a market of adequate liquidity (as determined by an Independent Financial Adviser), the fair market value (i) of such Spin-Off Securities (other than PTM Spin-Off Securities) shall equal the arithmetic mean of the daily Volume Weighted Average Prices of such Spin-Off Securities and (ii) of such options, warrants

or other rights shall equal the arithmetic mean of the daily closing prices of such options, warrants or other rights, in the case of both (i) and (ii) during the period of five trading days on the relevant market commencing on such date (or, if later, the first such trading day such Spin-Off Securities options, warrants or other rights are publicly traded); and (d) in the case of (i) translated into euro (if declared or paid in a currency other than euro) at the rate of exchange used to determine the amount payable to Shareholders who were paid or are to be paid or are entitled to be paid the cash Dividend in euro; and in any other case, converted into euro (if expressed in a currency other than euro) at such rate of exchange as may be determined in good faith by an Independent Financial Adviser to be the spot rate ruling at the close of business on that date (or if no such rate is available on that date the equivalent rate on the immediately preceding date on which such a rate is available). In addition, in the case of (i) and (ii), any withholding or deduction required to be made on account of tax and any associated tax credit shall be disregarded.

Final Maturity Date means 28 August 2014.

Further Bonds means any further Bonds issued pursuant to Condition 16 and consolidated and forming a single series with the then outstanding Bonds.

Independent Financial Adviser means an investment bank of international repute appointed by the Issuer and approved in writing by the Trustee or, if the Issuer fails to make such appointment and such failure continues for a reasonable period (as determined by the Trustee) and the Trustee is indemnified to its satisfaction against the costs, fees and expenses of such adviser, appointed by the Trustee following consultation with the Issuer.

Interest Payment Date has the meaning provided in Condition 5.1.

Lisbon business day means a day (other than a Saturday or Sunday) on which commercial banks and foreign exchange markets are open for business in Lisbon.

Newco Scheme means a scheme of arrangement or analogous proceeding (i) which effects the interposition of a limited liability company (**Newco**) between the Shareholders of Portugal Telecom immediately prior to the scheme of arrangement or analogous proceeding (the **Existing Shareholders**) and Portugal Telecom and (ii) in respect of which the Issuer and the Trustee agree, immediately prior to the implementation of such Newco Scheme, to make such amendments to the Conditions and the Trust Deed as are necessary, in the opinion of the Trustee, to ensure that (a) the Bonds may be exchanged for ordinary shares in Newco *mutatis mutandis* in accordance with and subject to these Conditions and the Trust Deed and (b) the Trust Deed and the Conditions (including, without limitation, the adjustment provisions (in Condition 6), the Events of Default (in Condition 9) and the Undertakings (in Condition 10)) provide at least the same protections and benefits to the Trustee and the Bondholders following the implementation of such Newco Scheme as they provided to the Trustee and the Bondholders prior to the implementation of the Newco Scheme, *mutatis mutandis*; provided, in all cases, that immediately after completion of the scheme of arrangement the only shareholders of Newco are the Existing Shareholders and that all Subsidiaries of Portugal Telecom immediately prior to the scheme of arrangement (other than Newco, if Newco is then a Subsidiary of Portugal Telecom) are Subsidiaries of Portugal Telecom immediately after the scheme of arrangement.

Optional Redemption Date has the meaning provided in Condition 7.2.

Optional Redemption Notice has the meaning provided in Condition 7.2.

Ordinary Shares means fully paid ordinary shares in the capital of Portugal Telecom currently with a par value of €0.03 each.

Parity Value means, in respect of any dealing day, the euro amount calculated as follows:

$$PV = OS \times MP$$

where

$$PV = \text{the Parity Value}$$

OS = the number of Ordinary Shares that would fall to be delivered on the exercise of Exchange Rights in respect of a Bond in the principal amount of €50,000 assuming the Exchange Date to be such dealing day

MP = the closing price for the Ordinary Shares as published by or derived from the Relevant Stock Exchange on such dealing day

provided that if on any such dealing day the Ordinary Shares shall have been quoted cum Dividend or cum-any other entitlement the closing price on such dealing day shall be deemed to be the amount thereof reduced by an amount equal to the Fair Market Value of any such Dividend or entitlement per Ordinary Share as at the date of first public announcement of such Dividend or entitlement.

a **person** includes any individual, company, corporation, firm, partnership, joint venture, undertaking, association, organisation, trust, state or agency of a state (in each case whether or not being a separate legal entity).

Record Date has the meaning provided in Condition 8.3.

Registration Date means the date on which the relevant Ordinary Shares (having, in the case of an issue of new Ordinary Shares, been registered with the Commercial Registry of Lisbon) are credited to an account of a financial intermediary with CVM.

Relevant Date means, in respect of any Bond, whichever is the later of (a) the date on which payment in respect of it first becomes due and (b) if any amount of the money payable is improperly withheld or refused the date on which payment in full of the amount outstanding is made or (if earlier) the date on which notice is duly given by the Issuer or to the Bondholders in accordance with Condition 17 that, upon further presentation of the Bond, where required pursuant to these Conditions, being made, such payment will be made, provided that such payment is in fact made as provided in these Conditions.

Relevant Stock Exchange means Euronext Lisbon or if at the relevant time the Ordinary Shares are not at that time listed on Euronext Lisbon, the principal stock exchange or securities market on which the Ordinary Shares are then listed, admitted to trading or quoted or dealt in.

Retroactive Adjustment has the meaning provided in Condition 6.3.

Securities means any securities including, without limitation, Ordinary Shares, bonds convertible or exchangeable in to Ordinary Shares or options warrants or other rights to subscribe for or purchase or acquire Ordinary Shares.

Shareholders means the holders of Ordinary Shares.

Specified Date has the meaning provided in Condition 6.2(g) and (h).

Spin-Off means:

- (a) a distribution of Spin-Off Securities by Portugal Telecom to Shareholders as a class; or
- (b) any transfer of any property or assets (including cash or shares or securities of or in or issued or allotted by any entity) by any entity (other than Portugal Telecom) to Shareholders as a class or, in the case of or in connection with a Newco Scheme, Existing Shareholders, as a class (but excluding the issue and allotment of shares by Newco to Existing Shareholders), pursuant in each case to any arrangements with Portugal Telecom or any of its Subsidiaries.

Spin-Off Securities means equity share capital of an entity other than Portugal Telecom.

Tangible Net Worth shall mean the total assets of the Issuer less the sum of intangible assets and total liabilities of the Issuer. A certificate of the auditors of the Issuer as to the amount of Tangible Net Worth shall, in the absence of manifest error, be final and conclusive.

TARGET System means the Trans-European Automated Real-Time Gross Settlement Express Transfer (TARGET) System or any successor thereto.

Volume Weighted Average Price means, in respect of an Ordinary Share or, as the case may be, a Spin-Off Security on any dealing day, the volume-weighted average price of an Ordinary Share or, as the case may be, a Spin-Off Security published by or derived (in the case of an Ordinary

Share) from the Relevant Stock Exchange or (in the case of a Spin-Off Security) from the principal stock exchange or securities market on which such Spin-Off Securities are then listed or quoted or dealt in, if any or, in any such case, such other source as shall be determined to be appropriate by an Independent Financial Adviser on such dealing day, provided that if on any such dealing day where such price is not available or cannot otherwise be determined as provided above, the Volume Weighted Average Price of an Ordinary Share or a Spin-Off Security, as the case may be, in respect of such dealing day shall be the Volume Weighted Average Price, determined as provided above, on the immediately preceding dealing day on which the same can be so determined.

Voting Rights means the right to vote at a general meeting of shareholders of Portugal Telecom.

References to any provision of any statute shall be deemed also to refer to any statutory modification or re-enactment thereof or any statutory instrument, order or regulation made thereunder or under such modification or re-enactment.

References to any issue or offer or grant to Shareholders or Existing Shareholders “as a class” or “by way of rights” shall be taken to be references to an issue or offer or grant to all or substantially all Shareholders or Existing Shareholders, as the case may be, other than Shareholder or Existing Shareholders, as the case may be, to whom, by reason of the laws of any territory or requirements of any recognised regulatory body or any other stock exchange or securities market in any territory or in connection with fractional entitlements, it is determined not to make such Issuer or offer or grant.

References in these Conditions to the principal amount of any Bond shall be to the face value thereof, being an authorised denomination of that Bond.

In making any calculation or determination of Current Market Price or Volume Weighted Average Price, such adjustments (if any) shall be made as an Independent Financial Adviser considers appropriate to reflect any consolidation or sub-division of the Ordinary Shares or any Issue of Ordinary Shares by way of capitalisation of profits or reserves, or any like or similar event.

For the purposes of Conditions 6.2, 6.3, 6.8, and 6.9 and Condition 10 only, (a) references to the “issue” of Ordinary Shares shall include the transfer and/or delivery of Ordinary Shares, whether newly issued and allotted or previously existing or held by or on behalf of Portugal Telecom or any of its Subsidiaries, and (b) Ordinary Shares held by or on behalf of Portugal Telecom or any of its Subsidiaries (and which, in the case of Condition 6.2(d) and (f), do not rank for the relevant right or other entitlement) shall not be considered as or treated as “in issue”.

4. REGISTRATION AND TRANSFER OF BONDS

4.1 Registration

The Issuer will cause a register (the **Register**) to be kept at the specified office of the Registrar outside the United Kingdom on which will be entered the names and addresses of the holders of the Bonds and the particulars of the Bonds held by them and of all transfers, redemptions and exchanges of Bonds.

4.2 Transfer

Bonds may, subject to the terms of the Agency Agreement and to Conditions 4.3 and 4.4, be transferred in whole or in part in an authorised denomination by lodging the relevant Bond (with the form of application for transfer in respect thereof duly executed and duly stamped where applicable) at the specified office of the Registrar or any Agent. No transfer of a Bond will be valid unless and until entered on the Register. A Bond may be registered only in the name of, and transferred only to, a named person (or persons, not exceeding four in number).

The Registrar will within seven business days, at the place of the specified office of the Registrar, of receipt of any duly made application for the transfer of a Bond, deliver a new Bond to the transferee (and, in the case of a transfer of part only of a Bond, deliver a Bond for the untransferred balance to the transferor) at the specified office of the Registrar or (at the risk

and, if mailed at the request of the transferee or, as the case may be, the transferor otherwise than by ordinary mail, at the expense of the transferee or, as the case may be, the transferor) mail the Bond by uninsured mail to such address as the transferee or, as the case may be, the transferor may request.

4.3 Formalities Free of Charge

Such transfer will be effected without charge subject to (a) the person making such application for transfer paying or procuring the payment of any taxes, duties and other governmental charges in connection therewith, (b) the Registrar being satisfied with the documents of title and/or identity of the person making the application and (c) such reasonable regulations as the Issuer may from time to time agree with the Registrar and the Trustee.

4.4 Closed Periods

Neither the Issuer nor the Registrar will be required to register the transfer of any Bond (or part thereof) (a) during the period of 15 days immediately prior to the Final Maturity Date or any earlier date fixed for redemption of the Bonds pursuant to Condition 7.2; (b) in respect of which an Exchange Notice has been delivered in accordance with Condition 6.8; (c) in respect of which a Bondholder has exercised its right to require redemption pursuant to Condition 7.3; or (d) during the period of 15 days ending on (and including) any Record Date (as defined in Condition 8.3) in respect of any payment of interest on the Bonds.

5. INTEREST

5.1 Interest Rate

The Bonds bear interest from and including the Closing Date at the rate of 4.125 per cent. per annum calculated by reference to the principal amount thereof and payable semi-annually in arrear on 28 February and 28 August in each year (each an **Interest Payment Date**), commencing on 28 February 2008. The amount of interest payable in respect of a Bond for any period which is not an Interest Period shall be calculated on the basis of the number of days in the relevant period from (and including) the first day of such period to (but excluding) the last day of such period divided by the number of days from (and including) the immediately preceding Interest Payment Date (or, if none, the Closing Date) to (but excluding) the next Interest Payment Date multiplied by 2.

Interest Period means the period beginning on (and including) the Closing Date and ending on (but excluding) 28 February 2008 (being the first Interest Payment Date) and each successive period beginning on (and including) an Interest Payment Date and ending on (but excluding) the next succeeding Interest Payment Date.

5.2 Accrual of Interest

Each Bond will cease to bear interest (a) where the Exchange Right shall have been exercised by a Bondholder, from the Interest Payment Date immediately preceding the relevant Exchange Date or, if none, the Closing Date (subject in any such case as provided in Condition 6.9 or 6.10) or (b) where such Bond is being redeemed or repaid pursuant to Condition 7 or Condition 9, from the due date for redemption thereof unless, upon due presentation thereof, payment of principal is improperly withheld or refused, in which event interest will continue to accrue at such rate (both before and after judgment) until whichever is the earlier of (i) the day on which all sums due in respect of such Bond up to that day are received by or on behalf of the relevant holder, and (ii) the day seven days after the Trustee or the Principal Paying Agent has notified Bondholders of receipt of all sums due in respect of all the Bonds up to that seventh day (except to the extent that there is failure in the subsequent payment to the relevant holders under these Conditions).

6. EXCHANGE OF BONDS

6.1 Exchange Period and Exchange Price

Subject to and as provided in these Conditions, each Bond shall entitle the holder (an **Exchange Right**) to exchange such Bond for new and/or existing Ordinary Shares as determined by the Issuer, credited as fully paid.

The number of Ordinary Shares to be issued or transferred and delivered on exercise of an Exchange Right shall be determined by dividing the principal amount of the relevant Bond by the exchange price (the **Exchange Price**) in effect on the relevant Exchange Date.

The initial Exchange Price is €13.9859 per Ordinary Share. On the basis of the initial Exchange Price, each €50,000 principal amount of Bonds would entitle the holder to receive (subject as provided in these Conditions) 3,575 Ordinary Shares. The Exchange Price is subject to adjustment in the circumstances described in Condition 6.2 and the expression "Exchange Price" shall be construed accordingly.

A Bondholder may exercise the Exchange Right in respect of a Bond by delivering such Bond to the specified office of any Agent in accordance with Condition 6.8 whereupon the Issuer shall (subject as provided in these Conditions) procure the delivery, to or as directed by the relevant Bondholder, of Ordinary Shares credited as paid up in full as provided in this Condition 6.

Subject to, and as provided in these Conditions, the Exchange Right in respect of a Bond may be exercised, at the option of the holder thereof, at any time (subject to any applicable fiscal or other laws or regulations and as hereinafter provided) from 3 January 2009 to the close of business (at the place where the relevant Bond is delivered for exchange) on the date falling eight days prior to the Final Maturity Date (both days inclusive) or, if the Bonds shall have been called for redemption pursuant to Condition 7.2 prior to the Final Maturity Date, then up to the close of business (at the place aforesaid) on the eighth day before the date fixed for redemption thereof pursuant to Condition 7.2, unless there shall be default in making payment in respect of such Bond on such date fixed for redemption, in which event the Exchange Right shall extend up to the close of business (at the place aforesaid) on the date on which the full amount of such payment becomes available for payment and notice of such availability has been duly given in accordance with Condition 17 or, if earlier, the Final Maturity Date; provided that, in each case, if the final such date for the exercise of Exchange Rights is not a business day at the place aforesaid, then the period for exercise of the Exchange Right by Bondholders shall end on the immediately preceding business day at the place aforesaid.

Exchange Rights may not be exercised (i) following the giving of notice by the Trustee pursuant to Condition 9; or (ii) in respect of a Bond which the relevant holder has exercised its right to require the Issuer to redeem pursuant to Condition 7.3.

Exchange Rights may not be exercised by a Bondholder in circumstances where the relevant Exchange Date would fall during the period commencing on the Record Date in respect of any payment of interest on the Bonds and ending on the relevant Interest Payment Date (both days inclusive).

The period during which Exchange Rights may (subject as provided below) be exercised by a Bondholder is referred to as the **Exchange Period**.

Notwithstanding the Exchange Period prescribed by this Condition 6.1, the Exchange Right in respect of a Bond may be exercised at any time during a Change of Control Period, save that Exchange Rights may not be exercised during a Change of Control Period (i) following the giving of notice by the Trustee pursuant to Condition 9; or (ii) in respect of a Bond which the relevant holder has exercised its right to require the Issuer to redeem pursuant to Condition 7.3.

Exchange Rights may only be exercised in respect of an authorised denomination. Where Exchange Rights are exercised in respect of part only of a Bond, the old Bond shall be cancelled and a new Bond for the balance thereof shall be issued in lieu thereof without charge but upon payment by the holder of any taxes, duties and other governmental charges payable in connection therewith and the Registrar will within seven business days, in the place of the specified office of the Registrar, following the relevant Exchange Date deliver such new Bond to

the Bondholder at the specified office of the Registrar or (at the risk and, if mailed at the request of the Bondholder otherwise than by ordinary mail, at the expense of the Bondholder) mail the new Bond by uninsured mail to such address as the Bondholder may request.

Fractions of Ordinary Shares will not be delivered on exchange or pursuant to Condition 6.3. However, except where any individual entitlement would be less than €10, a cash payment shall be made by the Issuer to the relevant exercising Bondholder in respect of any such fraction equal to the product of the closing price of an Ordinary Share on the relevant Exchange Date as published by or derived from the Relevant Stock Exchange multiplied by such fraction. Payment of any such amount shall be made not later than seven TARGET Business Days following the relevant Exchange Date by transfer to a euro account maintained by the Bondholder with a bank in a city in which banks have access to the TARGET System as specified in the relevant Exchange Notice. If the Exchange Right in respect of more than one Bond is exercised at any one time such that Ordinary Shares to be delivered on exchange or pursuant to Condition 6.3 are to be registered in the same name, the number of such Ordinary Shares to be delivered in respect thereof shall be calculated on the basis of the aggregate principal amount of such Bonds being so exchanged and rounded down to the nearest whole number of Ordinary Shares.

The Issuer and Portugal Telecom will procure that Ordinary Shares to be delivered or transferred on exchange will be delivered or transferred to the holder of the Bonds completing the relevant Exchange Notice or his nominee.

6.2 Adjustment of Exchange Price

Upon the happening of any of the events described below, the Exchange Price shall be adjusted as follows:

- (a) If and whenever there shall be a consolidation, reclassification or subdivision in relation to the Ordinary Shares, the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such consolidation, reclassification or subdivision by the following fraction:

$$\frac{A}{B}$$

where:

- A is the aggregate number of Ordinary Shares in issue immediately before such consolidation, reclassification or subdivision, as the case may be; and
- B is the aggregate number of Ordinary Shares in issue immediately after, and as a result of, such consolidation, reclassification or subdivision, as the case may be.

Such adjustment shall become effective on the date the consolidation, reclassification or subdivision, as the case may be, takes effect.

- (b) If and whenever Portugal Telecom shall issue any Ordinary Shares credited as fully paid to the Shareholders by way of capitalisation of profits or reserves (including any share premium account or capital redemption reserve) other than (1) where any such Ordinary Shares are issued instead of the whole or part of a cash Dividend which the Shareholders would or could otherwise have received or (2) where the Shareholders may elect to receive a cash Dividend in lieu of such Ordinary Shares, the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such issue by the following fraction:

$$\frac{A}{B}$$

where:

- A is the aggregate nominal amount of the issued Ordinary Shares immediately before such issue; and

B is the aggregate nominal amount of the issued Ordinary Shares immediately after such issue.

Such adjustment shall become effective on the date of issue of such Ordinary Shares.

- (c) (i) If and whenever Portugal Telecom shall pay or make any Extraordinary Dividend to the Shareholders the Exchange Price shall be adjusted by multiplying the Exchange Price in force on the day immediately preceding the date on which the Ordinary Shares are trading ex-the relevant Extraordinary Dividend by the following fraction:

$$\frac{A - B}{A - T}$$

where:

- A is the Current Market Price of one Ordinary Share on the first date on which the Ordinary Shares are traded ex-the relevant Extraordinary Dividend on the Relevant Stock Exchange or, in the case of a purchase, redemption or buy back of Ordinary Shares or any depositary or other receipts or certificates representing Ordinary Shares by or on behalf of Portugal Telecom or any Subsidiary of Portugal Telecom, on which such Ordinary Shares (or depositary or other receipts or certificates) are purchased, redeemed or bought back or, in the case of a Spin-Off, is the Current Market Price of an Ordinary Share on the first date on which the Ordinary Shares are traded ex-the relevant Spin-Off;
- B is the portion of the Fair Market Value of the aggregate Extraordinary Dividend attributable to one Ordinary Share, with such portion being determined by dividing the Fair Market Value of the aggregate Extraordinary Dividend by the number of Ordinary Shares entitled to receive the relevant Extraordinary Dividend (or, in the case of a purchase, redemption or buy back of Ordinary Shares or any depositary or other receipts or certificates representing Ordinary Shares by or on behalf of Portugal Telecom or any Subsidiary of Portugal Telecom, by the number of Ordinary Shares in issue immediately following such purchase); and
- T is the amount (if any) by which the Threshold Amount in respect of the Relevant Fiscal Year exceeds an amount equal to the aggregate of the Fair Market Values of any previous Dividends per Ordinary Share paid or made in respect of such Relevant Fiscal Year (where T shall be zero if such amount is equal to, or exceeds, the Threshold Amount in respect of such Relevant Fiscal Year). For the avoidance of doubt T shall equal the Threshold Amount in respect of the Relevant Fiscal Year where no previous Dividends per Ordinary Share have been paid in such Relevant Fiscal Year.

Such adjustment shall become effective on the first date on which the Ordinary Shares are traded ex-the relevant Extraordinary Dividend on the Relevant Stock Exchange or, in the case of a purchase, redemption or buy back of Ordinary Shares or any depositary or other receipts or certificates representing Ordinary Shares by or on behalf of Portugal Telecom or any Subsidiary of Portugal Telecom, on the date such purchase, redemption or buy back is made or, in any such case if later, the first date upon which the Fair Market Value of the relevant Dividend is capable of being determined as provided herein.

Extraordinary Dividend means any Cash Dividend or Non-Cash Dividend (the **Relevant Dividend**) paid or made in respect of a fiscal year of Portugal Telecom (the **Relevant Fiscal Year**), where (a) the Fair Market Value of the Relevant Dividend per Ordinary Share or (b) the sum of (i) the Fair Market Value of the Relevant Dividend per Ordinary Share and (ii) an amount equal to the aggregate of the Fair Market Value or Values of any other Dividend or Dividends per Ordinary Share paid or made in respect of such Relevant Fiscal Year, exceeds the Threshold Amount and, in that case, the Extraordinary Dividend is the Relevant Dividend.

Threshold Amount means in respect of any Relevant Fiscal Year, €0.575 per Ordinary Share, adjusted *pro rata* for any adjustments to the Exchange Price made pursuant to the provisions of these Conditions, save in the case of the PTM Spin-Off (as defined below), the occurrence of which will not trigger, in any circumstances, an adjustment to the Threshold Amount and save that no adjustment to the Exchange Price at any time (the **Applicable Time**) will trigger a pro rata adjustment to the Threshold Amount unless such adjustment to the Exchange Price at the Applicable Time, when aggregated with any previous adjustments to the Exchange Price since the preceding date on which the Threshold Amount was adjusted (or, if none, the Closing Date), would lead to an adjustment to the Exchange Price in force at the Applicable Time of 3 per cent. or more (the **Aggregate Amount**). For the avoidance of doubt, such Threshold Amount at the Applicable Time will be adjusted pro rata, as if the Exchange Price in force at the Applicable Time would have been adjusted by the Aggregate Amount.

Cash Dividend means (i) any Dividend which is to be paid or made in cash (in whatever currency), but other than falling within paragraph (b) of the definition of **Spin-Off** and (ii) any Dividend determined to be a Cash Dividend pursuant to paragraph (a) of the definition of **Dividend**, and for the avoidance of doubt, a Dividend falling within paragraph (c) or (d) of the definition of **Dividend** shall be treated as being a Non-Cash Dividend.

Non-Cash Dividend means any Dividend which is not a Cash Dividend, and shall include a Spin-Off but shall exclude the PTM-Spin-Off (as defined below).

Notwithstanding the above provisions of this Condition 6.2(c)(i), on an adjustment to the Threshold Amount as a result of the current and any previous adjustments to the Exchange Price amounting to the Aggregate Amount, the applicable Exchange Price which is due to be multiplied by the fraction set out above will be recalculated to reflect the Exchange Price which would have been in force (on the day immediately preceding the date on which the Ordinary Shares are trading ex-the relevant Extraordinary Dividend) if the previous adjustments to the Exchange Price would have resulted, at the time that such previous adjustments were made, in a pro rata adjustment to the Threshold Amount.

(ii) If Portugal Telecom shall undertake the PTM Spin-Off (as defined below), the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such PTM Spin-Off by the sum of the Daily Metrics during the period of five dealing days on the Relevant Stock Exchange immediately preceding the first date on which the Ordinary Shares are traded ex-the PTM Spin-Off (as defined below) and

Daily Metric means:

$$((A-B) / A) * 1/5$$

where:

- A is the Volume Weighted Average Price of an Ordinary Share of Portugal Telecom on each such dealing day determined in the manner specified herein; and
- B is the portion of the Fair Market Value of the aggregate PTM Spin-Off Securities attributable to one Ordinary Share, with such portion being determined by dividing the Fair Market Value of the aggregate PTM Spin-Off Securities by the number of Ordinary Shares entitled to receive the PTM-Spin Off, and for the purposes of which the definition of Fair Market Value shall be amended as set out below.

Such adjustment shall become effective on the first date on which the Ordinary Shares are traded ex-the PTM Spin-Off Securities on the Relevant Stock Exchange.

In this Condition 6.2(c)(ii) only:

Fair Market Value of the aggregate PTM Spin-Off Securities means the daily Volume Weighted Average Price of the ordinary shares of PTM on each such dealing day;

PTM means PT Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A.;

PTM Spin-Off means a distribution of PTM Spin-Off Securities; and

PTM Spin-Off Securities means the PTM shares to be distributed to shareholders of Portugal Telecom pursuant to the PTM Spin-Off.

In making any calculation for the purposes of this Condition 6.2(c), such adjustment (if any) shall be made as an Independent Financial Adviser may determine in good faith to be appropriate to reflect (i) any consolidation or sub-division of Ordinary Shares or the issue of Ordinary Shares by way of capitalisation of profits or reserves, or any like or similar event or (ii) any change in the fiscal year of Portugal Telecom.

For the purposes of the above, the Fair Market Value of a Dividend shall (subject as provided in paragraph (a) of the definition of **Dividend** and in the definition of **Fair Market Value**) be determined as at the first date on which the Ordinary Shares are trading ex the relevant Dividend, and in the case of a Spin-Off (other than the PTM Spin-Off), the Fair Market Value of the relevant Dividend shall be the Fair Market Value of the relevant Spin-Off Securities or, as the case may be, the relevant property or assets.

- (d) If and whenever Portugal Telecom shall issue Ordinary Shares to Shareholders as a class by way of rights, or issue or grant to Shareholders as a class by way of rights, options, warrants or Securities, in each case at a price per Ordinary Share which is less than 95 per cent. of the Current Market Price per Ordinary Share on the dealing day immediately preceding the date of the first public announcement of the terms of the issue or grant of such Ordinary Shares, options, warrants or other rights, the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such issue or grant by the following fraction:

$$\frac{A + B}{A + C}$$

where:

- A is the number of Ordinary Shares in issue immediately before such announcement;
- B is the number of Ordinary Shares which the aggregate amount (if any) payable for the Ordinary Shares issued by way of rights, or for the options or warrants or other rights issued by way of rights and for the total number of Ordinary Shares deliverable on the exercise thereof, would purchase at such Current Market Price per Ordinary Share; and
- C is the number of Ordinary Shares issued or, as the case may be, the maximum number of Ordinary Shares which may be issued upon exercise of such options, warrants or rights calculated as at the date of issue of such options, warrants or rights.

Such adjustment shall become effective on the first date on which the Ordinary Shares are traded ex-rights, ex-options or ex-warrants on the Relevant Stock Exchange.

- (e) If and whenever Portugal Telecom shall issue any Securities (other than Ordinary Shares or options, warrants or other rights to subscribe for or purchase any Ordinary Shares) to Shareholders as a class by way of rights or grant to Shareholders as a class by way of rights any options, warrants or other rights to subscribe for or purchase any Securities (other than Ordinary Shares or options, warrants or other rights to subscribe for or purchase Ordinary Shares), the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such issue or grant by the following fraction:

$$\frac{A - B}{A}$$

where:

- A is the Current Market Price of one Ordinary Share on the dealing day on which the terms of such issue or grant are publicly announced; and

B is the Fair Market Value on the date of such announcement (or if that date is not a dealing day, the next following dealing day) of the portion of the rights attributable to one Ordinary Share.

Such adjustment shall become effective on the first date on which the Ordinary Shares are traded ex-rights, ex-options or ex-warrants on the Relevant Stock Exchange.

- (f) If and whenever Portugal Telecom shall issue (otherwise than as mentioned in subparagraph 6.2(d) above) wholly for cash or for no consideration any Ordinary Shares (other than on the exercise of any rights of conversion into, or exchange or subscription for or purchase of, Ordinary Shares (including, for the avoidance of doubt, conversion of the Bonds in accordance with the Conditions)) or issue or grant (otherwise than as mentioned in subparagraph 6.2(d) above) wholly for cash or for no consideration any options, warrants or other rights to subscribe for or purchase any Ordinary Shares (other than the Bonds, which term shall include for these purposes any Further Bonds), in each case at a price per Ordinary Share which is less than 95 per cent. of the Current Market Price per Ordinary Share on the date (or if that date is not a dealing day, the immediately preceding dealing day) of the first public announcement of the terms of such issue or grant, the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such issue or grant by the following fraction:

$$\frac{A + B}{A + C}$$

where:

- A is the number of Ordinary Shares in issue immediately before the issue of such Ordinary Shares or the grant of such options, warrants or rights;
- B is the number of Ordinary Shares which the aggregate consideration (if any) receivable for the issue of such Ordinary Shares or, as the case may be, for the Ordinary Shares to be issued or otherwise made available upon the exercise of any such options, warrants or rights, would purchase at such Current Market Price per Ordinary Share; and
- C is the number of Ordinary Shares to be issued pursuant to such issue of such Ordinary Shares or, as the case may be, the maximum number of Ordinary Shares which may be issued upon exercise of such options, warrants or rights calculated as at the date of issue of such options, warrants or rights.

Such adjustment shall become effective on the date of issue of such Ordinary Shares or, as the case may be, the grant of such options, warrants or rights.

- (g) If and whenever Portugal Telecom or any Subsidiary of Portugal Telecom or (at the direction or request of or pursuant to any arrangements with Portugal Telecom or any Subsidiary of Portugal Telecom) any other company, person or entity (otherwise than as mentioned in sub-paragraphs 6.2(d), 6.2(e) or 6.2(f) above) shall issue wholly for cash or for no consideration any Securities (other than the Bonds, which term shall include for this purpose any Further Bonds), which by their terms of issue carry (directly or indirectly) rights of conversion into, or exchange or subscription for, Ordinary Shares (or shall grant any such rights in respect of existing Securities so issued) or Securities which by their terms might be redesignated as Ordinary Shares, and the consideration per Ordinary Share receivable upon conversion, exchange, subscription or redesignation is less than 95 per cent. of the Current Market Price per Ordinary Share on the date (or if such date is not a dealing day, the immediately preceding dealing day) of the first public announcement of the terms of issue of such Securities (or the terms of such grant), the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such issue (or grant) by the following fraction:

$$\frac{A + B}{A + C}$$

where:

- A is the number of Ordinary Shares in issue immediately before such issue or grant (but where the relevant Securities carry rights of conversion into or rights of exchange or subscription for Ordinary Shares which have been issued, purchased or acquired by Portugal Telecom or any subsidiary of Portugal Telecom (or at the direction or request of or pursuant to any arrangement with Portugal Telecom or any Subsidiary of Portugal Telecom) for the purposes of or in connection with such issue, less the number of such Ordinary Shares so issued), purchased or acquired;
- B is the number of Ordinary Shares which the aggregate consideration (if any) receivable for the Ordinary Shares to be issued or otherwise made available upon conversion or exchange or upon exercise of the right of subscription attached to such Securities or, as the case may be, for the Ordinary Shares to be issued or to arise from any such redesignation would purchase at such Current Market Price per Ordinary Share; and
- C is the maximum number of Ordinary Shares to be issued or otherwise made available upon conversion or exchange of such Securities or upon the exercise of such right of subscription attached thereto at the initial conversion, exchange or subscription price or rate or, as the case may be, the maximum number of Ordinary Shares which may be issued or arise from any such redesignation.

Provided that if at the time of issue of the relevant Securities or date of grant of such rights (as used in this sub-paragraph 6.2(g) the **Specified Date**) such number of Ordinary Shares is to be determined by reference to the application of a formula or other variable feature or the occurrence of any event at some subsequent time (which may be when such Securities are converted or exchanged or rights of subscription are exercised or, as the case may be, such Securities are redesignated or at such other time as may be provided) then for the purposes of this sub-paragraph 6.2(g), “C” shall be determined by the application of such formula or variable feature or as if the relevant event occurs or had occurred as at the Specified Date and as if such conversion, exchange, subscription, purchase or acquisition or, as the case may be, redesignation had taken place on the Specified Date.

Such adjustment shall become effective on the date of issue of such Securities or, as the case may be, the grant of such rights.

- (h) If and whenever there shall be any modification of the rights of conversion, exchange or subscription attaching to any such Securities (other than the Bonds, which term shall include for this purpose any Further Bonds) as are mentioned in sub-paragraph 6.2(g) above (other than in accordance with the terms (including terms as to adjustment) applicable to such Securities upon issue) so that following such modification the consideration per Ordinary Share receivable has been reduced and is less than 95 per cent. of the Current Market Price per Ordinary Share on the date (or if such date is not a dealing day, the immediately preceding dealing day) of the first public announcement of the proposals for such modification, the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately prior to such modification by the following fraction:

$$\frac{A + B}{A + C}$$

where:

- A is the number of Ordinary Shares in issue immediately before such modification (but where the relevant Securities carry rights of conversion into or rights of exchange or subscription for Ordinary Shares which have been issued, purchased or acquired by Portugal Telecom or any Subsidiary of Portugal Telecom (or at the direction or request or pursuant to any arrangements with Portugal Telecom or any Subsidiary of Portugal Telecom) for the purposes of or in connection with such issue, less the number of such Ordinary Shares so issued, purchased or acquired);

- B is the number of Ordinary Shares which the aggregate consideration (if any) receivable for the Ordinary Shares to be issued or otherwise made available upon conversion or exchange or upon exercise of the right of subscription attached to the Securities so modified would purchase at such Current Market Price per Ordinary Share or, if lower, the existing conversion, exchange or subscription price of such Securities; and
- C is the maximum number of Ordinary Shares which may be issued or otherwise made available upon conversion or exchange of such Securities or upon the exercise of such rights of subscription attached thereto at the modified conversion, exchange or subscription price or rate but giving credit in such manner as an Independent Financial Adviser shall consider appropriate for any previous adjustment under this sub-paragraph or sub-paragraph 6.2(g) above.

Provided that if at the time of such modification (as used in this sub-paragraph 6.2(h) the **Specified Date**) such number of Ordinary Shares is to be determined by reference to the application of a formula or other variable feature or the occurrence of any event at some subsequent time (which may be when such Securities are converted or exchanged or rights of subscription are exercised or at such other time as may be provided) then for the purposes of this paragraph 6.2(h), “C” shall be determined by the application of such formula or variable feature or as if the relevant event occurs or had occurred as at the Specified Date and as if such conversion, exchange or subscription had taken place on the Specified Date.

Such adjustment shall become effective on the date of modification of the rights of conversion, exchange or subscription attaching to such Securities.

- (i) If and whenever Portugal Telecom or any Subsidiary of Portugal Telecom or (at the direction or request of or pursuant to any arrangements with Portugal Telecom or any Subsidiary of Portugal Telecom) any other company, person or entity shall offer any Securities in connection with which offer Shareholders as a class are entitled to participate in arrangements whereby such Securities may be acquired by them (except where the Exchange Price falls to be adjusted under sub-paragraphs 6.2(b), (c), (d), (f), (g) above or (j) below (or would fall to be so adjusted if the relevant issue or grant was at less than 95 per cent. of the Current Market Price per Ordinary Share on the relevant dealing day) or under subparagraph 6.2(e) above) the Exchange Price shall be adjusted by multiplying the Exchange Price in force immediately before the making of such offer by the following fraction:

$$\frac{A - B}{A}$$

where:

- A is the Current Market Price of one Ordinary Share on the dealing day immediately preceding the date on which the terms of such offer are first publicly announced; and
- B is the Fair Market Value on the date of such announcement (or if such date is not a dealing day, the next following dealing day) of the portion of the relevant offer attributable to one Ordinary Share.

Such adjustment shall become effective on the first date on which the Ordinary Shares are traded ex-rights on the Relevant Stock Exchange.

- (j) If a Change of Control shall occur, then upon any exercise of Exchange Rights where the Exchange Date falls during the Change of Control Period, the Exchange Price shall be as set out below, provided that on each occasion on which the Exchange Price is adjusted pursuant to the preceding provisions of this Condition 6.2 each Exchange Price shown in the following table shall be adjusted at the same time by the same proportion:

Exchange Date	<i>Exchange Price</i>
	<i>(Euro)</i>
On or before 28 August 2008.....	10.17
Thereafter, but on or before 28 August 2009.....	10.72
Thereafter, but on or before 28 August 2010.....	11.26
Thereafter, but on or before 28 August 2011.....	11.81
Thereafter, but on or before 28 August 2012.....	12.35
Thereafter, but on or before 28 August 2013.....	12.90
Thereafter and until the Final Maturity Date.....	13.44

- (k) If Portugal Telecom, in consultation with the Trustee, determines that an adjustment should be made to the Exchange Price as a result of one or more circumstances not referred to above in this Condition 6.2 (even if the relevant circumstance is specifically excluded from the operation of sub-paragraphs 6.2(a) to (j) above), Portugal Telecom shall, at its own expense and acting reasonably, request an Independent Financial Adviser to determine as soon as practicable what adjustment (if any) to the Exchange Price is fair and reasonable to take account thereof and the date on which such adjustment should take effect and upon such determination such adjustment (if any) shall be made and shall take effect in accordance with such determination, provided that an adjustment shall only be made pursuant to this subparagraph 6.2(k) if such Independent Financial Adviser is so requested to make such a determination not more than 21 days after the date on which the relevant circumstance arises and if the adjustment would result in a reduction to the Exchange Price.

Notwithstanding the foregoing provisions, where the events or circumstances giving rise to any adjustment pursuant to this Condition 6.2 have already resulted or will result in an adjustment to the Exchange Price or where the events or circumstances giving rise to any adjustment arise by virtue of any other events or circumstances which have already given or will give rise to an adjustment to the Exchange Price or where more than one event which gives rise to an adjustment to the Exchange Price occurs within such a short period of time that, in the opinion of Portugal Telecom, a modification to the operation of the adjustment provisions is required to give the intended result, such modification shall be made to the operation of the adjustment provisions as may be advised by an Independent Financial Adviser to be in its opinion appropriate to give the intended result and provided further that, for the avoidance of doubt, the issue of Ordinary Shares pursuant to the exercise of Exchange Rights shall not result in an adjustment to the Exchange Price.

For the purpose of any calculation of the consideration receivable or price pursuant to subparagraphs (d), (f), (g), and (h), the following provisions shall apply:

- (A) the aggregate consideration receivable or price for Ordinary Shares issued for cash shall be the amount of such cash;
- (B) (x) the aggregate consideration receivable or price for Ordinary Shares to be issued or otherwise made available upon the conversion or exchange of any Securities shall be deemed to be the consideration or price received or receivable for any such Securities and (y) the aggregate consideration receivable or price for Ordinary Shares to be issued or otherwise made available upon the exercise of rights of subscription attached to any Securities or upon the exercise of any options, warrants or rights shall be deemed to be that part (which may be the whole) of the consideration or price received or receivable for such Securities or, as the case may be, for such options, warrants or rights which are attributed by Portugal Telecom to such rights of subscription or, as the case may be, such options, warrants or rights or, if no part of such consideration or price is so attributed, the Fair Market Value of such rights of subscription or, as the case may be, such options warrants or rights as at the date of the first public announcement of the terms of issue of such Securities or, as the case may be, such options, warrants or rights, plus in the case of

each of (x) and (y) above, the additional minimum consideration receivable or price (if any) upon the conversion or exchange of such Securities, or upon the exercise of such rights or subscription attached thereto or, as the case may be, upon exercise of such options, warrants or rights and (z) the consideration receivable or price per Ordinary Share upon the conversion or exchange of, or upon the exercise of such rights of subscription attached to, such Securities or, as the case may be, upon the exercise of such options, warrants or rights shall be the aggregate consideration or price referred to in (x) or (y) above (as the case may be) divided by the number of Ordinary Shares to be issued upon such conversion or exchange or exercise at the initial conversion, exchange or subscription price or rate;

- (C) if the consideration or price determined pursuant to (a) or (b) above (or any component thereof) shall be expressed in a currency other than euro it shall be converted into euro at such rate of exchange as may be determined in good faith by an Independent Financial Adviser to be the spot rate ruling at the close of business on the date of the first public announcement of the terms of issue of such Securities (or if no such rate is available on that date, the equivalent rate on the immediately preceding date on which such rate is available); and
- (D) in determining consideration or price pursuant to the above, no deduction shall be made for any commissions or fees (howsoever described) or any expenses paid or incurred for any underwriting, placing or management of the issue of the relevant Ordinary Shares or Securities or otherwise in connection therewith.

6.3 Retroactive Adjustments

If the Exchange Date in relation to the exchange of any Bond shall be after any consolidation, reclassification or sub-division as is mentioned in Condition 6.2(a), or after the record date or other due date for the establishment of entitlement for any such issue, distribution grant or offer (as the case may be) as is mentioned in Condition 6.2(b), (c) (in relation to a Capital Distribution other than one comprised of an Extraordinary Dividend), (d), (e) or (i), or after any such issue or grant as is mentioned in Condition 6.2(f) and (g) or, in relation to any Extraordinary Dividend in respect of the Ordinary Shares which constitutes a Capital Distribution, falls on or after the date falling 2 calendar months after the end of the fiscal year of Portugal Telecom in respect of which the said Dividend is paid or made or declared, in any case in circumstances where the relevant Exchange Date falls before the relevant adjustment becomes effective under Condition 6.2 (such adjustment, a **Retroactive Adjustment**), then the Issuer shall (conditional upon the relevant adjustment becoming effective) procure that there shall be issued or delivered to the exchanging Bondholder, in accordance with the instructions contained in the Exchange Notice, such additional number of Ordinary Shares (if any) (the **Additional Ordinary Shares**) as, together with the Ordinary Shares issued or to be issued or delivered on conversion of the relevant Bond (together with any fraction of an Ordinary Share not so issued), is equal to the number of Ordinary Shares which would have been required to be issued or delivered on exchange of such Bond if the relevant adjustment (more particularly referred to in the said provisions of Condition 6.2) to the Exchange Price had in fact been made and become effective immediately prior to the relevant Exchange Date, provided that if the relevant Bondholder shall be entitled to receive the relevant Extraordinary Dividend in respect of the Ordinary Shares to be issued or delivered to it, then no such Retroactive Adjustment shall be made in relation to such Dividend and the relevant Bondholder shall not be entitled to receive Additional Ordinary Shares in relation thereto.

6.4 Decision of an Independent Financial Adviser

If any doubt shall arise as to whether an adjustment is to be made to the Exchange Price or as to the appropriate adjustment to the Exchange Price, and following consultation between the Issuer and an Independent Financial Adviser, a written opinion of such Independent Financial Adviser in respect of such adjustment to the Exchange Price shall be conclusive and binding on all concerned, save in the case of manifest error.

6.5 Employees' Share Schemes

No adjustment will be made to the Exchange Price where Ordinary Shares or other Securities (including rights, warrants and options) are issued, offered, exercised, allotted, appropriated, modified or granted to, or for the benefit of, employees or former employees (including Directors holding or formerly holding executive office or the personal service company of any such person) or their spouses or relatives, in each case, of Portugal Telecom or any of its Subsidiaries or any associated company or to a trustee or trustees to be held for the benefit of any such person, in any such case pursuant to any employees' share or option scheme.

6.6 Rounding Down and Notice of Adjustment to the Exchange Price

On any adjustment, the resultant Exchange Price, if not an integral multiple of €0.01, shall be rounded down to the nearest whole multiple of €0.01. No adjustment shall be made to the Exchange Price where such adjustment (rounded down if applicable) would be less than 1 per cent. of the Exchange Price then in effect. Any adjustment not required to be made, and/or any amount by which the Exchange Price has been rounded down, shall be carried forward and taken into account in any subsequent adjustment and such subsequent adjustment shall be made on the basis that the adjustment not required to be made had been made at the relevant time.

Notice of any adjustments to the Exchange Price shall be given by the Issuer and Portugal Telecom to Bondholders in accordance with Condition 17 and the Trustee promptly after the determination thereof.

The Exchange Price shall not in any event be reduced to below the nominal value of the Ordinary Shares and Portugal Telecom undertakes that it shall not take any action, and shall procure that no action is taken, that would otherwise result in an adjustment to the Exchange Price to below such nominal value.

6.7 Change of Control

Following the occurrence of a Change of Control, the Issuer or Portugal Telecom shall give notice thereof to the Trustee and the Bondholders in accordance with Condition 17 (a **Change of Control Notice**) within 14 days of the first day on which it becomes so aware.

The Change of Control Notice shall specify the Exchange Price applicable in consequence of the Change of Control as set out in Condition 6.2(j), as adjusted where appropriate, and shall inform Bondholders of their right to exercise Exchange Rights as provided in these Conditions and their entitlement to exercise their rights to require redemption of their Bonds pursuant to Condition 7.3. The Change of Control Notice shall also specify:

- (a) all information material to Bondholders concerning the Change of Control;
- (b) the Exchange Price immediately prior to the occurrence of the Change of Control and the Exchange Price applicable pursuant to Condition 6.2(j) during the Change of Control Period;
- (c) the closing price of the Ordinary Shares as derived from the Relevant Stock Exchange as at the latest practicable date prior to the publication of such notice;
- (d) the last day of the Change of Control Period;
- (e) the Change of Control Put Date (as defined in Condition 7.3); and
- (f) such other information relating to the Change of Control as the Trustee may require.

The Trustee shall not be required to take any steps to ascertain whether a Change of Control or any event which could lead to a Change of Control has occurred or may occur.

6.8 Procedure for exercise of Exchange Rights

The Exchange Right may be exercised by a Bondholder during the Exchange Period by delivering the relevant Bond to the specified office of any Transfer and Exchange Agent during its usual business hours, accompanied by a duly completed and signed notice of exchange (an **Exchange Notice**) in the form (for the time being current) obtainable from any Transfer and

Exchange Agent. Exchange Rights shall be exercised subject in each case to any applicable fiscal or other laws or regulations applicable in the jurisdiction in which the specified office of the Transfer and Exchange Agent to whom the relevant Exchange Notice is delivered is located. If such delivery is made after the end of normal business hours or on a day which is not a business day in the place of the specified office of the relevant Transfer and Exchange Agent, such delivery shall be deemed for all purposes of these Conditions to have been made on the next following such business day.

An Exchange Notice, once delivered, shall be irrevocable.

The exchange date in respect of a Bond (the **Exchange Date**) shall be the Lisbon business day immediately following the date of the delivery of the Bonds and the Exchange Notice and, if applicable, the making of any payment to be made as provided below.

A Bondholder exercising an Exchange Right must pay directly to the relevant authorities any taxes and capital, stamp, issue and registration and transfer taxes and duties arising on exchange (other than any taxes or capital duties or stamp duties or issue, registration or transfer taxes payable in the Netherlands or Portugal in respect of the allotment and issue or transfer and delivery payable in the Netherlands or Portugal in respect of the allotment and issue or transfer and delivery of any Ordinary Shares on such exchange (including any Additional Ordinary Shares), which shall be paid by the Issuer) and such Bondholder must pay all, if any, taxes arising by reference to any disposal or deemed disposal of a Bond or interest therein in connection with such exchange. For the avoidance of doubt, the Trustee shall not be responsible for determining whether such taxes or capital, stamp, issue or registration and transfer taxes and duties are payable or the amount of such taxes or capital, stamp, issue or registration duties and it shall not be responsible or liable for any failure by the Issuer to pay such taxes or capital, stamp, issue or registration and transfer taxes and duties.

Ordinary Shares to be issued or delivered on exercise of Exchange Rights will be issued in uncertificated form through the facilities of CVM. The Ordinary Shares to be delivered will be delivered to the account of a financial intermediary at CVM specified in the relevant Exchange Notice.

The Issuer and Portugal Telecom will take all necessary steps to procure that the Ordinary Shares to be issued or delivered on exercise of Exchange Rights are issued and/or delivered as soon as possible as directed in the relevant Exchange Notice and, in particular Portugal Telecom shall execute all deeds and other documents for the issuance of share capital, if required, and deliver the same for registration to the Commercial Registry of Lisbon and all (if any) other relevant authorities within 20 Lisbon business days following the relevant Exchange Date and promptly upon such registration make all necessary filings and applications to Euronext Lisbon for the listing of such Ordinary Shares.

6.9 Ordinary Shares and Accrued Interest

- (a) Subject to Condition 6.10, a Bondholder which has exercised its Exchange Right in relation to a Bond shall not be entitled to any payment in respect of, or adjustment for interest accrued on, such Bond from (and including) the Interest Payment Date immediately preceding the applicable Exchange Date.
- (b) Ordinary Shares issued upon exchange of the Bonds will be fully paid and will in all respects rank *pari passu* with the fully paid Ordinary Shares in issue on the relevant Registration Date, except in any such case for any right excluded by mandatory provisions of applicable law and (subject to Condition 6.9(c)) except that such Ordinary Shares will not rank for any rights, distributions or payments the record date or other due date for the establishment of entitlement for which falls prior to the relevant Registration Date.
- (c) If the Exchange Date shall be prior to the date falling 2 calendar months after the end of the fiscal year of Portugal Telecom ending on or immediately preceding such Exchange Date, or shall be prior to the end of a fiscal year of Portugal Telecom, the Ordinary

Shares to be issued in respect of the relevant exercise of Exchange Rights shall in all cases rank for, and entitle the relevant Bondholder to receive, any cash Dividend declared or paid or made by Portugal Telecom in respect of such fiscal year.

- (d) If the Exchange Date shall be on or after the date falling 2 calendar months after the end of the fiscal year of Portugal Telecom ending on or immediately preceding such Exchange Date, the Ordinary Shares to be issued in respect of the relevant exercise of Exchange Rights shall not entitle the relevant Bondholder to receive any dividends or other distributions declared or paid or made with respect to the fiscal year of Portugal Telecom ended on or immediately preceding such Exchange Date.

Although the Issuer may deliver or procure the delivery of existing issued Ordinary Shares upon exercise of Exchange Rights, rather than newly issued Ordinary Shares, there is no obligation on the Issuer and/or Portugal Telecom to do so.

In view of the requirements under Portuguese law for completing various formalities required in connection with an issue of share capital, Bondholders should be aware that it may take approximately 60 days following the exercise of Exchange Rights for newly issued Ordinary Shares to be delivered to the relevant Bondholder. As a result, Bondholders exercising Exchange Rights may not be able to sell or otherwise transfer or dispose of, or exercise any rights in relation to, the Ordinary Shares to which they are entitled upon such exercise for a material period following such exercise. However, there can be no assurances that if newly issued Ordinary Shares are to be delivered to a holder upon exercise of Exchange Rights that those Ordinary Shares will be issued and delivered, and the Registration Date occur, within a 60 day period following such exercise.

6.10 Interest on Exchange

If any notice requiring the redemption of any Bonds is given pursuant to Condition 7.2 on or after the fifteenth Lisbon business day prior to a record date which has occurred since the last Interest Payment Date (or in the case of the first Interest Period, since the Closing Date) in respect of any Dividend or distribution payable in respect of the Ordinary Shares where such notice specifies a date for redemption falling on or prior to the date which is 14 days after the Interest Payment Date next following such record date, interest shall accrue on Bonds in respect of which Exchange Rights shall have been exercised and in respect of which the Exchange Date falls after such record date and on or prior to the Interest Payment Date next following such record date in respect of such Dividend or distribution, in each case from and including the preceding Interest Payment Date (or, if such Exchange Date fails before the first Interest Payment Date, from the Closing Date) to but excluding such Exchange Date. The Issuer shall pay any such interest by not later than 14 days after the relevant Exchange Date by a euro cheque drawn on, or by transfer to a euro account maintained with, a bank in a city in which banks have access to the TARGET System in accordance with instructions given by the relevant Bondholder in the relevant Exchange Notice.

6.11 Purchase or Redemption of Ordinary Shares

Portugal Telecom may exercise such rights as it may from time to time enjoy to purchase or redeem or buy back its own shares (including Ordinary Shares) or any depositary or other receipts representing the same without the consent of the Bondholders.

6.12 No duty to Monitor

The Trustee shall not be under any duty to monitor whether any event or circumstance has happened or exists which may require an adjustment to be made to the Exchange Price and will not be responsible to the Bondholders for any loss arising from any failure by it to do so.

6.13 Consolidation, Amalgamation or Merger

Without prejudice to Condition 6.2(j), in the case of (i) any consolidation, amalgamation or merger of Portugal Telecom with any other corporation (other than a consolidation), amalgamation or merger in which Portugal Telecom is the continuing corporation) (a **Successor in Business**) or (ii) any sale or transfer of all, or substantially all, of the assets of Portugal

Telecom to another entity (whether by operation of law or otherwise) (also a **Successor in Business**), Portugal Telecom will forthwith notify the Trustee and the Bondholders of such event and take such steps as shall be required by the Trustee (including the execution of a deed supplemental to or amending the Trust Deed) to ensure that each Bond then outstanding will (during the period in which Exchange Rights may be exercised) be exchanged into the class and amount of shares and other securities and property of the Successor in Business receivable upon such consolidation, amalgamation, merger, sale or transfer by a holder of the number of Ordinary Shares which would have become liable to be issued, transferred or delivered upon exercise of Exchange Rights immediately prior to such consolidation, amalgamation, merger, sale or transfer. Such supplemental deed, supplement or amendment will provide for adjustments which will be as nearly equivalent as may be practicable to the adjustments provided for in this Condition 6. The above provisions of this Condition 6.13 will apply, *mutatis mutandis* to any subsequent consolidations, amalgamations, mergers, sales of transfers.

7. REDEMPTION AND PURCHASE

7.1 Final Redemption

Unless previously purchased and cancelled, redeemed or exchanged as herein provided, the Bonds will be redeemed at their principal amount on the Final Maturity Date. The Bonds may only be redeemed at the option of the Issuer prior to the Final Maturity Date in accordance with Condition 7.2.

7.2 Redemption at the Option of the Issuer

On giving not less than 30 nor more than 60 days' notice (an **Optional Redemption Notice**) to the Trustee and to the Bondholders in accordance with Condition 17, the Issuer may redeem all but not some only of the Bonds on the date (the **Optional Redemption Date**) specified in the Optional Redemption Notice at their principal amount, together with accrued interest to such date:

- (a) at any time on or after 11 September 2010, if the Parity Value on each of at least 20 dealing days in any period of 30 consecutive dealing days ending not earlier than 14 days prior to the giving of the relevant Optional Redemption Notice, exceeds 130 per cent. of the principal amount of a Bond on each such dealing day; or
- (b) if, at any time prior to the date the relevant Optional Redemption Notice is given, Exchange Rights shall have been exercised and/or purchases (and corresponding cancellations) and/or redemptions effected in respect of 90 per cent. or more in principal amount of the Bonds originally issued.

Parity Value shall have the meaning provided in Condition 3.

7.3 Redemption at the option of Bondholders

Following the occurrence of a Change of Control, the holder of each Bond will have the right to require the Issuer to redeem that Bond on the Change of Control Put Date at its principal amount, together with accrued and unpaid interest to such date. To exercise such right, the holder of the relevant Bond must deliver such Bond to the specified office of any Agent, together with a duly completed and signed notice of exercise in the form for the time being current obtainable from the specified office of any Agent (a **Change of Control Put Exercise Notice**), at any time during the Change of Control Period. The **Change of Control Put Date** shall be the twenty-first calendar day after the expiry of the Change of Control Period.

Payment in respect of any such Bond shall be made by transfer to a euro account maintained with a bank in a city in which banks have access to the TARGET System as specified by the relevant Bondholder in the relevant Change of Control Put Exercise Notice.

A Change of Control Put Exercise Notice, once delivered, shall be irrevocable and the Issuer shall redeem all Bonds the subject of Change of Control Put Exercise Notices delivered as aforesaid on the Change of Control Put Date.

7.4 Optional Redemption Notices

Any Optional Redemption Notice shall be irrevocable. Any such notice shall specify (i) the Optional Redemption Date, (ii) the Exchange Price, the aggregate principal amount of the Bonds outstanding and the closing price of the Ordinary Shares as derived from the Relevant Stock Exchange, in each case as at the latest practicable date prior to the publication of the Optional Redemption Notice and (iii) the last day on which Exchange Rights may be exercised by Bondholders.

7.5 Purchase

Subject to the requirements (if any) of any stock exchange on which the Bonds may be listed at the relevant time and subject to compliance with applicable laws and regulations, the Issuer, Portugal Telecom or any Subsidiary of Portugal Telecom may at any time purchase Bonds in the open market or otherwise at any price.

7.6 Cancellation

All Bonds which are redeemed or in respect of which Exchange Rights are exercised will be cancelled and may not be reissued or resold. Bonds purchased by the Issuer, Portugal Telecom or any of their respective Subsidiaries shall be surrendered to the Principal Paying Agent for cancellation and may not be reissued or re-sold.

8. PAYMENTS

8.1 Principal

Payment of principal in respect of the Bonds and accrued interest payable on a redemption of the Bonds other than on an Interest Payment Date will be made to the persons shown in the Register at the close of business on the Record Date and subject to the surrender of the Bonds at the specified office of the Registrar or of any of the Agents.

8.2 Interest and other Amounts

- (a) Payments of interest due on an Interest Payment Date will be made to the persons shown in the Register at close of business on the Record Date.
- (b) Payments of all amounts other than as provided in Condition 8.1 and Condition 8.2(a) will be made as provided in these Conditions.

8.3 Record Date

Record Date means the seventh business day, in the place of the specified office of the Registrar, before the due date for the relevant payment.

8.4 Payments

Each payment in respect of the Bonds pursuant to Condition 8.1 and 8.2(a) will be made by euro cheque mailed on the due date for any payment in respect of a Bond to the holder of the relevant Bond at his address appearing in the Register on the Relevant Record Date. However, upon application by the holder to the specified office of the Registrar or any Agent not less than 15 days before the due date for any payment in respect of a Bond, such payment may be made by transfer to a euro account maintained by the payee with a bank in a city in which banks have access to the TARGET System.

Where payment is to be made by cheque, the cheque will be mailed, on the business day preceding the due date for payment or, in the case of payments referred to in Condition 8.1, if later, on the business day on which the relevant Bond is surrendered as specified in Condition 8.1 (at the risk and, if mailed at the request of the holder otherwise than by ordinary mail, expense of the holder).

8.5 Payments subject to fiscal laws

All payments in respect of the Bonds are subject in all cases to any applicable fiscal or other laws and regulations. No commissions or expenses shall be charged to the Bondholders in respect of such payments.

8.6 Taxation

All payments made by or on behalf the Issuer in respect of the Bonds or either of the Keep Well Providers under the Keep Well Agreements will be made subject to and after deduction or withholding for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the Netherlands or Portugal (as the case may be) or any political subdivision or any authority thereof or therein having power to tax required to be made by law. Neither the Issuer nor the Keep Well Providers will be required to pay any additional or further amounts in respect of such deduction or withholding.

8.7 Delay in payment

Bondholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due (i) as a result of the due date not being a business day, (ii) if the Bondholder is late in surrendering the relevant Bond or (iii) if a cheque mailed in accordance with this Condition arrives after the date for payment.

8.8 Business Days

In this Condition, **business day** means a day on which the TARGET System is operating and in the case of presentation or surrender of a Bond, a day (other than a Saturday or Sunday) on which banks and foreign exchange markets are open for business, in the place of the specified office of the Registrar or relevant Agent, to whom the relevant Bond is presented or surrendered.

8.9 Agents, etc.

The initial Agents and Registrar and their initial specified offices are listed below. The Issuer reserves the right under the Agency Agreement at any time, with the prior written approval of the Trustee (which approval shall not be unreasonably withheld or delayed), to vary or terminate the appointment of any Agent or the Registrar and appoint additional or other Agents, provided that it will (i) maintain a Principal Paying Agent, a Principal Transfer and Exchange Agent and a Registrar (which may be the Principal Transfer and Exchange Agent), (ii) maintain Agents having specified offices in at least two major European cities including, so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of that Stock Exchange so require, a Paying Agent and a Transfer and Exchange Agent with specified offices in Luxembourg, (iii) a Paying Agent and a Transfer and Exchange Agent with specified offices in a European Union member state that will not be obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any other European Union Directive implementing the conclusions of the ECOFIN council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive and (iv) maintain a Registrar with a specified office outside the United Kingdom. Notice of any change in the Agents or the Registrar or their specified offices will promptly be given by the Issuer to the Bondholders in accordance with Condition 17.

8.10 Fractions

When making payments to Bondholders, if the relevant payment is not of an amount which is a whole multiple of the smallest unit of the relevant currency in which such payment is to be made, such payment will be rounded down to the nearest unit.

9. EVENTS OF DEFAULT AND ENFORCEMENT

If any one or more of the following events (each an **Event of Default**) shall occur, the Trustee at its discretion may, and if so requested in writing by the holders of not less than one-quarter in principal amount of the Bonds then outstanding or if so directed by an Extraordinary Resolution of the Bondholders (subject in each case to being indemnified and/or secured and/or prefunded to its satisfaction) shall (but in the case of the happening of any of the events mentioned in sub-paragraph (b), (c), (d), (f) or (g) below only if the Trustee shall have certified to the Issuer and each Keep Well Provider that the occurrence of such event is, in its opinion, materially prejudicial to the interests of the Bondholders), by written notice to the Issuer and each Keep Well Provider, declare the Bonds to be, and forthwith upon such declaration the Bonds shall become, immediately due and repayable at their principal amount, together with accrued interest:

- (a) if the Issuer fails to pay any amount of any principal or interest due in respect of the Bonds or any of them and the failure continues for a period of seven days in the case of principal and 14 days in the case of interest; or
- (b) if the Issuer or any Keep Well Provider fails to perform or observe any of its other obligations under these Terms and Conditions or the Trust Deed and the failure continues for the period of 30 days next following the service by the Trustee on the Issuer and the relevant Keep Well Provider of notice requiring the same to be remedied; or
- (c) if any Indebtedness for Borrowed Money of the Issuer, any Keep Well Provider or any Material Subsidiary becomes due and repayable prematurely by reason of an event of default (however described) or the Issuer, either Keep Well Provider or any Material Subsidiary fails to make any payment in respect of any Indebtedness for Borrowed Money on the due date for payment as extended by any applicable grace period as originally provided or if the Issuer, either Keep Well Provider or any Material Subsidiary fails in making any payment due under any guarantee and/or indemnity given by it in relation to any Indebtedness for Borrowed Money of any other person, provided that no such event shall constitute an Event of Default unless the relative Indebtedness for Borrowed Money either alone or when aggregated with other Indebtedness for Borrowed Money relative to all (if any) other such events which shall have occurred shall amount to at least €20,000,000 (or its equivalent in any other currency) and provided further that, for the purposes of this Condition 9(c), the Issuer, either Keep Well Provider and any Material Subsidiary shall not be deemed to be in default with respect to such Indebtedness for Borrowed Money, guarantee or indemnity if it shall be contesting in good faith by appropriate means its liability to make payment thereunder and has been advised by independent legal advisers of recognised standing that it is reasonable for it to do so; or
- (d) if a secured party enforces its security over the whole or a substantial part of the undertaking, assets and revenues of the Issuer or either Keep Well Provider; or
- (e) save for the purposes of reorganisation on terms previously approved by the Trustee in writing or by an Extraordinary Resolution of the Bondholders, if any order is made by any competent court or an effective resolution passed for the winding up or dissolution of the Issuer or any Keep Well Provider; or
- (f) save for the purposes of reorganisation on terms approved by the Trustee in writing or by an Extraordinary Resolution of the Bondholders, if the Issuer or either Keep Well Provider ceases to carry on the whole or substantially the whole of its business (except for the purpose of a transfer of the whole or substantially the whole of its business to a Subsidiary which shall, within one business day upon the happening of such transfer, enter into a keep well agreement, in a form previously approved in writing by the Trustee, on substantially the same terms as the relevant Keep Well Agreement and shall comply with such other conditions as the Trustee may require including, but not limited to, taking steps to ensure the validity and enforceability thereof, making appropriate consequential modifications to the provisions of these Terms and Conditions and the Trust Deed, becoming a party to the Trust Deed and agreeing to be bound by the provisions thereof

and giving the requisite notifications to Bondholders) or the Issuer or any Keep Well Provider stops payment of, or is unable to, or admits inability to, pay, its debts (or any class of its debts) as they fall due, or is deemed unable to pay its debts pursuant to or for the purposes of any applicable law, or is adjudicated or found bankrupt or insolvent; or

- (g) if proceedings are initiated against the Issuer or either Keep Well Provider under any applicable liquidation, insolvency, bankruptcy, moratorium of payments, composition, reorganisation or other similar laws, or a receiver, administrator, manager or other similar official is appointed in relation to the whole or a substantial part of the undertaking, assets or revenues of the Issuer or either Keep Well Provider, or an encumbrancer takes possession of the whole or a substantial part of the undertaking, assets or revenues of either of them, or a distress, execution, attachment, sequestration or other process is levied, enforced upon, sued out or put in force against the whole or a substantial part of the undertaking, assets or revenues of any of them unless, in any such case, discharged within 45 days or contested in good faith by appropriate means by the Issuer or the relevant Keep Well Provider, and the Issuer or the relevant Keep Well Provider has been advised by recognised independent legal advisers of good repute that it is reasonable to do so; or
- (h) if the Issuer or either Keep Well Provider initiates or consents to judicial proceedings relating to itself under any applicable liquidation, insolvency, bankruptcy, moratorium of payments, composition, reorganisation or other similar laws or makes a conveyance or assignment for the benefit of, or enters into any composition or other arrangement with, its creditors generally; or
- (i) if it is or will become unlawful for the Issuer or any Keep Well Provider to perform or comply with any of its material obligations under or in respect of the Bonds, the Trust Deed or the relevant Keep Well Agreement; or
- (j) either Keep Well Agreement is terminated or any provision of either Keep Well Agreement is amended or waived in circumstances where such amendment or waiver would have, in the opinion of the Trustee, an adverse effect on the interests of the Bondholders or is not enforced in a timely manner by the Issuer or is breached by either Keep Well Provider provided that in the case of such non-enforcement or breach this has, in the opinion of the Trustee, an adverse effect on the interests of the Bondholders.

For the purposes of these Terms and Conditions:

Indebtedness for Borrowed Money means any present or future indebtedness (whether being principal, premium, interest or other amounts) for or in respect of (i) money borrowed, (ii) liabilities under or in respect of any acceptance or acceptance credit or (iii) any notes, bonds, debentures, debenture stock, loan stock or other securities offered, issued or distributed whether by way of public offer, private placing, acquisition consideration or otherwise and whether issued for cash or in whole or in part for a consideration other than cash.

Material Subsidiary means, at any particular time, a Subsidiary whose turnover represents at least ten per cent. of the consolidated turnover of Portugal Telecom and its Subsidiaries on a consolidated basis and for these purposes:

- (i) all calculations shall be made by reference to (A) the latest annual non-consolidated audited accounts of the relevant Subsidiary used for the purpose of the then latest audited consolidated annual accounts of Portugal Telecom and (B) the then latest consolidated audited annual accounts of Portugal Telecom; and
- (ii) on a Material Subsidiary transferring all or substantially all of its assets or business to another Subsidiary, the transferor shall cease to be a Material Subsidiary and any such transferee which is not already a Material Subsidiary shall thereupon be deemed to be a Material Subsidiary until publication of the next annual audited accounts after which whether it is or is not a Material Subsidiary shall be determined in accordance with (i) above.

A report by a reputable firm of accountants, approved by the Trustee, that in their opinion a Subsidiary is not or was not at any particular time a Material Subsidiary shall, in the absence of manifest error, be conclusive and binding on all parties.

Subsidiary means any company in which Portugal Telecom holds, directly or indirectly through another Subsidiary, more than 50 per cent. of the share capital or Voting Rights.

10. UNDERTAKINGS

Whilst any Exchange Right remains exercisable, Portugal Telecom will, save with the approval of an Extraordinary Resolution or with the prior written approval of the Trustee where, in its opinion, it is not materially prejudicial to the interests of the Bondholders to give such approval:

- (a) not issue or pay up any Securities, in either case by way of capitalisation of profits or reserves, other than:
 - (i) by the issue of fully paid Ordinary Shares to Shareholders and other holders of shares in the capital of the Issuer which by their terms entitle the holders thereof to receive Ordinary Shares or other Shares or Securities on a capitalisation of profits or reserves; or
 - (ii) by the issue of Ordinary Shares paid up in full (in accordance with applicable law) and issued wholly, ignoring fractional entitlements, in lieu of the whole or part of a cash dividend; or
 - (iii) by the issue of fully paid equity share capital (other than Ordinary Shares) to the holders of equity share capital of the same class and other holders of shares in the capital of the Issuer which by their terms entitle the holders thereof to receive equity share capital (other than Ordinary Shares); or
 - (iv) by the issue of Ordinary Shares or any equity share capital to, or for the benefit of, any employee or former employee, director or executive holding or formerly holding executive office of Portugal Telecom or any of its Subsidiaries or any associated company or to trustees or nominees to be held for the benefit of any such person, in any such case pursuant to an employee, director or executive share or option scheme whether for all employees, directors, or executives or any one or more of them,

unless, in any such case, the same constitutes a Dividend or otherwise gives rise (or would, but for the provisions of Condition 6.6 relating to the carry forward of adjustments or roundings, give rise) to an adjustment to the Exchange Price; or

- (b) not modify the rights attaching to the Ordinary Shares with respect to voting, dividends or liquidation nor issue any other class of equity share capital carrying any rights which are more favourable than the rights attaching to the Ordinary Shares but so that nothing in this Condition 10(b) shall prevent:
 - (i) the issue of equity share capital to employees or former employees or directors (including directors holding or formerly holding executive office or the personal service company of any such person) whether of Portugal Telecom or any of its Subsidiaries or associated companies by virtue of their office or employment pursuant, in each such case, to any employees' share or option scheme; or
 - (ii) any consolidation, reclassification or subdivision of the Ordinary Shares; or
 - (iii) any modification of such rights which is not, in the opinion of an Independent Financial Adviser (acting as an expert) materially prejudicial to the interests of the holders of the Bonds; or
 - (iv) any issue of equity share capital where the issue of such equity share capital results, or would, but for the provisions of Condition 6.6 relating to roundings or the carry forward of adjustments or the fact that the consideration per Ordinary Share receivable therefor is at least 95 per cent of the Current Market Price per Ordinary Share, otherwise result, in an adjustment to the Exchange Price; or

- (v) any issue of equity share capital or modification of rights attaching to the Ordinary Shares, where prior thereto Portugal Telecom shall have instructed an Independent Financial Adviser to determine what (if any) adjustments should be made to the Exchange Price as being fair and reasonable to take account thereof and such Independent Financial Adviser shall have determined either that no adjustment is required or that an adjustment resulting in an increase in the Exchange Price is required and, if so, the new Exchange Price as a result thereof and the basis upon which such adjustment is to be made and, in any such case, the date on which the adjustment shall take effect (and so that the adjustment shall be made and shall take effect accordingly);
- (c) procure that no Securities (whether issued by Portugal Telecom or any Subsidiary of Portugal Telecom or procured by Portugal Telecom or any Subsidiary of Portugal Telecom to be issued or issued by any other person pursuant to any arrangement with Portugal Telecom or any Subsidiary of Portugal Telecom) issued without rights to convert into, or exchange or subscribe for Ordinary Shares shall subsequently be granted such rights exercisable at a consideration per Ordinary Share which is less than 95 per cent. of the Current Market Price per Ordinary Share at the close of business on the last dealing day preceding the date of the first public announcement of the proposed inclusion of such rights unless the same gives rise (or would, but for the provisions of Condition 6.6 relating to roundings or the carry forward of adjustments, give rise) to an adjustment to the Exchange Price and that at no time shall there be in issue Ordinary Shares of differing nominal values, save where such Ordinary Shares have the same economic rights;
- (d) not make any issue, grant or distribution or any other action taken if the effect thereof would be that, on the exercise of Exchange Rights, Ordinary Shares could not, under any applicable law then in effect, be legally issued as fully paid;
- (e) not reduce its issued share capital, or any uncalled liability in respect thereof, or any non distributable reserves, except:
 - (i) pursuant to the terms of issue of the relevant share capital; or
 - (ii) by means of a purchase or redemption of share capital of Portugal Telecom including, for the avoidance of doubt, the €2.1 billion share buy back being implemented by Portugal Telecom to the extent, in any such case, permitted by applicable law; or
 - (iii) by way of transfer to reserves as permitted under applicable law; or
 - (iv) where the reduction does not include any distribution of assets; or
 - (v) to create distributable reserves; or
 - (vi) pursuant to a Newco Scheme; or
 - (vii) where the reduction is permitted by applicable law and the Trustee is advised by an Independent Financial Adviser, acting as expert, that the interests of the Bondholders will not be materially prejudiced by such reduction; or
 - (viii) where the reduction is permitted by applicable law and results in (or would, but for the provisions of Condition 6.6 relating to roundings or the carry forward of adjustments, result in) an adjustment to the Exchange Price,

provided that, without prejudice to the other provisions of these Conditions, Portugal Telecom may exercise such rights as they may from time to time enjoy pursuant to applicable law to purchase, redeem or buy back its Ordinary Shares and any depositary or other receipts or certificates representing Ordinary Shares without the consent of Bondholders;
- (f) if any offer is made to all (or as nearly as may be practicable all) Shareholders (or all (or as nearly as may be practicable all) Shareholders other than the offer or and/or any associate (or affiliate) of the offer or) to acquire the whole or a majority of the issued Ordinary Shares, or if any person proposes a scheme with regard to such acquisition, give

notice of such offer or scheme to the Bondholders at the same time as any notice thereof is sent to Shareholders (or as soon as reasonably practicable thereafter) that details concerning such offer or scheme may be obtained from the specified offices of the Agents and, where such an offer or scheme has been recommended by the board of directors of Portugal Telecom, or where such an offer has become or been declared unconditional in all respects, use all reasonable endeavours to procure that a like offer or scheme is extended to the holders of any Ordinary Shares issued during the period of the offer or scheme arising out of the exercise of the Exchange Rights by the Bondholders;

- (g) use its best endeavours to ensure that the Ordinary Shares issued upon exercise of Exchange Rights will, as soon as is practicable, be listed on the Relevant Stock Exchange and will be listed, quoted or dealt in, as soon as is practicable, on any other stock exchange or securities market on which the Ordinary Shares may then be listed or quoted or dealt in;
- (h) procure that it shall not become domiciled or resident in or subject generally to the taxing authority of any jurisdiction (other than the Netherlands) unless it would not thereafter be required pursuant to then current laws and regulations to withhold or deduct for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of such jurisdiction or any political subdivision thereof or therein having power to tax in respect of any payment on or in respect of the Bonds;
- (i) in the event of a Newco Scheme take (or shall procure that there is taken) all necessary action to ensure that (to the satisfaction of the Trustee) immediately upon completion of the scheme of arrangement or analogous proceeding, such amendments are made to these Conditions and the Trust Deed as are necessary, in the opinion of the Trustee, to ensure that (a) the Bonds may be exchanged for ordinary shares in Newco *mutatis mutandis* in accordance with and subject to these Conditions and the Trust Deed and (b) the Trust Deed and the Conditions (including, without limitation, the adjustment provisions (in Condition 6), the Events of Default (in Condition 9) and the Undertakings (in Condition 10)) provide at least the same protections and benefits to the Trustee and the Bondholders following the implementation of such Newco Scheme as they provided to the Trustee and the Bondholders prior to the implementation of the Newco Scheme, *mutatis mutandis*; and
- (j) for so long as any Bond remains outstanding, use its best endeavours to ensure that its issued and outstanding Ordinary Shares shall be listed on Euronext Lisbon or another regulated, regularly operating, recognised stock exchange or securities market in the European Union, Switzerland or the United States.

11. PRESCRIPTION

Claims against the Issuer for payment in respect of the Bonds shall be prescribed and become void unless made within 10 years (in the case of principal) or 5 years (in the case of interest) from the appropriate Relevant Date in respect of such payment. Claims in respect of any other amounts payable in respect of the Bonds shall become void unless made within 10 years following the due date for payment thereof.

12. REPLACEMENT OF BONDS

If any Bond is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of any Agent subject to all applicable laws and stock exchange requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Bonds must be surrendered before replacements will be issued.

13. MEETINGS OF BONDHOLDERS MODIFICATION, WAIVER AND SUBSTITUTION

13.1 Meetings of Bondholders

The Trust Deed contains provisions for convening meetings of Bondholders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of any of these Conditions or any provisions of the Trust Deed or the Keep Well Agreements. Such a meeting may be convened by the Issuer, either Keep Well Provider or the Trustee and shall be convened by the Issuer if requested in writing by Bondholders holding not less than 10 per cent. in principal amount of the Bonds for the time being outstanding. The quorum for any meeting convened to consider an Extraordinary Resolution will be one or more persons holding or representing more than 50 per cent. in principal amount of the Bonds for the time being outstanding, or at any adjourned meeting one or more persons present being or representing Bondholders whatever the principal amount of the Bonds so held or represented, unless the business of such meeting includes consideration of proposals, *inter alia*, (i) to modify the maturity of the Bonds or the dates on which interest is payable in respect of the Bonds, (ii) to reduce or cancel the principal amount, or interest on, the Bonds or to reduce the amount payable or redemption of the Bonds or modifying or cancelling the Exchange Rights, (iii) to increase the Exchange Price other than in accordance with these Conditions, (iv) to change the currency of any payment in respect of the Bonds, or (v) to modify the provisions concerning the quorum required at any meeting of Bondholders or the majority required to pass an Extraordinary Resolution, in which case the necessary quorum will be one or more persons holding or representing not less than three quarters, or at any adjourned meeting not less than one-half, in principal amount of the Bonds for the time being outstanding. Any Extraordinary Resolution duly passed shall be binding on Bondholders (whether or not they were present at the meeting at which such resolution was passed).

13.2 Modification and Waiver

The Trustee may agree, without the consent of the Bondholders, to (i) any modification of any of the provisions of the Trust Deed, any trust deed supplemental to the Trust Deed, the Agency Agreement, any agreement supplemental to the Agency Agreement, the Bonds, these Conditions or either Keep Well Agreement which in the Trustee's opinion is of a formal, minor or technical nature or is made to correct a manifest error or to comply with mandatory provisions of law, and (ii) any other modification to the Trust Deed, any trust deed supplemental to the Trust Deed, the Agency Agreement, any agreement supplemental to the Agency Agreement, the Bonds, these Conditions or either Keep Well Agreement, and any waiver or authorisation of any breach or proposed breach, of any of the provisions of the Trust Deed, any trust deed supplemental to the Trust Deed, the Agency Agreement, any agreement supplemental to the Agency Agreement, the Bonds, these Conditions or either Keep Well Agreement which is, in the opinion of the Trustee, not materially prejudicial to the interests of the Bondholders. The Trustee may, without the consent of the Bondholders, determine any Event of Default or a Potential Event of Default (as defined in the Trust Deed) should not be treated as such, provided that in the opinion of the Trustee, the interests of Bondholders will not be materially prejudiced thereby. Any such modification, authorisation, waiver or determination shall be binding on the Bondholders and, if the Trustee so requires, such modification shall be notified to the Bondholders promptly in accordance with Condition 17.

13.3 Substitution

The Trustee may agree, without the consent of the Bondholders, to the substitution in place of the Issuer of (i) any Successor in Business (as defined in Condition 6.13 hereto) or (ii) either Keep Well Provider or any other Subsidiary, in each case, as principal debtor under the Trust Deed and the Bonds (a **Substitution**). Such substitution shall be subject to (a) the relevant provisions of the Trust Deed, (b) save in the case of a substitution in place of the Issuer of a Successor in Business, the Bonds continuing to be convertible or exchangeable into Ordinary Shares as provided in these Conditions *mutatis mutandis* as provided in these Conditions or, in the case of a substitution in place of the Issuer of a Successor in Business, the Bonds being exchangeable into the class and amount of shares and other securities and property of the

Successor in Business as prescribed by Condition 6.13 hereto and (c) each Keep Well Provider (other than a Keep Well Provider which is substituted as principal debtor) undertaking like obligations in respect of such substituted principal debtor to those set out in the relevant Keep Well Agreement or, if applicable, such other obligations in respect of the previous principal debtor which may be in force immediately prior to the substitution in place of such Keep Well Provider's obligations under the relevant Keep Well Agreement.

13.4 Entitlement of the Trustee

In connection with the exercise by it of any of its trusts, powers, authorities and discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution), the Trustee shall have regard to the general interests of the Bondholders as a class but shall not have regard to any interests arising from circumstances particular to individual Bondholders (whatever their number) and, in particular but without limitation, shall not have regard to the consequences of any such exercise for individual Bondholders (whatever their number) resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory or any political subdivision thereof and the Trustee shall not be entitled to require, nor shall any Bondholder be entitled to claim, from the Issuer, either of the Keep Well Providers, the Trustee or any other person any indemnification or payment in respect of any tax consequence of any such exercise upon individual Bondholders.

14. ENFORCEMENT

The Trustee may, at any time at its discretion and without further notice, institute such proceedings against the Issuer and/or either Keep Well Provider as it may think fit to enforce the provisions of the Trust Deed and the Keep Well Agreements but it shall not be bound to take any such proceedings or take any other action under the Trust Deed or either Keep Well Agreement unless (i) it shall have been so directed by an Extraordinary Resolution of the Bondholders or so requested in writing by the holders of at least one-quarter in nominal amount of the Bonds then outstanding, and (ii) it shall have been indemnified and/or secured and/or prefunded to its satisfaction. No Bondholder shall be entitled (A) to proceed directly against the Issuer unless the Trustee, having become bound so to do, fails so to do within a reasonable period and such failure shall be continuing, or (B) to take proceedings to enforce the provisions of the Keep Well Agreement.

15. THE TRUSTEE

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility, including relieving it from taking proceedings unless indemnified and/or secured and/or prefunded to its satisfaction. The Trustee is entitled to enter into business transactions with the Issuer or Portugal Telecom and any entity related to the Issuer or Portugal Telecom without accounting for any profit. The Trustee may rely without liability to Bondholders on a report, confirmation or certificate or any advice of any accountants, financial advisers or investment bank, whether or not addressed to it and whether their liability in relation thereto is limited (by its terms or by any engagement letter relating thereto entered into by the Trustee or in any other manner), by reference to a monetary cap, methodology or otherwise.

16. FURTHER ISSUES

The Issuer may from time to time, without the consent of the Bondholders, create and issue further notes, bonds or debentures either having the same terms and conditions in all respects as the outstanding notes, bonds or debentures of any series (including the Bonds) or in all respects except for the first payment of interest on them and so that such further issue shall be consolidated and form a single series with the outstanding notes, bonds or debentures of any series (including the Bonds) or upon such terms as to interest, conversion, premium, redemption and otherwise as the Issuer may determine at the time of their issue. Any further notes, bonds or debentures forming a single series with the outstanding notes, bonds or debentures of any series (including the Bonds) constituted by the Trust Deed or any deed supplemental to it shall,

and any other notes, bonds or debentures may, with the consent of the Trustee, be constituted by a deed supplemental to the Trust Deed. The Trust Deed contains provisions for convening a single meeting of the Bondholders and the holders of notes, bonds or debentures of other series in certain circumstances where the Trustee so decides.

17. NOTICES

Notices to Bondholders shall be valid if published in a daily newspaper of general circulation in London (which is expected to be the Financial Times) and (so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of that Stock Exchange so require) in a leading newspaper having general circulation in Luxembourg (which is expected to be *d'Wort*) and/or the Luxembourg Stock Exchange's website, *www.bourse.lu*. Any such notice shall be deemed to have been given on the date of the last such publication as provided above.

18. CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999

No person shall have any right to enforce any term or condition of the Bonds under the Contracts (Rights of Third Parties) Act 1999.

19. GOVERNING LAW AND JURISDICTION

19.1 Governing Law

The Trust Deed, the Agency Agreement and the Bonds are governed by, and shall be construed in accordance with, English law.

19.2 Jurisdiction

The courts of England are to have jurisdiction to settle any disputes which may arise out of or in connection with the Trust Deed or the Bonds and accordingly any legal action or proceedings arising out of or in connection with the Trust Deed or the Bonds (**Proceedings**) may be brought in such courts. Each of the Issuer and each of the Keep Well Providers has in the Trust Deed irrevocably submitted to the jurisdiction of such courts and has waived any objection to Proceedings in such courts whether on the ground of venue or on the ground that the Proceedings have been brought in an inconvenient forum. This submission is made for the benefit of the Trustee and each of the Bondholders and shall not limit the right of any of them to take Proceedings in any other court of competent jurisdiction nor shall the taking of Proceedings in one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction (whether concurrently or not).

19.3 Agent for Service of Process

Each of the Issuer and each of the Keep Well Providers has irrevocably appointed Clifford Chance Securities Limited at its registered office for the time being, currently at 10 Upper Bank Street, London E14 5JJ, as its agent in England to receive service of process in any Proceedings in England. Nothing herein or in the Trust Deed shall affect the right to serve process in any other manner permitted by law.

The Bonds do not constitute obligations of, and are not guaranteed by, Portugal Telecom or PTC.

**SUMMARY OF PROVISIONS RELATING TO THE BONDS WHILE REPRESENTED
BY A GLOBAL CERTIFICATE**

1. Exchange

The Global Bond is exchangeable in whole but not in part (free of charge to the holder) for Bonds in registered form (**Definitive Bonds**) if the Global Bond is held by or on behalf of a clearing system and such clearing system is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so. Thereupon the holder may give notice to the Trustee of its intention to exchange the Global Bond for Definitive Bonds on or after the Global Bond Exchange Date (as defined below) specified in the relevant notice.

On or after the Global Bond Exchange Date the holder of the Global Bond may surrender the Global Bond to or to the order of the Principal Paying, Transfer and Exchange Agent. In exchange for the Global Bond, the Issuer will deliver, or procure the delivery of, an equal aggregate principal amount of duly executed and authenticated Definitive Bonds, security printed in accordance with any applicable legal and stock exchange requirements and in or substantially in the form set out in Schedule 1 to the Trust Deed. On exchange of the Global Bond, the Issuer will procure that it is cancelled and returned to the holder together with any relevant Definitive Bonds.

Global Bond Exchange Date means a day falling not less than 60 days after that on which the notice requiring exchange is given and on which banks are open for business in the city in which the specified office of the Principal Paying, Transfer and Exchange Agent is located.

2. Payments

Payments of principal and interest in respect of Bonds represented by the Global Bond will be made against presentation and endorsement and, if no further payment falls to be made in respect of the Bonds, surrender of the Global Bond to or to the order of the Principal Paying, Transfer and Exchange Agent or such other Paying Transfer and Exchange Agent as shall have been notified to the Bondholders for such purpose. A record of each payment so made will be endorsed on the appropriate schedule to the Global Bond, for information purposes only.

3. Notices

So long as the Bonds are represented by the Global Bond and the Global Bond is held on behalf of a clearing system, notices to Bondholders may be given by delivery of the relevant notice to that clearing system for communication by it to entitled accountholders in substitution for publication as required by the Conditions, except that so long as the Bonds are listed on the Luxembourg Stock Exchange and the rules of that Exchange so require, notices shall also be published in a leading newspaper having general circulation in Luxembourg (which is expected to be *d'Wort*) and/or the Luxembourg Stock Exchange's website, www.bourse.lu.

4. Prescription

Claims against the Issuer in respect of principal and interest on the Bonds while the Bonds are represented by the Global Bond will become void unless it is presented for payment within a period of 10 years (in the case of principal) and five years (in the case of interest) from the appropriate Relevant Date (as defined in the Conditions).

5. Purchase and Cancellation

Cancellation of any Bond required by the Conditions to be cancelled following its purchase will be effected by endorsement by or on behalf of the Principal Paying, Transfer and Exchange Agent of the reduction in the principal amount of the Global Bond.

6. Meetings

At any meeting of Bondholders, the holder of the Global Bond will be treated as having one vote in respect of each EUR50,000 in principal amount of Bonds.

7. Trustee's Powers

In considering the interests of Bondholders while the Global Bond is held on behalf of a clearing system, the Trustee may have regard to any information provided to it by such clearing system or its operator or a participant in such system as to the identity (either individually or by category) of its accountholders with entitlements to the Global Bond (or an interest in respect thereof) and may consider such interests as if such accountholders were the holder of the Global Bond.

8. Exchange Rights

The Exchange Rights in respect of the Bonds will be exercisable by presentation of the Global Bond to or to the order of the Principal Paying, Transfer and Exchange Agent for notation of exercise of the relevant Exchange Rights together with one or more duly completed Exchange Notices.

9. Redemption at the Option of the Bondholders

For so long as all of the Bonds are represented by this Global Bond and such Global Bond is held on behalf of Euroclear and/or Clearstream, Luxembourg, the option of the Bondholders provided for in Condition 7.3 may be exercised by an accountholder giving notice to the Principal Paying, Transfer and Exchange Agent in accordance with the standard procedures of Euroclear and Clearstream, Luxembourg (which may include notice being given on his instruction by Euroclear or Clearstream, Luxembourg or any common depositary for them to the Principal Paying, Transfer and Exchange Agent by electronic means) and in a form acceptable to Euroclear and Clearstream, Luxembourg of the principal amount of the Bonds in respect of which such option is exercised and at the same time presenting or procuring the presentation of the Global Bond to the Principal Paying, Transfer and Exchange Agent for notation accordingly within the time limits set forth in that Condition.

USE OF PROCEEDS

The net proceeds of the offering of the Bonds will be on-lent by the Issuer to PT and other entities in the Group for the Group's general corporate purposes.

RELATIONSHIP OF THE ISSUER WITH PORTUGAL TELECOM SGPS, S.A. AND PT COMUNICAÇÕES, S.A.

PT and PTC have each entered into a keep well agreement dated 28, August, 2007 with the Issuer (each a “Keep Well Agreement” and together the “Keep Well Agreements”) governed by English law. The following is the text of the Keep Well Agreements:

“KEEP WELL AGREEMENT

This Agreement is executed by way of deed poll and is made the 28 August, 2007 by:

- (1) PORTUGAL TELECOM, SGPS, S.A., a company incorporated under the laws of Portugal (“PT” or the “Parent”); and
- (2) PORTUGAL TELECOM INTERNATIONAL FINANCE B.V., a private company with limited liability (*besloten vennootschap met beperkte aansprakelijkheid*) incorporated under the laws of The Netherlands (the “Issuer”).

WHEREAS:

- (A) The Issuer is a direct wholly-owned subsidiary of the Parent; and
- (B) Citicorp Trustee Company Limited (the **Trustee**, which expression shall wherever the context so admits include any successor as trustee for holders of the Exchangeable Bonds (as defined below)), the Issuer and PT have entered into a trust deed dated 28 August 2007 (the **Trust Deed**) relating to the issue by the Issuer of €750,000,000 4.125 per cent. exchangeable bonds due 2014 (the **Exchangeable Bonds**).

NOW, THEREFORE, the Parent and the Issuer hereby covenant and agree as follows:

1. The Parent shall, directly or indirectly, own all of the issued and outstanding share capital of the Issuer as long as any Exchangeable Bond is outstanding and shall not pledge, grant a security interest in, encumber or alienate any of such share capital.
2. The Parent shall, with effect on and from the date of this Agreement, cause the Issuer to maintain a Tangible Net Worth (as hereinafter defined), as determined in accordance with generally accepted accounting principles in The Netherlands applied on a consistent basis as shown on the Issuer’s most recent audited balance sheet (commencing with the Issuer’s audited balance sheet at 31 December 2006), of at least one euro.

Tangible Net Worth shall mean the total assets of the Issuer less the sum of intangible assets and total liabilities of the Issuer. A certificate of the auditors of the Issuer as to the amount of Tangible Net Worth shall, in the absence of manifest error, be final and conclusive.

3. If the Issuer at any time shall have insufficient funds or other liquid assets to meet its payment obligations (including in respect of any obligations under the Exchangeable Bonds) or to repay borrowings then maturing or subsequently to mature, upon receipt of notice from the Issuer to such effect, the Parent shall make, or have made, available to the Issuer, before the due date of such payment obligations or borrowings, funds sufficient to enable the Issuer to meet such payment obligations or to repay such borrowings, as the case may be, in full as they fall due. The Issuer shall use the funds made available to it by the Parent hereunder solely for the fulfilment of its payment obligations and the repayment at maturity of its borrowings.
4. Any and all funds from time to time provided by the Parent to the Issuer pursuant to Clause 3 above shall be either (i) by way of subscription for and payment of share capital (other than redeemable share capital) of the Issuer, or (ii) by way of subordinated loan, that is to say, a loan which, and interest on which, is not permitted to be, and is not capable of being, repaid or paid unless all other debt of the Issuer has been fully satisfied and is subordinated on a winding-up of the Issuer to all of the unsecured and unpreferred creditors of the Issuer other than the Parent.

5. The Parent warrants and agrees that its payment obligations which may arise hereunder constitute unsecured and unsubordinated obligations of the Parent and rank *pari passu* with all other unsecured and unsubordinated obligations of the Parent other than those obligations which are preferred by law.
6. This Agreement is not, and nothing herein contained and nothing done by the Parent pursuant hereto shall be deemed to constitute, a guarantee, direct or indirect, by the Parent of any Exchangeable Bonds or any other debt of the Issuer (or of any subsidiary of the Issuer) or of any instrument issued by the Issuer or of any subsidiary of the Issuer.
7. If the Issuer shall be in liquidation, administration or receivership or other analogous proceedings (including if the Issuer is declared bankrupt (*faillissement*) or is granted a moratorium of payment (*surséance van betaling*) or enters into winding-up proceedings (*ontbinding*)) and the Parent shall be in default of its obligations hereunder, the Parent shall be liable to the Issuer by way of liquidated damages for such default in an amount equal to the sum that the Parent would have paid had it performed in full all of its obligations hereunder, and the Issuer and any liquidator, administrator or receiver of the Issuer or other analogous officer or official shall be entitled to claim accordingly.
8. The Parent undertakes to the Issuer that it will, in the event of failure of the Issuer to perform the same when due to be performed, procure the performance by the Issuer of its obligations under the Conditions and the Trust Deed to deliver Ordinary Shares to the Bondholders on the exercise of Exchange Rights in the manner prescribed therein.
9. This Agreement may be modified, amended or terminated only by the written agreement of the Parent and the Issuer, provided, however, that no such modification, amendment or termination shall be made which may have any adverse effect upon the holders of any Exchangeable Bonds taken as a whole while any Exchangeable Bonds are outstanding.
10. The Parent and the Issuer each hereby covenant as follows:
 - (a) it will not consent, either orally or in writing, to any modification or amendment to this Agreement which may have any adverse effect upon the Bondholders (as defined below) and it will not terminate this Agreement while any Exchangeable Bond remains outstanding;
 - (b) it will give written notice to the Trustee on behalf of the Bondholders at least 30 days prior to any proposed modification, amendment or termination of this Agreement;
 - (c) it will fully and promptly perform its obligations and exercise its rights under this Agreement and, in the case of the Issuer (without limitation to the foregoing), exercise its right to enforce performance of the terms of this Agreement by the Parent; and
 - (d) it will consent to the giving of an order of specific performance or similar relief by any court of competent jurisdiction in the event that any action is brought in respect of this Agreement.
11.
 - (a) This Agreement shall take effect as a deed poll for the benefit of the Trustee on behalf of the Bondholders. No other person, firm, company or association (unincorporated or incorporated) shall be entitled to any benefit under this Agreement whatsoever whether under the Contracts (Rights of Third Parties) Act 1999 or otherwise.
 - (b) The Parent and the Issuer hereby acknowledge and covenant that obligations binding upon it contained herein are owed to, and shall be for the benefit of the Trustee on behalf of the Bondholders.
 - (c) The Parent and the Issuer hereby further acknowledge and covenant that the Trustee shall be entitled on behalf of the Bondholders to enforce the said obligations against the Parent and the Issuer, if and only insofar as at the time the proceedings for such enforcement are instituted, any Exchangeable Bonds which have become due and payable remain unpaid in whole or in part.

- (d) This Agreement shall be deposited with and held by the Trustee for so long as the Trust Deed is in force and any Exchangeable Bonds remain outstanding. The Parent hereby acknowledges the right of the holder of any Exchangeable Bond to obtain from the Parent a copy of this Agreement.
 - (e) **Bondholder** has the same meaning in relation to each Exchangeable Bond as specified in the Terms and Conditions of the Exchangeable Bonds.
 - (f) Unless otherwise defined herein, all words and expressions defined in the Trust Deed (or the terms and conditions of the Exchangeable Bonds scheduled thereto) shall, where the context so requires and admits, have the same respective meanings in this Agreement.
- 12. This Agreement may be executed in any number of counterparts, all of which taken together shall constitute one and the same instrument.
 - 13. The Issuer and the Parent hereby irrevocably agree that the courts of England are to have jurisdiction to settle any disputes which may arise out of or in connection with this Agreement and that accordingly any suit, action or proceedings (together, **Proceedings**) arising out of or in connection with this Agreement may be brought in such courts. The Issuer and the Parent hereby irrevocably waive any objection which they may have to the laying of the venue of any Proceedings in any such courts and any claim that any such Proceedings have been brought in an inconvenient forum and hereby further irrevocably agree that a judgment in any Proceedings brought in the English courts shall be conclusive and binding upon the Issuer or the Parent, as the case may be, and may be enforced in the courts of any other jurisdiction. Nothing contained herein shall limit any right to take Proceedings against the Issuer or the Parent, as the case may be, in any other court of competent jurisdiction nor shall the taking of Proceedings in one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction, whether concurrently or not. The Issuer and the Parent hereby appoint Clifford Chance Secretaries Limited at its registered office for the time being (being at the date hereof at 10 Upper Bank Street, London E14 5JJ) as their respective agent for service of process and agree that, in the event of Clifford Chance Secretaries Limited ceasing so to act, they will appoint another person as their respective agent for service of process in England in respect of any Proceedings.
 - 14. This Agreement shall be governed by, and construed in accordance with, the laws of England.
 - 15. If the Issuer is represented by an attorney or attorneys in connection with the signing and/or execution and/or delivery of this Agreement or any agreement or document referred to herein or made pursuant hereto and the relevant power or powers of attorney is or are expressed to be governed by the laws of a particular jurisdiction, it is hereby expressly acknowledged and accepted by the other parties hereto that such laws shall govern the existence and extent of such attorney's or attorneys' authority and the effects of the exercise thereof.

KEEP WELL AGREEMENT

This Agreement is executed by way of deed poll and is made the 28 August, 2007 by:

- (1) PT COMUNICAÇÕES, S.A., a company incorporated under the laws of Portugal (“PTC”); and
- (2) PORTUGAL TELECOM INTERNATIONAL FINANCE B.V., a private company with limited liability (*besloten vennootschap met beperkte aansprakelijkheid*) incorporated under the laws of The Netherlands (the “Issuer”).

WHEREAS:

- (A) The Issuer is a direct wholly-owned subsidiary of Portugal Telecom, SGPS, S.A. (formerly known as Portugal Telecom, S.A., hereinafter referred to as **PT** or the **Parent**); and
- (B) Citicorp Trustee Company Limited (the **Trustee**, which expression shall wherever the context so admits include any successor as trustee for holders of the Exchangeable Bonds (as defined below)), the Issuer, PT and PTC have entered into a trust deed dated 28 August 2007 (the **Trust Deed**) relating to the issue by the Issuer of €750,000,000 4.125 per cent. exchangeable bonds due 2014 (the **Exchangeable Bonds**).

NOW, THEREFORE, PTC and the Issuer hereby covenant and agree as follows:

1. PTC shall, with effect on and from the date of this Agreement, cause the Issuer to maintain a Tangible Net Worth (as hereinafter defined), as determined in accordance with generally accepted accounting principles in The Netherlands applied on a consistent basis as shown on the Issuer’s most recent audited balance sheet (commencing with the Issuer’s audited balance sheet at 31 December 2006), of at least one euro.

Tangible Net Worth shall mean the total assets of the Issuer less the sum of intangible assets and total liabilities of the Issuer. A certificate of the auditors of the Issuer as to the amount of Tangible Net Worth shall, in the absence of manifest error, be final and conclusive.

2. If the Issuer at any time shall have insufficient funds or other liquid assets to meet its payment obligations (including in respect of any obligations under the Exchangeable Bonds) or to repay borrowings then maturing or subsequently to mature, upon receipt of notice from the Issuer to such effect, PTC shall make, or have made, available to the Issuer, before the due date of such payment obligations or borrowings, funds sufficient to enable the Issuer to meet such payment obligations or to repay such borrowings, as the case may be, in full as they fall due. The Issuer shall use the funds made available to it by PTC hereunder solely for the fulfilment of its payment obligations and the repayment at maturity of its borrowings.
3. Any and all funds from time to time provided by PTC to the Issuer pursuant to Clause 2 above shall be either (i) by way of subscription for and payment of share capital (other than redeemable share capital) of the Issuer, or (ii) by way of subordinated loan, that is to say, a loan which, and interest on which, is not permitted to be, and is not capable of being, repaid or paid unless all other debt of the Issuer has been fully satisfied and is subordinated on a winding-up of the Issuer to all of the unsecured and unpreferred creditors of the Issuer other than PTC.
4. PTC warrants and agrees that its payment obligations which may arise hereunder constitute unsecured and unsubordinated obligations of PTC and rank *pari passu* with all other unsecured and unsubordinated obligations of PTC other than those obligations which are preferred by law.
5. This Agreement is not, and nothing herein contained and nothing done by PTC pursuant hereto shall be deemed to constitute, a guarantee, direct or indirect, by PTC of any Exchangeable Bonds or any other debt of the Issuer (or of any subsidiary of the Issuer) or of any instrument issued by the Issuer or of any subsidiary of the Issuer.
6. If the Issuer shall be in liquidation, administration or receivership or other analogous proceedings (including if the Issuer is declared bankrupt (*faillissement*) or is granted a moratorium of payment (*surséance van betaling*) or enters into winding-up proceedings (*ontbinding*)) and PTC shall be in default of its obligations hereunder, PTC shall be liable to the Issuer by way of liquidated damages for such default in an amount equal to the sum that PTC

would have paid had it performed in full all of its obligations hereunder, and the Issuer and any liquidator, administrator or receiver of the Issuer or other analogous officer or official shall be entitled to claim accordingly.

7. This Agreement may be modified, amended or terminated only by the written agreement of PTC and the Issuer, provided, however, that no such modification, amendment or termination shall be made which may have any adverse effect upon the holders of any Exchangeable Bonds taken as a whole while any Exchangeable Bonds are outstanding.
8. PTC and the Issuer each hereby covenant as follows:
 - (a) it will not consent, either orally or in writing, to any modification or amendment to this Agreement which may have any adverse effect upon the Bondholders (as defined below) and it will not terminate this Agreement while any Exchangeable Bond remains outstanding;
 - (b) it will give written notice to the Trustee on behalf of the Bondholders at least 30 days prior to any proposed modification, amendment or termination of this Agreement;
 - (c) it will fully and promptly perform its obligations and exercise its rights under this Agreement and, in the case of the Issuer (without limitation to the foregoing), exercise its right to enforce performance of the terms of this Agreement by PTC; and
 - (d) it will consent to the giving of an order of specific performance or similar relief by any court of competent jurisdiction in the event that any action is brought in respect of this Agreement.
9.
 - (a) This Agreement shall take effect as a deed poll for the benefit of the Trustee on behalf of the Bondholders. No other person, firm, company or association (unincorporated or incorporated) shall be entitled to any benefit under this Agreement whatsoever whether under the Contracts (Rights of Third Parties) Act 1999 or otherwise.
 - (b) PTC and the Issuer hereby acknowledge and covenant that obligations binding upon it contained herein are owed to, and shall be for the benefit of the Trustee on behalf of the Bondholders.
 - (c) PTC and the Issuer hereby further acknowledge and covenant that the Trustee shall be entitled on behalf of the Bondholders to enforce the said obligations against PTC and the Issuer, if and only insofar as at the time the proceedings for such enforcement are instituted, any Exchangeable Bonds which have become due and payable remain unpaid in whole or in part.
 - (d) This Agreement shall be deposited with and held by the Trustee for so long as the Trust Deed is in force and any Exchangeable Bonds remain outstanding. PTC hereby acknowledges the right of the holder of any Exchangeable Bond to obtain from PTC a copy of this Agreement.
 - (e) **Bondholder** has the same meaning in relation to each Exchangeable Bond as specified in the Terms and Conditions of the Exchangeable Bonds.
 - (f) Unless otherwise defined herein, all words and expressions defined in the Trust Deed (or the terms and conditions of the Exchangeable Bonds scheduled thereto) shall, where the context so requires and admits, have the same respective meanings in this Agreement.
10. This Agreement may be executed in any number of counterparts, all of which taken together shall constitute one and the same instrument.
11. The Issuer and PTC hereby irrevocably agree that the courts of England are to have jurisdiction to settle any disputes which may arise out of or in connection with this Agreement and that accordingly any suit, action or proceedings (together, **Proceedings**) arising out of or in connection with this Agreement may be brought in such courts. The Issuer and PTC hereby irrevocably waive any objection which they may have to the laying of the venue of any Proceedings in any such courts and any claim that any such Proceedings have been brought in an inconvenient forum and hereby further irrevocably agree that a judgment in any Proceedings brought in the English courts shall be conclusive and binding upon the Issuer or PTC, as the

case may be, and may be enforced in the courts of any other jurisdiction. Nothing contained herein shall limit any right to take Proceedings against the Issuer or PTC, as the case may be, in any other court of competent jurisdiction nor shall the taking of Proceedings in one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction, whether concurrently or not. The Issuer and PTC hereby appoint Clifford Chance Secretaries Limited at its registered office for the time being (being at the date hereof at 10 Upper Bank Street, London E14 5JJ) as their respective agent for service of process and agree that, in the event of Clifford Chance Secretaries Limited ceasing so to act, they will appoint another person as their respective agent for service of process in England in respect of any Proceedings.

12. This Agreement shall be governed by, and construed in accordance with, the laws of England.
13. If the Issuer is represented by an attorney or attorneys in connection with the signing and/or execution and/or delivery of this Agreement or any agreement or document referred to herein or made pursuant hereto and the relevant power or powers of attorney is or are expressed to be governed by the laws of a particular jurisdiction, it is hereby expressly acknowledged and accepted by the other parties hereto that such laws shall govern the existence and extent of such attorney's or attorneys' authority and the effects of the exercise thereof.

PORTUGAL TELECOM, SGPS, S.A.

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 Portuguese Republic. Portugal Telecom was incorporated on 23 June 1994, under Decree-Law 122/94, as a result of the merger, effective 1 January 1994, of Telecom Portugal, SA, Telefones de Lisboa e Porto (TLP), S.A. and Teledifusora de Portugal, S.A.

Portugal Telecom has its registered office at Av. Fontes Pereira de Melo, No. 40, 1069-300 Lisbon, Portugal (Telephone: +351 21 500 1701) and is registered in the Lisbon Company Register, 4th Section, Registration No. 3602/94076.

According to article three of its Articles of Association, Portugal Telecom's object and purpose is to manage holdings in other companies as an indirect means of performing economic activities. Portugal Telecom manages ownership interests in operating companies. Portugal Telecom may, without restriction, acquire or hold quotas or shares in any company, as defined under Portuguese law, hold participations in complementary groups of companies or in European economic interest groups of companies and form or participate in any temporary or permanent association with public or private companies.

The Articles of Association of Portugal Telecom are available to investors on the company's website (www.telecom.pt).

Portugal Telecom provides telecommunications and multimedia services in Portugal and Brazil. In this section, references to "Portugal Telecom" or "PT" are to Portugal Telecom, SGPS, S.A. and its consolidated subsidiaries. Portugal Telecom's service offering covers a full range of:

- wireline services, which include fixed line telephone services for retail and wholesale customers, leased lines, unbundled local loop access and wholesale line rental, interconnection, Internet access (dial-up and broadband), data and business solutions, portal and e-commerce services;
- mobile telecommunications services, such as voice, data and Internet-related services;
- multimedia services, which consist of cable and satellite television services, telephony services (VoIP), broadband Internet and film distribution and screening;
- sales of telecommunications and multimedia equipment; and
- Portuguese-language television programming activities and provision of content.

In Portugal, Portugal Telecom is the leading provider of all of these services according to data provided by ANACOM. The provision of wireline services in Portugal continues to account for a large proportion of Portugal Telecom's revenues (30.1 per cent. during 2006) as compared to revenues derived from any other line of business in the group. In Brazil, Portugal Telecom has a leading position in the mobile market according to data provided by ANATEL. To strengthen Portugal Telecom's position in the Brazilian mobile telecommunications market, it entered into a strategic alliance with Telefónica Móviles S.A. ("Telefónica Móviles") (the Spanish mobile telecommunications company that has merged with and into Telefónica S.A. ("Telefónica"), the Spanish telecommunications company), pursuant to which it created, on 27 December 2002, a mobile telecommunications services company in Brazil, Brasilcel, which was rebranded Vivo on 8 April 2003.

The telecommunications market is increasingly characterized by new technological developments resulting in new opportunities and risks for telecommunications operators, the growth in demand for Internet-related services and the increasing use of information technology in telecommunications services. The key elements of Portugal Telecom's strategy include:

- enhancing the performance of its operations in the evolving domestic competitive landscape, including initiatives such as rolling out triple-play VoIP offers and offering differentiated broadband services;
- completing the announced spin-off of PT's interest in PT Multimédia, which is described in more detail below;

- seeking to promote a model of shared utilisation of mobile networks, which would facilitate the further penetration of third generation services and rapid deployment of mobile TV capabilities;
- continuing its existing partnerships and seeking to manage its international assets in a proactive manner in selected markets where it has a clear competitive advantage;
- continuing its focus on the operational enhancement of Vivo; and
- seeking to concentrate and crystallize the value of selected assets in Africa.

Portugal Telecom's specific strategies in its domestic market include the following:

Wireline

- roll out triple-play services through the launch of IP television;
- continue to develop and market voice services at flat rates;
- continue to improve the attractiveness of its broadband services by offering exclusive content and value-added services rather than focusing only on price and speed;
- in its data and corporate unit, increase its emphasis on value-added, integrated information technology and solutions to business; and
- continue to implement cost control measures in the fixed network.

Domestic Mobile

- continue to develop and bring to market innovative data and video services for third-generation mobile phones;
- consolidate leadership in the mobile market, including by building on recent gains in the corporate and youth segments; and
- seek operational savings through outsourcing and other strategies.

Group-Wide Initiatives

- seek further company-wide operating efficiencies by centralizing common functions; and
- continue to use workforce reductions to decrease its labor costs and increase its productivity over time.

In addition, Portugal Telecom will continue to seek avenues for growing its business in a manner consistent with the promotion of competition in the Portuguese telecommunications market.

One of such initiatives consists of the spin-off of PT Multimédia from the Portugal Telecom Group, which shall positively contribute to the development of the telecommunications market in Portugal, allowing the market to develop increasingly innovative and convergent services to consumers. The resulting market structure should provide regulatory relief for PT's wireline business, giving it flexibility to offer more and better services to its customers, while PT Multimédia would be able to pursue its own competitive strategy, domestically and abroad. By allowing the management of each company to focus on its core competencies, PT believes that this strategy is more likely to create greater value for shareholders over time. The proposed separation of PT Multimédia from PT also addresses the long-standing objectives of the Portuguese regulators.

Multimedia Business

In addition, in 2006 and early 2007, PT articulated a strategy for PT Multimédia based on the following points:

- grow triple-play services, which PT Multimédia's subsidiary TV Cabo launched in early 2007;
- seek further penetration by focusing on under served regions of Portugal;
- seek to stimulate demand for pay TV services by promoting development of high-quality Portuguese language content; and
- continue to focus on improvements in quality of service.

Following the completion of the proposed spin-off of PT Multimédia, that company will develop its own independent strategy that may differ from the strategy PT has articulated.

Recent Developments

Sonaecom Tender Offer

On 6 February 2006, Sonae, SGPS, S.A. and Sonaecom-SGPS, S.A. (“Sonaecom”), announced an unsolicited tender offer for all the outstanding ordinary shares (including ordinary shares represented by American Depositary Shares) of Portugal Telecom at an initial price of €9.50 in cash per share. The offer was made by Sonaecom and Sonaecom, B.V., both subsidiaries of Sonae, SGPS, S.A., a Portuguese conglomerate engaged in the distribution business, shopping center development, media and telecommunications services, information technology services and other businesses. Sonaecom also offered €5,000 in cash for each €5,000 in principal amount of outstanding convertible bonds issued by Portugal Telecom pursuant to resolutions of a general meeting of its shareholders on 5 February 2001 and of its Board of Directors on 29 November 2001.

Concurrently with its announcement of the tender offer for ordinary shares and convertible bonds of Portugal Telecom, Sonaecom announced a tender offer for all the outstanding ordinary shares of Portugal Telecom’s subsidiary PT – Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A., or PT Multimédia, for €9.03 per share.

On 15 February 2007, Sonaecom increased its offer consideration to €10.50 per share. At the extraordinary meeting of shareholders of PT held on 2 March 2007, the removal of the voting limitation in the bylaws of PT, one of the conditions of the Sonaecom offer, was rejected by the majority of the votes cast and the Sonaecom offer lapsed.

Proposed Spin-Off of PT Multimédia

On 3 August 2006, PT announced its intent to spin off its 58.43 per cent. interest in PT Multimédia through a distribution to shareholders, subject to shareholder approval. PT’s management has concluded that the separation of PT Multimédia from PT should positively contribute to the development of the telecommunications market in Portugal, allowing the market to develop increasingly innovative and convergent services to consumers. The resulting market structure should provide regulatory relief for PT’s wireline business, giving it flexibility to offer more and better services to its customers, while PT Multimédia would be able to pursue its own competitive strategy, domestically and abroad. By allowing the management of each company to focus on its core competencies, PT believes that this strategy is more likely to create greater value for shareholders over time. The proposed separation also addresses the long-standing objectives of the Portuguese regulators.

The spin off proposal approved by the shareholders grants the Board of Directors the authority to determine all the terms and conditions of the spin off to the extent not otherwise contained in the shareholder approval. These terms and conditions are expected to include non opposition from the competent regulatory authorities, including the Portuguese Securities Commission (*Comissão do Mercado de Valores Mobiliários – CMVM*), and PT cannot assure you that these conditions will be met or that they will be met on a timely basis. In addition, the implementation of the proposal will be subject to market conditions and the financial and accounting situation of Portugal Telecom. The spin off also involves the suppression of the special rights attributed to the class A shares of PT Multimédia held by Portugal Telecom by means of their conversion into ordinary shares or by other means, but PT cannot assure you that this condition will be met.

Announcement Regarding Shareholder Remuneration and Funding of Post-Retirement Benefits

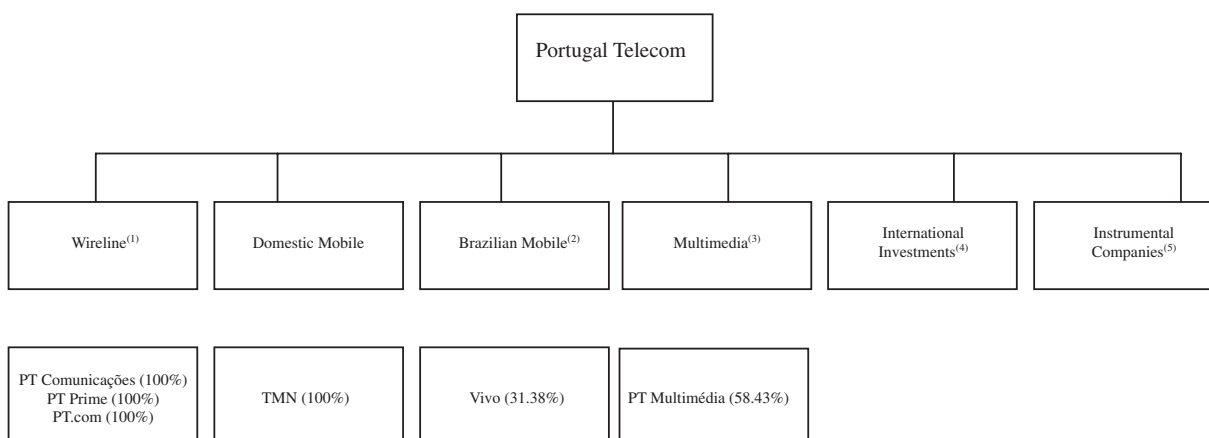
In February 2007, in connection with the PT Board response to the tender offer by Sonaecom, PT announced a shareholder remuneration package comprised of a €2.1 billion share buyback, a €0.475 per share dividend related to the year 2006, a €0.575 per share dividend related to years 2007 and 2008, and the spin-off of PT Multimédia. As of the date of this Offering Circular, PT has paid the dividend relating to the year 2006, and as at 26 July 2007, PT has entered into equity swap agreements with several financial institutions in connection with the share buyback program for 69,689,692 shares, representing 6.17% of PT share capital. In addition, PT shareholders approved the

spin-off of PT Multimédia at the annual general shareholders' meeting on 22 April 2007, but the spin-off has not yet been completed and is subject to conditions.

PT has also announced that it intends to contribute €1.0 billion between 2006 and 2008 to fund post-retirement benefits, upon achieving an improved labour relations framework.

Business Units

Portugal Telecom's market is characterized by increasing competition and rapid technological change. In 1999, Portugal Telecom's Board of Directors adopted a plan to reorganise the company to better position it in this competitive market. As part of its reorganisation, 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 it aligned its subsidiaries according to business lines. Portugal Telecom's business unit subsidiaries are held directly and indirectly by Portugal Telecom in its role as holding company. Portugal Telecom has integrated different functions across the board, with particular emphasis on information systems (PT Sistemas de Informação), research and development capabilities (PT Inovação), back office activities (PT Pro), central purchasing capabilities (PT Compras) and call centre operations (PT Contact). In addition, in April 2004 Portugal Telecom created Portugal Telecom Investimentos Internacionais-Consultoria Internacional, S.A. to manage all of its international businesses. The diagram below presents Portugal Telecom's different businesses as of 30 June 2006.



- (1) Providing wireline services in Portugal, including PT's fixed telephone service, Internet access services, wholesale services and data and business solutions services.
- (2) Providing multimedia services in Portugal, including cable operations through TV Cabo, audiovisuals services through Lusomundo Audiovisuals and Lusomundo Cíneas, and media services through Lusomundo Media.
- (3) Various international investments, including global telecommunications operators in Cabo Verde Islands, São Tomé e Príncipe Islands and Macao, mobile operators in Namibia, Morocco and Angola, and other investments in various countries.
- (4) Various instrumental companies providing services to PT Group companies, including PT Sistemas de Informação (information systems), PT Inovação (research and development), PT Pro (shared services), PT Compras (central purchasing) and PT Contact (call centres).

The following table sets forth the operating revenues (in millions of euro's) of each of PT's major business lines, on a standalone basis, for the years ended 31 December 2005 and 2006 and for the six months ended 30 June 2006 and 2007.

	<i>Year Ended 31 December</i>			<i>Six Months ended 30 June</i>	
	<i>2004</i>	<i>2005</i>	<i>2006</i>	<i>2006</i>	<i>2007</i>
Wireline Business:					
Retail	1,379.4	1,318.8	1,173.5	607.1	525.9
Wholesale	476.4	457.7	464.2	230.7	235.2
Data and Corporate	242.0	244.9	250.5	124.5	133.7
Directories	129.7	120.4	108.9	55.8	49.4
Sales	36.1	34.2	32.8	14.8	20.9
Other	41.5	37.7	41.9	20.5	27.8
Total	2,305.2	2,213.6	2,071.8	1,053.5	992.9
Domestic Mobile Business:					
Services	1,446.3	1,403.6	1,363.2	661.7	666.5
Sales	153.3	146.3	129.7	53.9	57.1
Other	6.7	7.1	9.4	4.4	4.5
Total	1,606.3	1,557.1	1,502.4	719.9	728.1
Multimedia Business⁽¹⁾					
Pay TV and Cable Internet	513.3	553.0	591.1	—	—
Audiovisuals	53.7	53.4	52.6	—	—
Cinema Exhibition	41.8	40.0	43.7	—	—
Other and eliminations	(10.0)	(18.0)	(20.9)	—	—
Total	598.8	628.5	666.5	—	—
Brazilian Mobile Business:					
Services	1,425.3	1,737.8	1,789.8	855.3	1,033.0
Sales	136.6	233.8	254.8	135.9	88.0
Other	37.3	65.3	60.2	23.1	19.3
Total	1,599.1	2,036.9	2,104.7	1,014.4	1,140.3
Other Businesses	163.2	215.2	238.2	114.3	189.1
Eliminations in consolidation	(305.1)	(265.8)	(240.6)	(96.4)	(94.7)
Total consolidated operating revenues....	5,967.4	6,385.4	6,342.9	2,805.7	2,955.8

(1) Following the approval of the PT Multimédia spin-off at PT's Annual Shareholders' Meeting on 27 April 2007, PT Multimédia has been considered for reporting purposes as a discontinued operation.

Wireline Business

PT's wireline business consists of the four operating companies, PT Comunicações, PT Prime, PT.com and PT Corporate, which provide the following services on its wireline network:

- retail, including fixed line telephone services and Internet access services to residential and small office home office customers;
- wholesale, including leased lines, interconnection services, unbundled access to its local loops, and transmission of television and radio signals;

- data and corporate, including data communications, leased lines to major clients, network managing and outsourcing; and
- other wireline services, including its directories business and sales of telecommunications equipment.

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

PT Prime offers corporate customers in Portugal data and corporate services through a "one-stop-shop" for a variety of flexible, efficient and innovative solutions using information technology, telecommunications, Internet and outsourcing. Before October 2003, PT held 87.5 per cent. of the share capital of PT Prime. In October 2003, PT acquired the remaining share capital of PT Prime from SIBS-Sociedade Interbancária de Serviços S.A., a Portuguese entity operating the ATM network and the inter-bank payment system in Portugal, for €39 million.

PT.com is the leading Internet company in Portugal, operating as an Internet Service Provider ("ISP"), using PT's fixed line network and the brands SAPO and Telepac, as well as in portal and related activities through sapo.pt, Portugal's leading Internet portal. PT.com was formed as PT Multimédia.com, or PTM.com, in March 2000 by PT Multimédia to aggregate all of its Internet activities focused on the residential and small and medium-sized enterprise markets. In October 2002, PT entered into an agreement with PT Multimédia to acquire its 100 per cent. interest in PTM.com. The sale of PT Multimédia's Internet business to PT was intended to encourage the continued growth of PT's broadband businesses and increase the loyalty of fixed line subscribers, while providing a single platform for investment and development of on-line services and content for the Portugal Telecom group. The results from PT services provided through PTM.com, renamed PT.com in November 2004, have been included in its wireline business segment since 2003.

PT Corporate, launched in July 2003, serves the largest economic groups and government related entities in Portugal, and acts as a single interface for every company within the PT Group, with the authority to represent, negotiate and sign in the name of each PT Group company. PT Corporate offers these large corporate customers solutions for fixed and mobile telecommunications, internet, technologies and information systems and outsourcing. Due to the size and specific business requirements of its clients, PT Corporate was created to contribute to its clients' business success by assuring the integrated and optimized development of their systems and information processes.

Fixed Line Network. PT had 4,342 million telephone and ADSL access lines in service at 30 June 2007, excluding external supplementary lines, direct extensions and active multiple numbers. PT breaks down its fixed line network into traditional main lines (PSTN), ISDN lines and asymmetric digital subscriber lines (ADSL) lines. Because of their large capacity, PT counts 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. PT offers high-speed Internet access through ADSL lines. As of 30 June 2007, PT had 779 thousand ADSL lines, of which 715 thousand were attributable to PT's ADSL retail business (which is operated by PT.com), and 3,146 thousand PSTN/ISDN lines, of which 75.6 per cent. were residential/small office home office clients, 18.4 per cent. were business and the remainder were mainly payphones, wholesale lines and other.

The following table shows the number of PT's main lines by category.

	<i>As of 31 December</i>					<i>As of</i>
	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>	<i>30th June, 2007</i>
Fixed line main lines in service (thousands)						
Traditional main lines	3,317	3,224	3,165	3,011	2,589	2,430
ISDN main line equivalents	826	813	783	758	727	716
ADSL	53	188	420	637	749	779
Unbundled local loop (ULL)	—	—	9	72	196	244
Wholesale line rental (WLR)	—	—	—	—	142	173
Total	4,196	4,225	4,377	4,478	4,404	4,342
PSTN/ISDN fixed line main lines per 100 inhabitants	41.9	41.2	40.6	40.5	40.4	n.a.
Public pay phones (thousands)	43.8	41.4	47.3	57.8	67.7	64.5

Over past years, PT has made significant investments to meet subscriber demand for lines and to modernize its fixed line network. As a result, the number of PSTN/ISDN lines per 100 inhabitants has almost doubled from 20.9 fixed line main lines at the end of 1989 to approximately 40.4 fixed line main lines at the end of 2006.

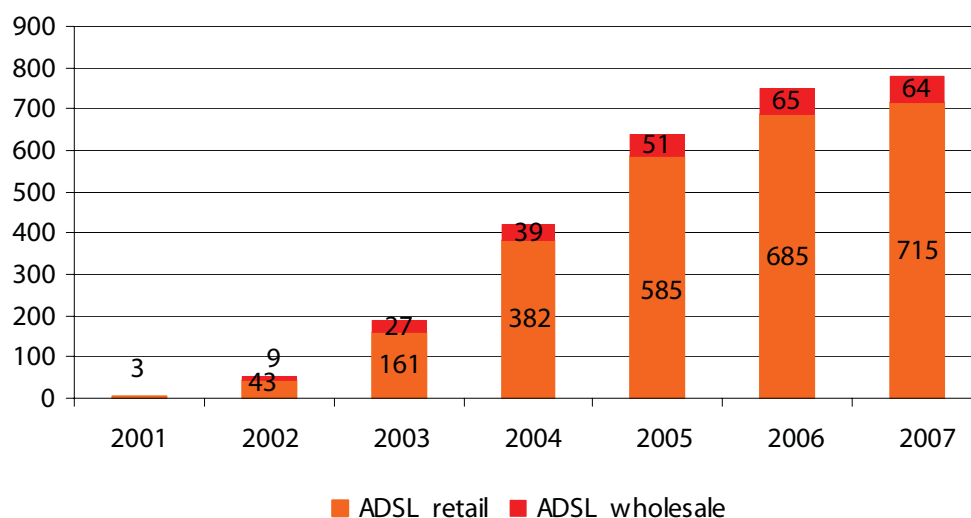
In September 1999, the number of active mobile cards (the mobile equivalent of main lines) overtook the number of fixed line main lines in Portugal, and traffic that once was transmitted in whole or in part on PT's fixed line network is being carried on its mobile network or on the network of other mobile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

All of PT's local switches in Portugal have been digital since 1999. Digital technology is used on all long distance and trunk connections. This level of digitalisation of its fixed line network permits PT 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 2006, PT Comunicações was providing approximately 1,089 thousand voice mail boxes.

PT has offered ISDN services commercially since 1994. PT offers a basic-rate service, which provides two communications channels. It also offers a primary-rate service which provides up to 30 communications channels. At the end of December 2006, PT had 249,069 subscribers to the basic-rate ISDN service and 7,640 subscribers to the primary-rate ISDN service. By the end of 2006, ISDN lines represented 21.9 per cent. of its total equivalent fixed line main lines, as compared with 20.1 per cent. one year before. The conversion of traditional main lines to ISDN lines results in increased quality of service, and PT's ISDN subscribers tend to produce higher levels of usage per line than traditional main line subscribers.

PT launched ADSL service in Lisbon and Oporto in 2002 and now covers virtually all of Portugal. PT offers ADSL lines both to retail customers, such as residential customers and small and medium-sized businesses, and to wholesale customers. During 2004, PT focused on customer retention and loyalty in order to turn around the wireline business. The aggressive rollout of ADSL was central to this strategy. Throughout 2004, new broadband products and offers were launched, including the launch of one of the first broadband prepaid offers in Europe and the revamping of the ADSL product brand, Sapo ADSL. In 2005, PT continued to improve the quality of services and customer care and to innovate, launching electronic billing with legal validity, VoIP and video services on SAPO Messenger, the group's instant messenger service. In 2006 PT continued to deploy ADSL as one of its principal strategies, increasing geographic coverage to almost all of Portugal and increasing transmission speeds, namely through the launch of ADSL2+ services. PT also introduced new pricing plans targeted to specific customer needs. The following chart shows the evolution of PT's ADSL retail and wholesale customer base for the periods indicated (2007 refers to the first half of 2007).

ADSL Customers
(Thousand)



PT had 0.2 billing complaints per 1,000 bills and 12.9 reported faults per 100 main lines in the year ended 31st December, 2006. The percentage of faults repaired in less than 12 working hours was 77.7 per cent. in 2006, compared with 79.4 per cent. in 2005. PT offers residential customers detailed billing on request without extra charge.

Traffic. Total traffic originated on the network has been decreasing since 2002, primarily because consumers have increasingly used mobile service instead of fixed line service and because of the migration of dial-up Internet users to ADSL. Traffic decreased by 15 per cent. from the six months ended 30th June, 2006 to the six months ended 30th June, 2007.

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

Total Growth of Originated Traffic

Year Ended 31 December

	2002		2003		2004		2005		2006	
	<i>Millions of minutes</i>	<i>%</i>	<i>Millions of minutes</i>	<i>%</i>	<i>Millions of minutes</i>	<i>%</i>	<i>Millions of minutes</i>	<i>%</i>	<i>Millions of minutes</i>	<i>%</i>
Domestic	6,480	39.6	5,841	40.1	5,236	42.8	4,669	44.7	4,002	46.2
International	402	2.5	382	2.6	372	3.0	411	3.9	395	4.6
Fixed-to-mobile	1,119	6.8	1,023	7.0	918	7.4	844	8.1	730	8.4
Internet	6,581	40.3	5,023	34.5	3,151	25.3	1,818	17.4	920	10.6
Other	1,758	10.8	2,294	15.8	2,673	21.5	2,704	25.9	2,622	30.2
Total	16,340	100.0	14,563	100.0	12,440	100.0	10,446	100.0	8,669	100.0

Six Months Ended 30th June.

	2006		2007	
	<i>Millions of minutes</i>	%	<i>Millions of minutes</i>	%
Domestic.....	2,078	45.6	1,851	47.9
International.....	198	4.4	192	5.0
Fixed-to-mobile	370	8.1	345	8.9
Internet	559	12.3	231	6.0
Other.....	1,345	29.6	1,246	32.2
Total	4,550	100.0	3,865	100.0

PT offers other ISPs access to its network under one of two regulated access regimes that may be chosen by the ISP: (1) the Reference Offer for Internet Access, which allows ISPs either to pay PT a call origination charge and a fee for invoicing customers on their behalf or to pay a wholesale flat rate and bill their customers directly or (2) the Reference Interconnection Offer, which offers two different billing structures based on call origination, with variations based on the manner in which the ISPs’ infrastructures are connected to PT’s network and billing arrangements. For additional information, see “– Regulation – Portugal – Interconnection – Internet Access”.

PT is required to provide carrier selection to its customers on all kinds of traffic. Carrier selection has been an additional factor that has contributed to the reduction in traffic on PT’s network. In addition, in January 2006, ANACOM, the Portuguese telecommunications regulator, published regulations permitting carrier pre-selection of non-geographic services, such as toll-free numbers.

Except for customer pre-selection and Internet traffic, PT accounts for traffic originating on its network in its fixed line telephone services unit, and PT allocates the revenue billed to customers to that unit. Traffic originating on other networks but terminating on PT’s network, and the related revenue, is allocated to PT’s wholesale unit.

Marketing. PT has increased marketing efforts aimed at customer loyalty and promoting increased usage of PT’s wireline telephone services.

Promotional Efforts and Market Analysis. PT aggressively promoted the sale of products and services targeted to specific customers in 2006 through, among other things:

- a 17.7 per cent. increase in 2006 of ADSL accesses to 749 thousand, with the rate of service coverage of PT’s network reaching nearly 100 per cent. in 2006, compared to 99.4 per cent. in 2005;
- the doubling of access speeds with the introduction of ADSL2+;
- the launch of new flat-rate pricing plans allowing unlimited calls for various time slots, namely “PT Total 50 per cent.”, “PT Fixo-Móvel Preferido” and “Noites Grátis+Local PT”. In particular, the “PT Fixo-Móvel Preferido” plan allows customers to make calls to a selected mobile network at €0.15 per minute, while paying the usual price to the other two mobile networks with no additional fee. The total number of pricing plans reached 4.2 million at 30 June 2007;
- the expansion of “telesafety” and video surveillance products through partnerships in the real estate sector;
- the launch of the SMS Agenda, which allows wireline telephones to store the most frequently dialed telephone numbers;
- the launch of the instant messenger service Instant Messaging of Sapo Messenger. Sapo Messenger had 641 thousand users at the end of 2006;

- the launch of several campaigns with strong acceptance from customers, namely a Valentine's Day campaign, a campaign allowing free telephone calls placed on the days the Portuguese soccer team played in Germany during the 2006 World Cup and a Christmas campaign;
- a summer Wi-Fi campaign offering 1,000 open hotspots with Wi-Fi access for PT's ADSL clients;
- the development and launch of a new blog platform in line with international best practices; and
- the launch of voice over Internet protocol (VoIP) with a monthly average of 13 thousand users.

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

Customer Care. To provide support and marketing services to its residential and business customers, PT has developed a network of regional organizations and retail service centers. In addition, PT 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's customer service representatives to access the history of customers' telephone use and commercial dealings with PT.

Increased Selling Efforts. PT has developed a distribution network through its retail service centers and agents such as supermarkets and other retail outlets. PT's customer support system allows it to develop and implement strategies to sell new and expanded services to its customers. PT often uses telemarketing to both the residential and small and medium sized enterprise market segments to develop closer relationships with its customers.

In 2006, PT continued to pursue its strategy of market segmentation, namely its residential and business market segments, and established partnerships between subsidiaries of Portugal Telecom to offer integrated telecommunications solutions to corporate customers, including simpler voice services and integrated website solutions. PT also executed agreements with corporate associations to benefit small businesses.

Retail

Fixed Line Telephone Services. PT provides public fixed line telephone services in Portugal to retail customers, primarily through its subsidiary PT Comunicações. This business area provided €1,173.5 million and €1,318.8 million during 2006 and 2005, respectively, and provided €525.9 million and €607.1 million during the six months ended 30 June 2007 and 2006, respectively. PT distinguishes between two principal sources of revenue in the provision of fixed telephone services:

- *Fixed charges*, including network access charges based on a monthly line rental and an initial installation fee, as well as (in most cases) a monthly fee from pricing packages; and
- *Traffic*, including charges for the use of PT's fixed line network based on rates dependent on amount and type of usage.

PT divides traffic into domestic and international traffic. Domestic traffic consists of domestic telephone services provided by PT Comunicações directly to subscribers that originate or terminate calls on PT's fixed line network. International traffic consists of international telephone services provided by PT Comunicações directly to users that originate calls on PT's fixed line network.

Since 2000, public switched fixed line telephone services in Portugal have been fully open to competition. As a result of this competition, as well as the trend toward use of mobile services instead of fixed line services, PT has experienced, and expects to continue to experience, erosion of market share of both access lines and of outgoing domestic and international traffic. See “–*Competition – Competition Facing PT's Wireline Business*”.

Fixed Charges. PT Comunicações fixed charges to domestic fixed line telephone subscribers include a one-time installation charge and a monthly line rental fee. These fixed charges provided

€568.1 million and €618.8 million to PT's wireline operating revenues during 2006 and 2005, respectively, and provided €249.2 million and €294.7 million during the six months ended 30 June 2007 and 2006, respectively.

In July 2005, PT created two different tariffs; one for the residential market and another for the business market. The installation charge remained the same for both markets, €71.83. The standard line rental fee was €12.66 for the residential market and €12.98 for the business market. The fee for basic ISDN lines was €26.46 per month for both markets. The chart below illustrates changes in PT's prices and fees from 2002 through 2006. All prices are in Euros and exclude VAT.

Fixed Fees for Fixed Line Telephone Services⁽¹⁾

	<i>As at December 31</i>				
	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>
Installation fee	71.83	71.83	71.83	71.83	71.83
Line rental per month.....	11.85	12.3	12.66	12.66	12.66 (residential) 12.98 (business)

(1) Amounts rounded to nearest hundredth

Traffic. Traffic contributed €425.1 million and €534.6 million to PT's wireline operating revenues during 2006 and 2005, respectively, and contributed €183.9 million and €222.7 million during the six months ended 30th June, 2007 and 2006, respectively. Measured in minutes, total fixed line traffic originating on PT's wireline network decreased by 17.0 per cent. in 2006, compared with 2005. The decrease was primarily due to the continuing effect of the trend toward use of mobile services instead of fixed line services and the migration of Internet users to ADSL.

Domestic. Domestic traffic contributed €372.7 million and €469.2 million to PT's wireline business's operating revenues in 2006 and 2005, respectively.

Prices. Since July 2006, PT has had two domestic tariffs: local (former local + regional) and national. Between the end of 2001 and the end of 2006, weighted average prices for domestic fixed line telephone services decreased by 0.83 per cent. per year in nominal terms. Compared with 2005, domestic prices decreased a further 1.0 per cent. over the course of 2006 in nominal, annualized terms. See “– Regulation – Portugal – Pricing of Wireline Services”.

The chart below illustrates changes in PT prices from 2002 through 2006. The call prices from 2002 through 2006 are for a three-minute call at peak rates in 2006 constant prices. All prices are in Euros and exclude VAT.

Principal Prices for Domestic Fixed Line Telephone Services⁽¹⁾

	<i>As at December 31</i>				
	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>
Local call prices	0.12	0.12	0.13	0.12	0.12 (residential) 0.13 (business)
Regional call prices	0.23	0.21	0.16	0.12	0.12 (residential) 0.13 (business)
National call prices	0.33	0.29	0.20	0.19	0.19 (residential) 0.19 (business)

(1) Amounts rounded to nearest hundredth.

PT's pricing structure has come more into line with pricing structures in the rest of the EU over the last ten years.

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

International. Revenues from international fixed line telephone services come primarily from charges to its individual and business subscribers in Portugal for outgoing calls. Revenues from international fixed line telephone services have generally decreased in recent years as a result of decreases in international traffic and prices for outgoing international calls, although traffic increased in 2005 as a result of growth in traffic from prepaid international calling cards.

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 receives higher payments from other international telecommunications operators than PT pays out to these operators. PT periodically renegotiates the amount of the payments with these operators.

In recent years, the billing rates among operators have been declining steadily, both for incoming and outgoing traffic. PT estimates that, on an aggregate basis in Euros, termination rates for international traffic at the end of 2006 decreased by a weighted average of approximately 17.0 per cent. for incoming traffic and 18.4 per cent. for outgoing traffic compared to the end of 2005.

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

Prices. PT sets traffic charges for international fixed line telephone services by groups of countries. Within each group, PT 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 2002 and the end of 2006, PT experienced aggregate reductions in real terms of 3.7 per cent. in international traffic prices.

The table below shows changes in prices for PT's international fixed line telephone services to selected destinations since 2002. The prices for 2002 through 2006 are peak rate prices per minute on the basis of a three-minute call, set at 2006 constant prices. They are in Euros and exclude VAT.

Selected Prices for the International Services⁽¹⁾

As of December 31

	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>
EU ⁽²⁾	0.27	0.27	0.27	0.27	0.27
Other European countries ⁽³⁾	0.61	0.61	0.61	0.61	0.61
United States	0.28	0.28	0.28	0.28	0.28
Canada	0.28	0.28	0.28	0.28	0.28
Brazil	0.57	0.57	0.57	0.57	0.57

(1) Euro amounts rounded to nearest hundredth.

(2) Including Switzerland.

(3) Excluding Norway and Iceland.

ADSL Services and ISPs. PT is the leader in providing Internet access in Portugal. As at 31 December 2006, PT had approximately 685 thousand ADSL retail customers, which represented an overall increase of 17 per cent. over the previous year. PT also offers dial-up paid and free Internet access services. In 2006, revenues from ADSL services grew 13 per cent. to €170.1 million, more than offsetting a 31.5 per cent. decline in dial-up revenues to €10.2 million, as increasing numbers of people switched to broadband service.

As at 30 June 2007, PT had approximately 715 thousand ADSL retail customers, which represented an overall increase of 12.5 per cent. over the total as of 30 June 2006. In the six months ended 30 June 2007, revenues from ADSL services grew 7.0 per cent. to 90.1 million compared to the six months ended 30 June 2006, more than offsetting a 51.0 per cent. decline in dial-up revenues to 2.7 million, as increasing numbers of people switched to broadband service.

Application Service Provider (“ASP”). PT also provides ASP services in Portugal, which include remote applications services, web hosting and web design services to small and medium-sized enterprises. PT had approximately 2,589 customers for its ASP business at 31 December 2006.

ISP Traffic Revenues. PT.com offers Internet access through the lines of PT’s fixed line network. PT.com retains all of the revenues from Internet traffic and pays PT Comunicações for use of the fixed line network.

In the second quarter of 2007, PT announced the soft launch of IPTV services. The triple-play offer, branded “meo”, includes 42 pay-TV channels (of which 10 are a la carte), a broadband access of up to 8MB and unlimited fixed-to-fixed calls for a total of Euro 54.90 per month. Additionally, customers can buy premium channels, such as SportTV (premium sports) and the Lusomundo movie channels. The service is provided using ADSL 2+ and is available for up to two televisions per home. PT was the first operator in Portugal to introduce HDTV and has the most extensive VOD offer in the market. The service is being initially rolled out in Lisbon and Oporto.

Wholesale

PT’s wireline wholesale services business, which is provided primarily through PT Comunicações, consists of:

- domestic and international interconnection telephone services which it provides to other telecommunications service providers in Portugal, including other companies in the PT Group;
- provision of carrier pre-selection and number portability;
- leasing of domestic and international lines to other telecommunications service providers and Portuguese cable television operators, including other companies in the PT Group;
- provision of ADSL on a wholesale basis to other ISPs, including other companies within the PT Group;
- transmission of television and radio signals for major broadcast television companies in Portugal;
- narrowband Internet access origination services, which PT provides to ISPs;
- other services provided to telecommunications service providers and operators, such as local loop unbundling and IP international connectivity;
- provision of co-location services and duct sharing to cable television companies; and
- provision of wholesale line rental.

Wholesale services provided €464.2 million and €457.7 million to PT’s wireline operating revenues in 2006 and 2005, respectively. Wholesale services provided €235.2 million and €230.7 million in the first half of 2007 and the first half of 2006, respectively.

Traffic. Interconnection and narrowband Internet access traffic comprised about 45 per cent. of PT’s wholesale business in terms of revenues in 2006. The service providers who purchase interconnection services include fixed and mobile network operators, telephony and data communications service providers, ISPs, value-added service providers and service providers whose international calls are terminated on or carried by PT’s network. Providing interconnection services means allowing third parties to connect their networks to PT’s network, and vice versa. PT has interconnection rates for call termination, call origination, transits and international interconnection. In 2006, interconnection rates per minute for call termination included local transit rates equal to €0.0064, single transit rates equal to €0.0093 and double transit rates equal to €0.0144, each based on a three-minute call made during peak hours. PT published the latest version of its reference offer for unbundled access to its local loops in September 2006 and since then have made available to its

competitors, where technical and space conditions are available, all of its local switches, 191 of which are co-located. Co-location means providing space and technical facilities to competitors to the extent necessary to reasonably accommodate and connect the relevant equipment of the competitor. See “– Regulation-Portugal – Unbundling of the Local Loop” and “– Regulation – Portugal – Number Portability and Carrier Selection”.

Wholesale traffic is generated by the interconnection portion of PT’s wholesale business, which decreased by 6.5 per cent. in 2006 compared with 2005 and 7.7 per cent. in the six months ended 30 June 2007 compared with the six months ended 30 June 2006. This decrease was primarily due to a decrease in Internet traffic, which was partially compensated for by increases in indirect access traffic. The following table sets forth the total amount of wholesale domestic traffic on PT’s fixed line network during the period 2002 through 2006.

Wholesale Domestic Traffic					
(millions of minutes)					
<i>Year ended December 31</i>					
	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Mobile ⁽¹⁾	998	959	912	880	840
Internet	6,581	5,023	3,151	1,818	920
International ⁽²⁾	1,420	1,318	1,413	1,581	1,779
Other ⁽³⁾	2,831	3,008	3,753	4,139	4,328
Total	<u>11,830</u>	<u>10,308</u>	<u>9,229</u>	<u>8,418</u>	<u>7,867</u>

(1) Reflects mobile-to-fixed calls terminated on PT’s fixed line network.

(2) Includes incoming international traffic (both fixed and mobile), outgoing international traffic from other operators using PT’s network and transit traffic.

(3) Includes fixed-to-fixed calls terminated on PT’s fixed line network, calls originated on PT’s network through indirect access through other operators and other traffic.

In the six months ended 30 June 2007, PT had total wholesale traffic of 3,705 million minutes, compared to 4,012 million minutes in the six months ended 30 June 2006.

Leased Lines. PT leases lines to other telecommunications providers for fixed, mobile and data communications services, including its other subsidiaries and competitors. Since 1996, PT has been leasing lines to resellers who offer voice services to corporate networks and closed user groups. Leased line services involve making a permanent point-to-point connection with dedicated and transparent capacity between two geographically separate points. PT offers a minimum set of leased lines (up to 2 Mbps) at the retail level to medium and large businesses, plus larger capacities on a commercial basis. In addition, PT offers terminating segments and trunk segments at the wholesale level to telecommunications providers. PT’s Concession requires it to provide leased lines to third parties.

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

Prices. The net prices and fees PT receives from providing access to its fixed line network on a wholesale basis are less per minute than those PT charges for domestic and international fixed line telephone services.

Domestic interconnection revenue per minute for calls terminated on PT’s network declined by 7.8 per cent. in nominal terms in 2006 compared with 2005. International interconnection revenue per minute declined by 21.0 per cent. in nominal terms in 2006 compared with 2005. In accordance with EU and Portuguese regulations, PT’s interconnection prices are based on PT’s costs (which are audited by ANACOM) plus a margin.

Data and Corporate Services

PT provides data and corporate services within its wireline business to top corporate and business customers that need complex telecommunications solutions, including:

- digital leased lines;
- broadband data and IP/MPLS Ethernet solutions;
- networking and systems integration solutions;
- Internet-related services and applications including Intranet and Extranet services;
- interactive systems and related applications;
- outsourcing of telecommunications application systems;
- consultancy services;
- web design and site management;
- fixed line and mobile convergence services;
- business-to-business e-commerce;
- security and disaster recovery solutions;
- housing and hosting solutions, including application service provider, or ASP, and enterprise resource planning, or ERP; and
- telephone services using Internet protocol.

PT is the leading supplier of the full range of these services in Portugal. Data and corporate operating revenues contributed €250.5 million and €244.9 million to PT's wireline operating revenues in 2006 and 2005, respectively.

Services. PT has developed a full range of telecommunications services for businesses, and PT integrates these services (together with other services it offers, such as fixed line services and domestic mobile services) to provide its customers with service packages. By combining its communications capabilities with its software-based integrated systems and applications, PT offers integrated voice, data and image solutions, virtual private networks, convergence solutions, consultancy and outsourcing. PT believes it is the primary service provider in Portugal capable of offering customers a full range of integrated and customized services. Despite increasing competition, overall demand for data and corporate services has been increasing. As a result of competition, PT has reduced its prices for leased lines and data services.

PT offers services in partnership with leading operators and service providers such as Telefónica, British Telecom, Orange and BT-Infonet. PT uses systems and networks in partnership with Siemens, Alcatel, Cisco Systems, Motorola, Nortel Networks and Matra/EADS Telecom.

PT leases lines and broadband capacity to large businesses for data communications and other private uses and provides related services. PT also provides integrated voice and data services to corporate customers. PT offers X.25/X.32 synchronous services and X.28 asynchronous services and other switched and non-switched data communications services, such as frame relay, virtual private networks over IP for data communications, broadband services, security/firewall services and VSAT satellite communications services. In addition, PT offers a new range of data, voice and Internet services, such as Intranet, Extranet and managed services, including VoIP. PT uses IP-based solutions to improve interconnections between companies and their employees and between customers and commercial partners through remote access. These solutions enable customers to integrate voice, video and data services in a flexible cost-effective manner with add-on capacity. The offering of web contact center solutions represents an evolution of the classic call center for customers.

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

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

In addition, PT provides outsourced corporate network services for its customers. For example, PT operates and manages the SIBS network, as well as the corporate networks of its strategic partners Caixa Geral de Depósitos, Banco Espírito Santo and CATT.

Networks. PT provides services over the largest IP/MPLS backbone in Portugal, with PT Prime leasing the necessary fixed line capacity from PT Comunicações. PT has points of presence in all major cities throughout Portugal, and PT links its network to its customers' premises through switches and access points that it owns. This broadband data transmission network provides high capacity, flexibility and security and can progressively incorporate current voice and data infrastructures at lower costs than alternative networks. PT also provides high speed Internet access through ADSL and ADS. PT Prime supplies full IP and broadband connectivity for the entire PT Group.

When PT receives revenues from services offered through lines leased by PT Prime from PT Comunicações, PT typically divides the revenues between PT Prime's own direct billings to PT Prime's customers and leased line revenues from the wholesale business of PT Comunicações. Revenues from fixed line voice services for corporate customers are not reflected in PT Prime's revenues, as they are included in retail revenues.

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

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

To support these new services and to respond to the increasing demand of e-business integrators, PT developed Corporate Internet Data Centers in Lisbon and Oporto, and PT is currently upgrading the Lisbon center. These facilities allow PT to provide services, such as colocation, sophisticated web hosting, ISP services, data storage, disaster recovery and ASP services.

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

Marketing and Customer Care. PT focuses significant resources on marketing and customer care. Account managers are given clear incentives to meet and exceed sales targets. PT is upgrading its sophisticated customer relationship management platform to increase focus on market and Internet efficiency.

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

PT offers its corporate customers services available from other companies in the PT Group. PT's subsidiary PT.com, for example, provides significant support for product development and the marketing of Internet and ADSL access.

Other Wireline Services

Other wireline services include primarily PT's directories business and sales of telecommunications equipment.

Directories. Operating revenues from PT's directories business amounted to €108.9 million in 2006 and €120.4 million in 2005. Operating revenues from PT's directories business amounted to €49.4 million in the six months ended 30 June 2007 and €55.8 million in the six months ended 30 June 2006. PT subcontracts to Páginas Amarelas (an associated company 25 per cent. owned by PT) for the publication and distribution of telephone directories throughout Portugal in return for an annual payment of approximately 64 per cent. of its gross revenues from the sale of advertising space. Currently, the provision of yellow page directory services is not subject to significant competition.

Sales of Telecommunications Equipment. Revenues from sales of telecommunications equipment amounted to €32.8 million in 2006 and €34.2 million in 2005, including the sale of handsets, modems and other telecommunications equipment. Revenues from sales of telecommunications equipment amounted to €20.9 million in the six months ended 30 June 2007 and €14.8 million in the six months ended 30 June 2006.

Domestic Mobile Business

PT conducts its mobile business in Portugal through its wholly-owned subsidiary TMN. TMN is the leading provider of mobile voice, data and Internet services in Portugal in terms of the number of active mobile telephone cards connected to its network, as well as by revenues, margins and profits.

Operating revenues from TMN amounted to €1,502.4 million in 2006 compared to €1557.1 million in 2005. Operating revenues from TMN amounted to €728.1 million in the six months ended 30 June 2007 compared to €719.9 million in the six months ended 30 June 2006. Mobile services have undergone significant growth in recent years in Portugal. At 31 December 2006 and 30 June 2007, there were approximately 115.7 and 117.2 active mobile telephone cards per 100 Portuguese inhabitants, respectively (according to ANACOM). This was more than the number of wireline main lines per 100 Portuguese inhabitants, which as of 31 December 2006 was 39 per cent., according to ANACOM. The table below provides statistical information relating to TMN.

	<i>As of December 31,</i>					<i>As of</i>
	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>	<i>30 June 07</i>
TMN – Portugal						
Number of subscribers (thousands)	4,426	4,887	5,053	5,312	5,704	5,814
Subscribers growth per annum (%)	13	10	3	5	7	8.4
Number of subscribers per 100 inhabitants (including competitors' subscribers)	81.9	89.8	95	108.7	115.7	117.2
Estimated market share by number of subscribers (%) ⁽¹⁾	51.9	48.7	48.8	46.4	46.7	46.8
Number of employees	1,192	1,109	1,133	1,184	1,140	n.a.

(1) Source: ANACOM and TMN.

As of 30 June 2007, TMN had 5,814 thousand subscribers, compared to 5,362 as of 30 June 2006. As of 30 June 2007, TMN's subscriber growth per annum was 8.4 per cent.

Services. TMN provides mobile telephone services using the GSM and UMTS technologies. GSM and UMTS are European and worldwide standards using digital technology. Through roaming agreements, TMN's subscribers can use GSM and UMTS services to make and receive mobile calls throughout Europe and in many other countries around the world.

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

In 2000, the Portuguese government opened a tender for UMTS services, and TMN received one of these licences. Licences were also awarded to Vodafone Portugal and Optimus.

In 2004, TMN began providing UMTS services to its customers, with an emphasis on new services, such as video telephony and high-speed data. PT has pursued a strategy of gradual improvements to network coverage, using existing GSM sites where possible in order to minimize the need to install costly new sites. At the end of 2006, TMN's UMTS population coverage was

approximately 80 per cent., and its geographic coverage was about 33 per cent., or 3,633 municipalities out of a total of 4,252 in Portugal, including every municipality with over five thousand inhabitants.

In April 2006, TMN launched HSDPA (High Speed Downlink Packet Access), the first step in the evolution of mobile broadband UMTS services. This technology will evolve in the coming years, positioning mobile operators as competitors in the high speed internet services market. In the first half of 2006, TMN also launched a mobile TV service in partnership with PT Multimédia and a mobile ticketing service in partnership with Lusomundo.

TMN paid spectrum fees in 2005 and 2006 of €27 million and €26 million, respectively, for the use of its 900 MHz and 1800 MHz GSM network and its UMTS network. These spectrum fees are recorded as an operating expense under “indirect taxes” in PT’s financial statements.

Portugal Telecom expects the development of third generation services to require certain additional investments by TMN. TMN made direct investments of €77.1 million in 2005 and €114.2 million in 2006 in building out its third generation network and services. In 2006, the investments made by TMN in connection with UMTS represented more than 61 per cent. of its total capital expenditures in 2006.

During 2005, and 2006 and the first six months of 2007, TMN continued to introduce new products and services in Portugal, such as:

- “+Perto” and “Plano”, two new packages of minutes targeted to postpaid customers;
- “Out Mail”, access to e-mail service on a continuous basis: anywhere and anytime;
- “Krava”, a new service whereby prepaid and postpaid customers are allowed to make calls that will be paid by the receiver;
- “Mix”, a new tariff plan for prepaid and postpaid customers using a single card;
- “Check in”, a service to customers who mainly use international calls;
- “Lost Calls Service”, an automatic service that advises you which numbers tried to call you when your mobile phone is disconnected or is unavailable;
- “Videosharing”, the first commercial video sharing service launched in Portugal, in partnership with Nokia;
- “TMN backup”, a service that provides remote back-up of all personal content on a TMN customer’s handset;
- “Localizz”, a new service of mobile localisation for the corporate segment, which allows on-line visualisation (through an Internet page) of all mobile phones of the company;
- “Giga access”, connectivity to e-mail or internet on a mobile basis;
- “Music edition”, a service that allows customers to share, hear and transfer music;
- “Walkman”, the first service in Portugal that allows customers to download up to 10 music CDs to their handsets;
- “Waiting Ring”, a service that allows customers to change waiting rings;
- “Mobile TV”, offering 26 TV channels, 24 hours a day, including news, music and sports. “Fast zapping” functionality was also introduced in order to improve the user’s experience;
- “E-Ticketing”, a service that allows customers to purchase cinema tickets via their mobile phones;
- “Jogos Multiplayer”, multiplayer games for mobile phones;
- “Serviço Banda Larga TMN”, a mobile phone service supported by the High Speed Downlink Packet Access technology, or 3.5G;
- “Push E-Mail”, which allows customers to receive e-mails in real time; and
- “Casa T”, the first home-zoned service in Portugal, which allows TMN customers to make free calls to the fixed and TMN networks after the first minute, in exchange for a monthly fixed fee.

In the first half of 2007, TMN introduced the following new products and services in Portugal:

“Office Box PME”, a new voice and data offer targeting the SME/SOHO segment, that includes mobile and fixed voice services, broadband, as well as internet and e-mail services;

“Internet no telemóvel”, a new mobile internet service based on a flat rate for unlimited usage of internet and e-mail access through mobile handsets; and

“kitados”, a new set of pricing plans launched to address the youth segment that allow customers to make unlimited on-net calls after the first minute, at night (“kit noite”), at the weekends (“kit fim de semana”) or to a selected number (“kit par”).

Peer-to-peer (“P2P”), messaging services via Short Messaging Services (“SMS”) or Multimedia Messaging Services (“MMS”) continue to account for a significant portion of TMN’s data revenues and are an area where TMN continues to experience significant growth, particularly through MMS, as MMS-enabled handsets are made available to a larger number of customers. In addition, TMN offers a wide range of other services in its data service portfolio, such as a multimedia mobile portal (I9-Inove) and a standard mobile portal (myTMN), multimedia content services (including Logos & Ring Tones or Java games), access to third-party branded content, connectivity to e-mail or the Internet via GPRS/UMTS, corporate solutions and mobile payment services. GPRS is a mobile data service standard for GSM handsets.

TMN’s multimedia portal I9-Inove optimizes the current capabilities of GPRS/UMTS systems to provide customers with faster, easier access and a wider range of services and content, such as Java Games, mobile TV, messaging services, goals from the Portuguese football league in video, TV Cabo’s programming guide and the Lusomundo cinema ticketing service, the first m-commerce service in Portugal. As of December 31, 2006, I9-Inove had reached approximately 1.8 million TMN customers. On the myTMN website (www.mytmn.pt), TMN customers can also access and buy a wide range of content (such as logos, ring tones and alerts), allowing personalisation of their mobile phones.

In keeping with its emphasis on innovation, TMN has a strong focus on offering services that meet customers’ expectations. For example, TMN recently launched a service called “tmn Backup”, which provides remote backup of all personal content on a handset (such as contacts, SMS messages, photos, ring tones, games and other downloads) that would be lost if the handset were stolen or misplaced. In March 2006, TMN launched the “Waiting Rings” service, which allows customers to personalize ring tones when calling a TMN customer. The launch of “Mobile TV” in April 2006 is another example of TMN’s focus on innovation, allowing customers to watch TV on their mobile phones wherever they are.

Another innovative service is the 12400 Video service, launched in 2004, which provides news and entertainment programs from the major Portuguese TV stations to customers through videocall. The 12400 Video is simple, practical and functional and is still the only such service in Portugal. To access the service, TMN’s 3G clients need only make a videocall to the number 12400 and choose the content they wish from a simplified menu.

TMN also offers a variety of Internet access and multimedia services, such as Wi-Fi, GPRS and UMTS Internet access and the ability to receive or send a fax over a mobile handset. The launch of HSDPA in April 2006, which allows speeds of up to 1.9 Mbps, improved mobile Internet access. In October 2006, TMN made available speeds of up to 3.6 Mbps.

TMN offers data services specifically focused on the corporate segment, such as SMS Express and the POS Mobile service. SMS Express allows users to send messages to a mailing list in a quick, automatic and easy form. POS Mobile allows TMN corporate clients to use POS (point of sale) mobile equipment to receive debit or credit payments at any place with total security. TMN also launched Localliz, which is a location-based service that allows mobile management and localisation of a company’s resources (such as handsets, cars, machines and containers) through an Internet website.

TMN offers an m-payment service called Telemultibanco that allows the payment of utility bills by mobile phone.

Data service usage has grown considerably as customers have become increasingly familiar with TMN data services, service offerings have been expanded and access speed has increased through the introduction of UMTS. PT is working to further increase data speeds to improve performance and the attractiveness of the TMN package of products, which PT expects will result in a higher contribution of data services (beyond P2P messaging) to overall revenues in the future.

In June 2005, TMN introduced a low-cost brand “Uzo” that targets low cost subscribers and uses TMN’s GSM network. Uzo offers a very simple service to its customers with no obligatory recharges and one tariff for voice calls and SMSs to all networks of 16 cents per minute and 8 cents per message, respectively. However, if the customer recharges its card with €15 or more, he or she is allowed to speak and to send messages to all networks for 12 cents per minute and 6 cents per message, respectively, for a period of 30 days. Uzo focuses primarily on selling SIM cards and lowcost mobile phones to its customers. Uzo’s products and services are offered through the Internet, Uzo’s call centers (which are separate from TMN’s call centers) and independent news stands and shops located throughout Portugal.

Subscribers and Traffic. TMN is the market leader in mobile services in Portugal. At 31 December 2006, TMN had approximately 5.7 million subscribers, representing an increase of 7.4 per cent. from 31 December 2005. At 31 December 2006, TMN’s subscribers represented 46.7 per cent. of the total mobile subscribers in Portugal. During 2006, TMN’s share of new mobile subscribers (net additions) was 50.2 per cent. according to ANACOM.

At 30 June 2007, TMN had approximately 5,814 million subscribers, representing an increase of 8.4 per cent. from 30 June 2006.

In addition to the increase in the number of subscribers, mobile usage grew during 2006. TMN’s voice traffic in terms of minutes grew by 4.2 per cent. to 7,802 billion minutes in 2006, compared to 7,486 billion minutes in 2005. Average monthly usage per subscriber decreased by 1.1 per cent to 120.3 minutes in 2006, compared to 121.6 minutes in 2005. Average monthly usage per subscriber decreased by 0.6 per cent. to 117.9 minutes in the six months ended 30 June 2007, compared to 118.6 minutes in the six months ended 30 June 2006, primarily due to lower fixed-mobile traffic and aggressive SMS promotions.

In terms of traffic from data transmission services, SMS increased by 148.4 per cent. during 2006, and there were an average of 59.9 SMS messages per month per user in 2006, 135.6 per cent. more than the average of 25.4 SMS messages per month per user in 2005. Traffic from WAP services supported by GPRS and UMTS networks increased by 46.9 per cent. in 2006.

Prices and Revenue Breakdown. PT believes that mobile services in Portugal are priced lower than the European average and are among the lowest in Europe. Mobile telephone charges are not regulated. Traffic charges, sales of handsets and connection and subscription fees represented approximately 90.2 per cent., 8.6 per cent. and 1.2 per cent, respectively, of TMN’s revenues in 2006, and approximately 88.5 per cent., 9.4 per cent. and 2.1 per cent., respectively, of TMN’s revenues in 2005. Monthly subscription fees range from €8.26 (+Perto; Plano) to €40.91 (Extra), excluding VAT.

However, fixed-to-mobile and mobile-to-mobile interconnection charges are regulated by ANACOM and have a significant impact on TMN’s business. In February 2005, ANACOM declared all mobile operators to have significant market power in call termination in mobile networks market. ANACOM has accordingly imposed price controls on interconnection rates for the termination of calls on mobile networks. In 2005, interconnection rates (both fixed-to-mobile and mobile-to-mobile) were reduced by an average of 23.5 per cent. compared with 2004 rates. In 2006, these rates were reduced by an average of 18.5 per cent. compared to the 2005 rates. In the six months ended 30 June 2007, fixed-to-mobile and mobile-to-mobile interconnection rates decreased by 10.2 per cent., compared to the six months ended 30 June 2006. These reductions have had, and are expected to continue to have, a significant impact on TMN’s interconnection revenues and consequently its earnings. Excluding the Euro 12 million negative impact of lower MTR, service revenues would have increased by 2,5% y.o.y. in the first half of 2007.

Products and Marketing. TMN offers a variety of innovative products. It was the first operator in the world to offer pre-paid services, and its prepaid and discount products are popular. PT

estimates that at the end of 2006, approximately 80.6 per cent. of its subscribers were using TMN's prepaid products. In order to improve customer retention and segmentation, TMN redesigned its entire offer of prepaid pricing plans in 2004. TMN has been expanding its subscriber base through increased advertising and the use of its own distribution network. TMN has recently focused on encouraging the use of mobile services by young people through SMS incentive packages. TMN experienced a 17.5 per cent. increase in the number of postpaid subscribers in 2006 as a result of a promotional campaign aimed at stimulating a switch from prepaid to postpaid services and also as a result of continued marketing efforts directed at corporations and in the middle and high-end segment of the market.

TMN markets its services through more than 2,000 points of sale, including TMN's sales force, Portugal Telecom retail shops, TMN shops, supermarket chains and independent dealers.

Network and Capital Investment. In recent years, TMN has made significant investments in its second and third generation networks. As a result of its investments, TMN has a technologically advanced high capacity network that provides extensive coverage across Portugal. As of the end of 2006, TMN's digital network had 4,181 GSM base stations, including 79 base stations added during 2006, and 2,227 UMTS B nodes, including 333 B nodes added during 2006. As of 31st December, 2006, these GSM base stations covered more than 98 per cent. of continental Portugal and 99 per cent. of the Portuguese population, and the UMTS B nodes covered approximately 33 per cent. of continental Portugal and 80 per cent. of the Portuguese population.

Since November 2005, TMN has been one of 18 operators in the world that are members of the Global Certification Forum, an industry group aimed at ensuring compatibility of mobile telecommunications systems.

Roaming. Roaming agreements between operators allow their subscribers to make and receive voice calls automatically, send and receive data, or access other services when traveling outside the geographical coverage area of the home network, by using a visited network. As of the end of 2006, TMN had entered into GSM roaming agreements with a total of 340 operators (in 192 countries or regions), 145 GPRS roaming agreements (in 101 countries or regions) and 62 3G roaming agreements (in 36 countries or regions).

Equipment Sales. TMN sells mobile phones and related equipment in Portugal. Equipment sales contributed €129.7 million and €146.3 million to TMN's operating revenues in 2006 and 2005, respectively. Equipment sales contributed €57.1 million and €53.9 million in the six months ended 30 June 2007 and 2006, respectively.

Brazilian Mobile Business

PT provides mobile telecommunications services in Brazil through Vivo Participações S.A. ("Vivo"), the leading mobile company in Brazil with a total of 30,241 million active mobile telephones at 30 June 2007. PT holds 50 per cent. of Vivo, which is a joint venture with Telefónica. The joint venture operates in 19 states in Brazil and in the Federal district of Brasília, which provide more than 83.1 per cent. of Brazil's GDP. In its areas of operation, Vivo had an estimated market share of approximately 37.3 per cent. at the end of June 2007. PT believes that the joint venture facilitates its ability to serve its Brazilian subscribers on a seamless basis throughout Brazil.

History and Organisational Structure. Until 2002, PT's mobile operations in Brazil, a country with a population of about 177 million people, had been active only in the states of São Paulo, Paraná and Santa Catarina. In January, 2001, PT entered into a strategic agreement with Telefónica Móviles (the former mobile subsidiary of Telefónica, which has since merged with and into Telefónica), to combine all of their mobile assets in Brazil to the extent permitted under Brazilian law. The strategic agreement was approved by the European Commission in March, 2001. In December 2002, ANATEL, the Brazilian telecommunications regulator, formally approved the transfer of all of Portugal Telecom's and Telefónica's direct and indirect interests in Brazilian mobile services companies to the mobile joint venture company.

On 27 December 2002, Portugal Telecom, through its subsidiary PT Móveis, and Telefónica, through its then subsidiary Telefónica Móviles, transferred all of their direct and indirect interests in

Brazilian mobile services companies to the joint venture company, named Brasilcel N.V. Portugal Telecom and Telefónica transferred to this company all of their interests in:

- Telesp Celular Participações S.A. (“TCP”), which controlled Telesp Celular (the band A operator in the state of São Paulo) and Global Telecom (the band B operator in the states of Paraná and Santa Catarina) and was contributed by Portugal Telecom (which had a controlling position) and by Telefónica Móviles;
- Tele Sudeste Celular Participações S.A. (“Tele Sudeste”), which controlled Telerj Celular, S.A. (the band A operator in the state of Rio de Janeiro), or Telerj, and Telest Celular, S.A. (the band A operator in the state of Espírito Santo), or Telest, and was contributed by Telefónica Móviles;
- Tele Leste Celular Participações S.A. (“Tele Leste”), which controlled Telebahia Celular, S.A. (“Telebahia”) (the band A operator in the state of Bahia) and Telergipe Celular, S.A. (the band A operator in the state of Sergipe) and was contributed by Telefónica Móviles; and
- Celular CRT Participações S.A., (“Celular CRT Participações”), which controlled Celular CRT, S.A., (“Celular CRT”) (the band A operator in the state of Rio Grande do Sul), and was contributed by Telefónica Móviles (which had a controlling position) and by Portugal Telecom.

The arrangements by which Portugal Telecom and Telefónica own and manage the joint venture and related issues are described below in “Strategic Alliances – Alliance with Telefónica”. Certain regulatory restrictions applicable to Vivo and its subsidiaries which result from their relationship with Telefónica, including the inability of Vivo and its subsidiaries to provide wireline long distance services in Brazil, are described below in “Regulation-Brazil – SMP Regulation”.

Before the transfer of these assets to the joint venture, TCP had acquired an 81.61 per cent. indirect economic interest in Global Telecom in 2001 through the acquisition of 49 per cent. of the voting shares and 100 per cent. of the non-voting shares of each of three holding companies that controlled Global Telecom. The total purchase price was R\$902.6 million. On 27 December 2002, the same day as the transfer of the assets to the joint venture, TCP acquired the remaining 51 per cent. of the voting shares of the three holding companies that owned Global Telecom for US\$82.0 million. TCP then owned 100 per cent. of the voting and non-voting shares of Global Telecom.

Although PT transferred all of its interests in mobile telecommunications companies in Brazil to Vivo on 27 December 2002, its consolidated statements of income and cash flows for the year ended 31 December 2002 continued to fully consolidate TCP’s results. However, its balance sheet as of 31 December 2002 proportionally consolidates all the assets and liabilities of Vivo. PT’s consolidated statements of income and cash flow for the years ended 31 December 2005 and 2006 and for the six months ended 30 June 2006 and 2007, and its balance sheets as of 31 December 2005 and 2006 and as of 30 June 2007 proportionally consolidate the results of Vivo.

On 25 April 2003, TCP acquired 61.1 per cent. of the voting capital stock of TCO (a band A operator in the midwestern and northern regions of Brazil) from Fixcel, a Brazilian company, for R\$1,529 million. As a result, TCO’s assets and liabilities as of 31 December 2005 and 2006 and as of 30 June 2007 are reflected in Portugal Telecom’s consolidated balance sheets as of these dates through its proportional consolidation of Vivo, and TCO’s income and cash flows for the years ended 31 December 2005 and 2006 are reflected in Portugal Telecom’s consolidated statements of income and cash flows for the year ended 31 December 2005 and 2006 through Portugal Telecom’s proportional consolidation of Vivo’s statements of income and cash flows.

On 18 November 2003, TCP acquired an additional 25.5 per cent. of the common shares of TCO in a tender offer to TCO minority shareholders for R\$538.8 million. Following the tender offer, TCP held 86.6 per cent. of the voting capital stock and 28.9 per cent. of the total capital stock of TCO, including treasury shares held by TCO.

In October 2004, TCP successfully completed a tender offer for additional shares of TCO, thereby increasing its economic interest in TCO to 50.6 per cent., for total consideration of

approximately R\$902 million. Concurrently with this transaction, Avista, a holding company owned by Vivo, was created for the purpose of acquiring additional interests in Vivo's operating companies. On 8 October 2004, Avista completed a tender offer for additional shares of Tele Sudeste, Tele Leste and Celular CRT Participações. As a result of the successful completion of the tender offer, Vivo increased its interest in Tele Sudeste to 91.0 per cent., in Tele Leste to 50.7 per cent. and in Celular CRT Participações to 67.4 per cent., for a total of approximately R\$607 million.

On 22 February 2006, the requisite percentages of the voting shareholders of the Vivo companies approved a corporate reorganisation. The corporate reorganisation consisted of a merger of shares under Brazilian law (incorporação de ações) of TCO with TCP and the merger of companies under Brazilian law (incorporação de empresas) of Tele Leste, Tele Sudeste and Celular CRT Participações with TCP.

In connection with these mergers, TCP was renamed "Vivo Participações S.A." On 31 March 2006, common shares and preferred shares of Vivo began trading on the São Paulo Stock Exchange under the ticker symbols "VIVO3" and "VIVO4", respectively, and ADSs of Vivo began trading on the New York Stock Exchange under the ticker symbol "VIV".

Vivo undertook the merger in order to align the interests of shareholders of the Vivo companies, to increase the liquidity of the securities held by those shareholders, to simplify the shareholding and organisational structure of the Vivo business and expand its shareholder base, and to take advantage of important synergies among the companies.

In October 2006, Vivo completed a further restructuring with the merger into Global Telecom (the company that provided mobile services in the states of Paraná and Santa Catarina and that was fully owned by TCP) of all other companies of Vivo that provided mobile services in the other states mentioned above. In connection with this transaction, Global Telecom was renamed "Vivo S.A.".

On 2 August 2007 Vivo signed a stock purchase agreement with Telpart Participações S.A. (**Telpart**) to acquire control of Telemig Celular Participações S.A. (**Telemig Participações**) and Tele Norte Celular Participações S.A. (**Tele Norte Participações**) comprised of 22.72 per cent. and 19.34 per cent. of total capital, respectively, for an aggregate amount of Real 1.2 billion, subject to certain price adjustments. In addition, Vivo will acquire from Telpart certain subscription rights for Real 87 million. The conclusion of the transaction is subject to the approval of ANATEL and ratification by the general shareholders meetings of Vivo and Telpart, among other customary closing conditions.

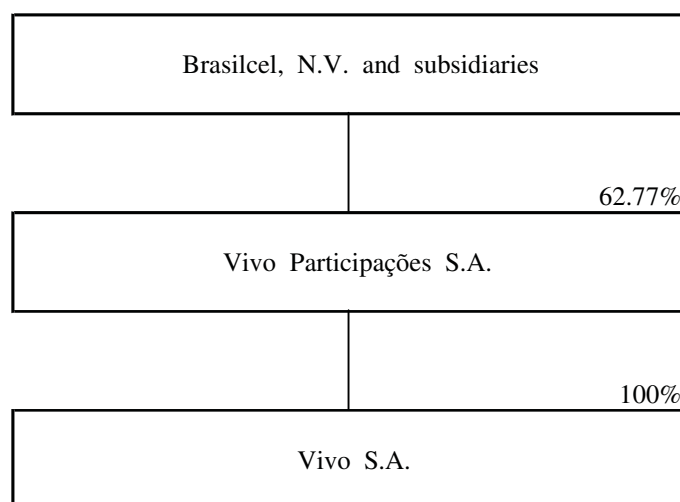
Upon closing of the transaction, in accordance with Brazilian law, Vivo will launch mandatory tender offers for the acquisition of common shares held by non-controlling shareholders at 80 per cent. of the price paid for the controlling stake. The mandatory tender offers will be extended to Telemig Participações, Telemig Celular, Tele Norte Participações and Amazônia Celular.

Additionally, Vivo intends to launch voluntary tender offers for up to 1/3 of all classes of preferred shares held by the non-controlling shareholders in the holding and operating companies, at a 25 per cent. premium to the weighted average price of the last 30 trading days up to 1 August 2007.

Assuming full acceptance of all offers, Vivo will have acquired a beneficial interest of 58.2 per cent. in Telemig Celular and 54.6 per cent. in Amazônia Celular, for an aggregate consideration of circa Real 2.9 billion (including the value of the subscription rights).

Telemig Celular and Amazônia Celular operate in the regions of Minas Gerais and Amazonia, respectively, so this will allow Vivo to increase its coverage and customer base.

The diagram below presents the ownership structure of Vivo as of 30 June 2007:



As of 30 June 2007, Brasilcel held 88.85 per cent. of the common shares of Vivo Participações, 47.76 per cent. of its preferred shares and 62.77 per cent of its total share capital.

Regions. Vivo provides mobile telecommunications services on the A and B Band frequency in 19 Brazilian states in addition to the federal district, representing a total of approximately 7.3 million square kilometres, or 85.6 per cent. of the Brazilian territory. This area includes more than 138.8 million people, representing 73.8 per cent. of Brazil's population, and 212 municipalities with a population in excess of 100,000.

The following table sets forth population, gross domestic product (GDP), and per capita income statistics for each state in Vivo's service regions at the dates and for the years indicated:

Area	Frequency Range	At December 31 2006		Last Available IBGE Data		
		Population (in thousands) ⁽¹⁾	Percent of Brazil's population ⁽¹⁾	GDP (in millions of reais) ⁽²⁾⁽³⁾	Percent of Brazil's GDP ⁽³⁾	Per capita income (in reais) ⁽²⁾⁽³⁾
São Paulo state	A Band	41,361	22.0%	546,607	30.9%	13,725
Paraná state	B Band	10,450	5.6%	108,699	6.2%	10,725
Santa Catarina state	B Band	6,004	3.2%	70,208	4.0%	12,159
Goiás state	A Band	5,786	3.1%	41,316	2.3%	7,501
Tocantins state	A Band	1,346	0.7%	4,768	0.3%	3,776
Mato Grosso state	A Band	2,884	1.5%	27,935	1.6%	10,162
Mato Grosso do Sul state ...	A Band	2,315	1.2%	19,954	1.1%	8,945
Rondônia state	A Band	1,576	0.8%	9,744	0.6%	6,238
Acre state	A Band	690	0.4%	3,242	0.2%	5,143
Amapá state	B Band	626	0.3%	3,720	0.2%	6,796
Amazonas state	B Band	3,355	1.8%	35,889	2.0%	11,434
Maranhão state	B Band	6,225	3.3%	16,547	0.9%	2,748
Pará state	B Band	7,180	3.8%	34,196	1.9%	4,992
Roraima state	B Band	409	0.2%	1,864	0.1%	4,881
Federal district	A Band	2,409	1.3%	43,522	2.5%	19,071
Bahia state	A Band	14,017	7.5%	86,882	4.9%	6,350
Sergipe state	A Band	2,017	1.1%	13,121	0.7%	6,782

Area	At December 31 2006			Last Available IBGE Data		
	Frequency Range	Population (in thousands) ⁽¹⁾	Percent of Brazil's population ⁽¹⁾	GDP (in millions of reais) ⁽²⁾⁽³⁾	Percent of Brazil's GDP ⁽³⁾	Per capita income (in reais) ⁽²⁾⁽³⁾
Rio de Janeiro state.....	A Band	15,650	8.3%	222,564	12.6%	14,639
Espirito Santo state.....	A Band	3,492	1.9%	34,488	2.0%	10,289
Rio Grande do Sul state.....	A Band	11,022	5.9%	142,874	8.1%	13,320
Vivo's service regions.....		138,814	73.8%	1,468,140	83.1%	10,210

Source: Instituto Brasileiro de Geografia e Estatística (IBGE)

(1) Estimates from IBGE for the year end 2006.

(2) According to the most recent IBGR data (2004).

(3) Nominal Brazilian GDP was R\$1,766,621 million as of December 2004, calculated by IBGE.

Operating and Other Data. The table below sets forth certain operating and other data for Vivo for 2004, 2005 and 2006.

	2004	2005	2006
Vivo-Operating Data			
Cellular lines in service at year-end (in thousands).....	26,543	29,805	29,053
Customer growth during year.....	5,887	3,262	(752)
Prepaid lines in service at year-end (in thousands).....	21,357	24,061	23,543
Minutes of use (MOU) ⁽¹⁾	89	78	74
Average revenues per user (in Reais) ⁽²⁾	32.8	28.7	27.2
Churn ⁽³⁾	22.4%	21.8%	34.8%
Penetration at year-end ⁽⁴⁾	37.0%	46.6%	55%
Estimated market share ⁽⁵⁾	50.9%	44.4%	38.2%
Estimated market share of net additions ⁽⁵⁾	38.1%	21.8%	(8.5)%
Vivo-Financial Data⁽⁶⁾			
Net operating revenues (in millions of Reais) ⁽⁶⁾	11,628.1	12,387.0	11,498.0
Net income (loss) (in millions of Reais) ⁽⁶⁾	(61.5)	(814.7)	(144.5)

(1) Monthly average, in minutes, of traffic per customer.

(2) Net revenues from services per month divided by the monthly average of customers.

(3) Churn is the number of customers that leave Vivo during the year, calculated as a percentage of the sum of the monthly average of customers.

(4) Number of cellular lines in service in the region, including competitors, divided by the population of the region.

(5) Source: ANATEL.

(6) Reflects 100 per cent. Vivo's results in accordance with IFRS.

The table below sets forth certain operating data for Vivo for the six months ended 30 June 2006 and 2007.

	Six Months Ended 30 June	
	2006	2007
Vivo – Operating Data		
Cellular lines in service at period-end (in thousands).....	28,525	30,240
Customer growth during year.....	(1,280)	1,187
Minutes of use (MOU) ⁽¹⁾	67	77
Average revenues per user (in Reais) ⁽²⁾	24.1	29.9
Estimated market share ⁽³⁾	40.4	37.3

(1) Monthly average, in minutes, of traffic per customer.

(2) Net revenues from services per month divided by the monthly average of customers.

(3) Source: ANATEL.

Services. Vivo provides cellular telecommunications services using GSM/EDGE, CDMA and TDMA technologies. Its network provides both CDMA digital service and AMPS, an analog service that has been substantially phased out. All services are provided on the 850 MHz frequency.

Vivo provides voice and ancillary services, including voicemail and voicemail notification, call forwarding, three-way calling, caller identification, short messaging, limitation on the number of used minutes, cellular chat room, and data services, such as wireless application protocol (“WAP”) service through which clients can access WAP sites and portals. Vivo offers direct access to the Internet through either PCMCIA cards (Personal Computer Memory Card International Association, an organization consisting of some 500 companies that has developed small, standardized credit card-sized devices called PC Cards) designed to connect compatible PDAs (Personal Digital Assistant, a handheld device that combines computing, telephone/fax, Internet and networking features) and laptops or cellular phones through a cable connection that offers corporate subscribers secure access to their intranet and office resources. Vivo also offers some new services like Multimedia Message Service and MExE (Mobile Execution Environment), which enables the mobile handset to download applications and execute them along with a user interface for easier access to Vivo’s services.

In 2006, Vivo launched:

- “Vivo Localiza Familia” – a location based service that allows children to be located and monitored by their parents via cellular phones or the Internet;
- “Vivo Localiza Amigos” – a location based service that enables customers to locate their friends, as well as to be located by their friends, using an address and a map of the applicable region;
- “Vivo Co-Piloto” – a location based service that assists the user in moving from one point to another in several Brazilian cities;
- “Vivo Bolão” – an interactive game that tests the user’s knowledge of soccer;
- “Instant Messenger” – the most popular Internet instant messenger application (MSN), which is now made available for Vivo handsets through SMS;
- “Vivo ao Vivo” – new interface for Vivo GSM terminals;
- “Vivo e Você na Copa” – exclusive CBF (Brazilian Soccer Confederation) content, including games, tones, wallpaper, videos and a voice portal, during the World Cup;
- “Vivo Chip” – a service menu on GSM SIM Cards;
- “Vivo Flash” – a fixed wireless connection to the Internet; and
- “Vivo Torpedo E-Mail Corporate” – a service that transforms the cellular phone number into an email address and enables users to receive every email sent to them as an SMS message.

Vivo has also improved its current product offerings, as follows:

- “TV no Celular” (video streaming) – now includes RTP (Radio e Televisão de Portugal) programming;
- “Vivo Play 3G” – now includes music content from Warner Music and Universal Music; and
- “Vivo Portal de Voz” – an auction service in partnership with SBT (Sistema Brasileiro de Televisão).

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

Subscribers and Traffic. At the end of 2006, there were approximately 99,918 million wireless subscribers in Brazil, and there was an estimated total market penetration rate of approximately 53 per cent. in Brazil as a whole, according to information published by ANATEL. In 2006, the Brazilian market experienced a 16 per cent. increase in the number of wireless subscribers and a 13 per cent. increase in those areas where Vivo operates. The greatest increase in subscribers was in the

Brazilian states of São Paulo, Rio de Janeiro, Rio Grande do Sul and the Centro Oeste region. As of 31 December 2006, Vivo had approximately 29.1 million wireless subscribers, with an estimated market share of 38.2 per cent. in its areas of operation and 29.1 per cent. in Brazil.

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

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

As of 31st December, 2006, Vivo had 307 sales outlets (94 in São Paulo, 50 in the states of Rio de Janeiro and Espírito Santo, 33 in the state of Rio Grande do Sul, 37 in the states of Paraná and Santa Catarina, 24 in the states of Bahia and Sergipe, and 69 in the states that make up the midwestern and northern regions of Brazil). Vivo also has a network of 7,837 authorized retail and resales dealerships with a total of 8,144 points of sale.

Prepaid telephone card recharging was available at 322,863 locations, including Vivo's own stores, dealers, lottery shops, physical and online card distributors, and at smaller shops, drugstores, newspaper stands, book stores, bakeries, gas stations, bars and restaurants. Online recharging is also provided by several banks' websites.

Customer Service. Vivo continued to outsource customer service, while maintaining management oversight. Customer service is available 24 hours from Vivo's call center and website.

Vivo's customer satisfaction is evaluated by regular satisfaction surveys. In the second half of 2006, 3,200 customers of Vivo and 2,200 customers of other non-affiliated companies were interviewed throughout Brazil about customer assistance, products and services. Vivo was ranked 8.21 on a scale from 1 to 10 for customer satisfaction, with the market average being 8.27. One of Vivo's most important objectives in 2006 was to retain its customers by increasing customer satisfaction. Towards this objective, Vivo took several actions. For example, one of the most frequent complaints from Vivo's customers was related to billing. Therefore, Vivo re-worked the billing process from the call center to the back office in order to speed up customer response time, to assure the quality of customer service and to increase the likelihood of first-call resolution. In addition, Vivo designed a new administrative structure to better track its premium customers and to suggest ways to improve retention.

Network. In 2006, Vivo began to implement a GSM network. Digitalization offers certain advantages, such as greater network capacity and additional revenue through the sale of value added services. By 31 December 2006, Vivo's telecommunications network in the state of São Paulo, which provides both CDMA digital and GSM digital services, covered 100 per cent. of the municipalities. Vivo's network is connected primarily through a fiber optic and radio transmission system, parts of which are owned and parts of which are leased, mainly from Telecomunicações de São Paulo S.A., or Telesp. The network consists of cellular switches, base stations and other network elements such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point, PDSN and gateways. NEC do Brasil S.A., Nortel Networks-Northern Telecom do Brasil, Motorola do Brasil Ltda., Lucent Technologies do Brasil, Ind. e Com. Ltda., Huawei do Brasil Telecomunicações Ltda. and Ericsson Telecomunicações S.A. are Vivo S.A.'s main suppliers in the state of São Paulo.

As of 31 December 2006, the telecommunications network in Parana and Santa Catarina, which provides both CDMA digital and GSM digital services, covered 59.8 per cent. of the municipalities, or 92.6 per cent. of the population, in its region. The Parana Santa Catarina network is primarily

connected by a fiber optic and radio transmission system, parts of which are owned and parts of which are leased, mainly from fixed operating companies (Brasil Telecom and Embratel) and Copel – Companhia Paranaense de Energia S.A. The network consists of cellular switches, base stations and other network elements, such as voicemail, prepaid service, Home Location Registers, Signaling Transfer Points and gateways. Motorola do Brasil Ltda., Huawei do Brasil Telecomunicações Ltda., Alcatel Telecomunicações S/A and Ericsson Telecomunicações S.A. are Vivo's main suppliers in the Paraná Santa Catarina network.

As of 31 December 2006, Vivo provided CDMA Digital, GSM digital, TDMA digital and AMPS analog services in the midwestern and northern regions, covering 45.8 per cent. of the municipalities, or 80.9 per cent. of the population in its region. Vivo's network is connected primarily through a fiber optic and radio transmission system, parts of which are owned and parts of which are leased, from incumbent wireline companies. The network consists of cellular switches, base-stations and other network elements such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point and gateways. Nortel Networks – Northern Telecom do Brasil, Motorola do Brasil Ltda. (presently Motorola Industrial Ltda. and Motorola Services Ltda.), Huawei do Brasil Telecomunicações Ltda. and Ericsson Telecomunicações are Vivo's main suppliers in the midwestern and northern region.

As of 31 December 2006, the telecommunications network of Vivo in Bahia and Sergipe covered 44.7 per cent. of the municipalities, or 77.6 per cent. of the population, in its region. Its network provides both CDMA digital, GSM digital and AMPS analog services. The network is connected primarily through a fiber optic and radio transmission system, parts of which are owned and parts of which are leased, mainly from Tele Norte Leste Participações S.A., or Telemar. The network includes cellular switches, base stations and other communication devices such as voicemail, prepaid service, Short Message Service and Home Location Registers. NEC do Brasil S.A., Ericsson Telecomunicações S.A., Nortel Networks-Northern Telecom do Brasil, Motorola Industrial Ltda., Motorola Services Ltda. and Lucent Technologies do Brasil, Ind. e Com. Ltda. are Vivo's main suppliers in the Bahia and Sergipe regions.

As of 31 December 2006, the telecommunications network of Vivo in the states of Rio de Janeiro and Espírito Santo covered 100 per cent. of the municipalities in its area. Its network provides both CDMA digital, GSM digital and AMPS analog services. This network is connected primarily through a fiber optic and radio transmission system, parts of which are owned and parts of which are leased, mainly from the incumbent wireline companies, and consists of cellular switches, base stations and other communication devices such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point, PDSN and gateways. NEC do Brasil S.A., Nortel Networks – Northern Telecom do Brasil, Ericsson Telecomunicações S.A., Huawei do Brasil Telecomunicações Ltda. and Lucent Technologies do Brasil, Ind. e Com. Ltda. are Vivo's main suppliers in Rio de Janeiro and Espírito Santo.

As of 31 December 2006, Vivo's network in the state of Rio Grande do Sul provides CDMA, GSM digital and TDMA digital and AMPS analog services, covering 70.1 per cent. of the municipalities, or 96.0 per cent. of the population, of this region. The Rio Grande do Sul network is connected primarily through a fiber optic and radio transmission system, parts of which are owned and parts of which are leased, mainly from Brasil Telecom. The network consists of cellular switches, base stations and other communication devices such as voicemail, prepaid service, Short Message Service, Home Location Registers and gateways. Nortel Networks – Northern Telecom do Brasil, Huawei do Brasil Telecomunicações Ltda., and Ericsson Telecomunicações S.A. are Vivo's main suppliers in Rio Grande do Sul.

Vivo's advanced network management technology increasingly ensures global management and supervision of all its network processes and network performance. The network management centers are located in São Paulo and Brasília. The network management center in São Paulo monitors the critical network operational parameters of São Paulo, Paraná, Santa Catarina and Rio Grande do Sul. The network management center in Brasília monitors the critical network operational parameters in the midwestern and northern regions, Rio de Janeiro, Espírito Santo, Bahia and Sergipe. These centers are able to identify abnormalities in both our network and in third parties' networks, using failure and signaling monitoring systems. In addition, quality and service standards are constantly

monitored. The network management centers are integrated with maintenance and operations teams that maintain and operate cellular and radio network elements, computing bases, service platforms and communications backbones.

Vivo's network is prepared to provide continuity of service for its customers in the event of network interruptions. Vivo has developed contingency plans for potential catastrophes in its switching centers, power supply interruptions and security breaches.

Vivo is required to meet certain requirements for service quality and annual network expansion. See “– Regulation of the Brazilian Telecommunications Industry – Obligations of Telecommunications Companies.” Vivo achieved all of its required network expansion obligations for 2006.

Capital Expenditures. The following table sets forth Vivo's total capital expenditures for the periods indicated:

Vivo	<i>Year ended 31 December</i>		
	<i>2004⁽¹⁾</i>	<i>2005⁽¹⁾</i>	<i>2006⁽¹⁾</i>
	<i>(in millions of reais)</i>		
Switching equipment.....	582.1	523.0	375.9
Transmission equipment.....	623.8	862.8	844.4
Information technology.....	291.9	407.6	414.8
Other ⁽²⁾	422.7	401.7	477.9
Total capital expenditures	1,920.5	2,195.1	2,113.0

(1) This financial information represents 100 per cent. of Vivo's capital expenditures, in accordance with IFRS.

(2) Consisting primarily of free handset rentals, network construction, furniture and fixtures, office equipment and store layouts.

Vivo's capital expenditures over the past three years have related primarily to increasing Vivo's network capacity and coverage. Vivo continued its projects for the improvement and expansion of the capacity of services rendered, which provided support to increase the CDMA 1XRTT and EVDO network, expansion of transmission routes, system centralization and integration (billing, collection and CRM, among others), development of new services and opening and renovating points of sale and terminals for the corporate segment.

In the aggregate, R\$2,113.0 million was invested during the year ended 31 December 2006, which included investments in the GSM/EDGE network and in the current CDMA/EV-DO network. This amount represented 18.4 per cent. of Vivo's net operating revenues.

Vivo's capital expenditures for 2007, estimated at R\$1.7 billion, are expected to include investments in network expansion (the GSM/EDGE overlay), introduction of new products and services to maximize the use of cellular phones, expansion of stores and improvement in the quality of services provided to customers. Vivo intends to pay these expenses with funds generated by operations and its available borrowing capacity. In the first semester 2007, Vivo has invested R\$572.7 million.

Interconnection Charges. Vivo earns revenue from any call that originates from another cellular or fixed-line service provider's network connecting one of Vivo's customers. Vivo charges the service provider from whose network the call originates a network usage charge for every minute that Vivo's network is used in connection with the call. See “– Business Overview – Operating Agreements – Interconnection Agreements”. Tariff increases are subject to ANATEL review and approval.

In 2003, ANATEL adopted “Bill & Keep” rules for interconnection charges for traffic between the networks of SMP operators. Under these rules, an SMP mobile operator pays for the use of another SMP mobile operator's network in the same authorization area only if the traffic carried from the first operator to the second exceeds 55 per cent. of the total traffic exchanged between them (known as a partial “Bill & Keep” regime). In that case, only those calls that have surpassed the 55 per cent. level will be subject to payment for network usage. In 2005, this regulatory regime contributed to a decrease in Vivo's revenues from interconnection fees charged to other companies. In

July 2006, the Bill & Keep regime was discontinued. The current rule is “full billing,” pursuant to which the SMP operator pays the entire call termination fee of the other mobile network. The partial “Bill and Keep” rule is still used between the SMP and SME (trunking) networks.

Roaming Fees. Vivo has agreements with major fixed-line providers for automatic roaming with all mobile service providers in Brazil and with some wireless service operators abroad. These contracts allow its subscribers to access the network of other mobile service providers when traveling outside its coverage area without having to change their handsets or mobile numbers. Vivo provides reciprocal services to subscribers of other mobile service providers when they are within its coverage area. The agreements require the contracting parties to provide service to roaming subscribers on the same basis as they provide service to their own subscribers. See “– *Operating Agreements – Roaming Agreements*”.

License. Under the SMP regime, Vivo converted its former concessions to SMP licenses. These SMP licenses have substantially the same terms and conditions as the other SMP licenses issued under the SMP regime, although some of the terms of Vivo’s former concessions, such as limits on prices charged to subscribers under its postpaid service plan (the Basic Plan), continue to apply despite conversion to SMP licenses. See “– *Regulation – Brazil – SMP Regulation*”.

By converting its concessions to SMP licenses, Vivo was required to introduce carrier selection on its network to give its subscribers the choice to use another carrier for long distance and international calls. The introduction of carrier selection increased the competitive pressures on Vivo’s business. In addition, because the SMP regime permits commercial negotiation of the interconnection rates it charges to wireline operators, Vivo may be forced to reduce these rates in the future. Vivo’s SMP licenses expire on the same dates as the concessions will expire. Vivo has the same right to apply for renewal as other SMP license holders that migrate to the SMP regime from their existing concessions.

Equipment Sales. Vivo sells CDMA dual-mode (800MHz CDMA-1xRTT/AMPS and 800MHz CDMA/AMPS), GSM and tri-mode (800/1900 CDMA and 800MHz AMPs), and dual technology (CDMA and GSM) cellular handsets and data devices in CDMA EVDO technology (PCMCIA, USB and deskmodem) through its stores and dealers. Vivo has overlaid its TDMA network with a CDMA network and has stopped selling TDMA handsets. Although Vivo still has some customers using analog service (approximately 0.1 per cent. of its total customer base as of 31 December 2006), Vivo has implemented a series of actions, such as providing discounts on digital handsets, discounts on monthly fees for digital services, digital handset rentals and free digital handsets, to encourage analog and TDMA customers to transfer to CDMA service. Vivo’s current suppliers for handsets are Motorola, LG, Samsung, Nokia, Pantech, SonyEricsson, BenQ-Siemens, Aiko and Kyocera.

Management. In accordance with the shareholders’ agreement between Portugal Telecom and Telefónica, Portugal Telecom is responsible for the appointment of Vivo’s chief executive officer and Telefónica is responsible for the appointment of Vivo’s chief financial officer. Following the mergers in February 2006, Vivo Participações S.A. (formerly TCP) continues to be managed by a Board of Directors and a Board of Executive Officers. Vivo’s shareholders elect the members of the Board of Directors. The Board of Directors must have between three and twelve members, each serving a three-year term. The Board of Vivo Participações S.A. continues to consist of nine members, and the terms of the current members of the Board will expire in April 2009. The Board of Directors holds regular quarterly meetings, and the chairman or two board members may call special meetings.

Operating Agreements. Vivo has agreements with major fixed-line and mobile operators in Brazil in order to lease physical space, real estate, air conditioning, energy, security and cleaning services. Vivo also leases transmission capacity necessary to complete the construction of its network infrastructure.

Interconnection Agreements. The terms of Vivo’s interconnection agreements include provisions with respect to the number of connection points and traffic signals. See “– *Regulation of the Brazilian Telecommunications Industry – Obligations of Telecommunications Companies*” and “– *Regulation of the Brazilian Telecommunications Industry – Interconnection*”.

Roaming Agreements. Vivo is a member of the Brazilian Roaming Association, a group composed of all companies providing cellular services in Brazil. This association was created to

standardize roaming services in Brazil and elsewhere. The roaming agreements require Vivo and the other cellular service providers to provide service to roaming customers on the same basis that each member provides to its own customers, and to carry out a monthly reconciliation of roaming customer usage charges. Vivo offers CDMA automatic international roaming in the United States, Argentina, Uruguay, Chile, Canada, China, Mexico, Venezuela, Puerto Rico, New Zealand, the Dominican Republic and South Korea. Vivo also provides international GSM services through third party partners using GSM handsets in most parts of Europe, Africa, the Americas, Asia and Oceania.

Multimedia Businesses

PT provides multimedia services in Portugal through its subsidiary PT Multimédia and through PT Multimédia's subsidiaries. Operating revenues from PT's Multimedia's businesses were €666.5 million in 2006 and €628.5 million in 2005. Operating revenues from PT's Multimedia businesses were €350.7 million in the six months ended 30th June, 2007 and €324.7 million in the six months ended 30th June, 2006.

Proposed Spin-Off. On 3 August 2006, PT announced its intent to spin off its 58.43 per cent. interest in PT Multimédia through a distribution to shareholders, subject to shareholder approval. On 21 March 2007, the Board of Directors proposed to the shareholders a dividend in kind of 4 PT Multimédia shares for each PT 25 shares owned, rounded down. This spin-off proposal was approved by the shareholders at the Annual General Meeting held on 27 April 2007.

PT's management has concluded that the separation of PT Multimédia from PT should positively contribute to the development of the telecommunications market in Portugal, allowing the market to develop increasingly innovative and convergent services to consumers. The resulting market structure should provide regulatory relief for PT's wireline business, giving it flexibility to offer more and better services to its customers, while PT Multimédia would be able to pursue its own competitive strategy, domestically and abroad. By allowing the management of each company to focus on its core competencies, PT believes that this strategy is more likely to create greater value for shareholders over time. The proposed separation also addresses the long-standing objectives of the Portuguese regulators.

Notwithstanding these potential benefits to PT Multimédia, the spin-off of PT Multimédia could have a negative impact on PT's wireline and mobile business performance.

Incorporation and Development. PT Multimédia was formed in July 1999 and PT transferred to it certain of its cable and satellite pay-TV activities, as well as Internet-related activities focused on residential customers and the small office home office and small and medium-sized enterprise markets, including:

- PT's cable television pay TV operations through cable and DTH satellite;
- cable and direct-to-home satellite programming activities;
- advertising sales;
- the provision of Internet access; and
- PT's minority stake in the leading Portuguese telephone directories business.

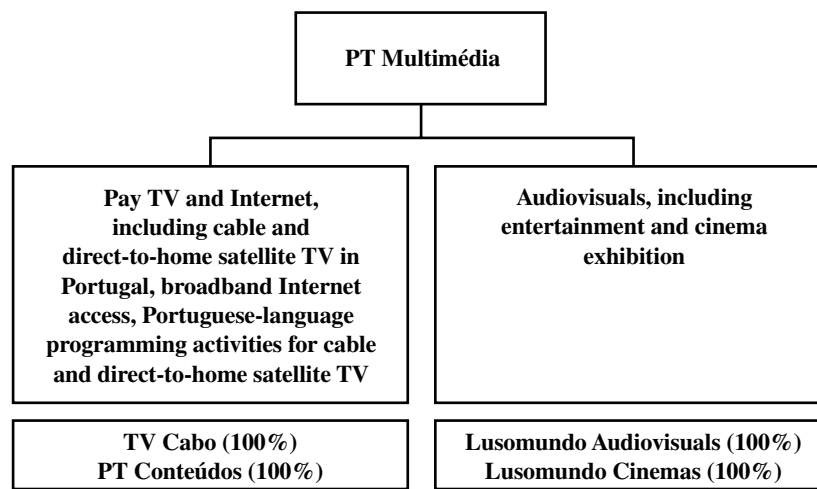
After an initial public offering of ordinary shares of PT Multimédia in November 1999 and various other transactions, PT now holds 58.43 per cent. of the ordinary shares of PT Multimédia.

On 28 February 2005, PT Multimédia announced the disposal of its 100 per cent. interest in Lusomundo Serviços, SGPS, S.A., including an 80.91 per cent. shareholding in Lusomundo Media, through the execution of a promissory sale and purchase agreement with Controlinveste, SGPS, S.A., a media and entertainment company. Through these companies, PT Multimédia previously ran a newspaper publishing and distribution business and a radio programming business. The sale was completed on 25 August 2005 after approval by the Portuguese Media Authority (Alta Autoridade para a Comunicação Social) and the Portuguese Competition Authority (Autoridade da Concorrência). The proceeds for PT Multimédia from the sale were €173.8 million, of which €10.1 million was paid to Portugal Telecom in connection with the acquisition of its 5.94 per cent. interest in Lusomundo Media, which was agreed prior to the closing of the transaction.

Overview. PT Multimédia's segments consist of:

- cable and satellite television through TV Cabo;
- broadband Internet access through cable modem provided by TV Cabo;
- telephony services (VoIP) provided by TV Cabo;
- TV programming activities through PT Conteúdos and its subsidiaries and affiliates;
- cinema distribution, negotiation of cinema rights for all film exhibition windows and distribution of DVDs, videos, and videogames through Lusomundo Audiovisuais; and
- cinema exhibition through Lusomundo Cinemas.

The diagram below shows PT Multimédia's major lines of business and the subsidiaries operating in each of those businesses as of 30 June 2007.



TV Cabo

PT Multimédia provides cable television and direct-to-home satellite television services through TV Cabo and its subsidiaries in Madeira and Azores. PT Multimédia owns 100 per cent. of TV Cabo. TV Cabo is also involved in advertising sales. In addition, it provides multimedia services, such as broadband cable Internet access and certain interactive digital television services. On 23 January 2007, TV Cabo launched telephony services, establishing itself as an integrated triple-play operator. The bundled triple play offer comprises Pay TV, broadband Internet and telephony. PT Multimédia expects that the sale of voice services to existing broadband customers should allow TV Cabo to further grow ARPU, increase broadband penetration, reduce churn and better segment its offers to meet customer demands.

Cable Television and Direct-to-Home Satellite Television Services. TV Cabo is the leading cable television operator in Portugal. At 30 June 2007, TV Cabo's cable network passed or provided potential access to approximately 2,699 million homes and had approximately 1,495 million cable and satellite customers, an increase of 3.6 per cent. over the first six months of 2006. At 30 June 2007, approximately 51.9 per cent. of TV Cabo's subscribers subscribed to its premium channels, for which it charges additional fees.

TV Cabo's cable television subscribers are charged an installation fee, a monthly subscription fee for programming packages and, for those with access to premium channels, an annual or monthly rental fee for set-top boxes.

Since September 1998, TV Cabo has also distributed a direct-to-home, or DTH, satellite television service in Portugal. TV Cabo distributes its DTH satellite service using Hispasat Satellite broadcasting capabilities. TV Cabo's DTH satellite service is the principal DTH digital multi-channel service specifically marketed in Portugal. TV Cabo's DTH satellite subscribers are charged an installation fee and a monthly subscription fee and are required either to purchase or rent from TV

Cabo a satellite dish and a digital set-top box. TV Cabo's DTH satellite service is mainly targeted at people whose homes are not served by TV Cabo's cable television network.

Because it offers cable and DTH satellite services, TV Cabo can distribute programming and advertising across Portugal. As of 30 June 2007, TV Cabo had approximately 1,495 thousand customers, of which 427 thousand were DTH satellite subscribers. At 30 June 2007, approximately 776 thousand of TV Cabo's subscribers subscribed to its premium channels, for which it charges additional fees.

Programming Content. As of 30 June 2007, TV Cabo offered 65 channels in its extended basic package (of which 40 were included in its basic package) and nine premium channels to cable and DTH satellite subscribers in continental Portugal. Over half of the channels distributed by TV Cabo, including Lusomundo channels (Premium, Gallery, Action and Happy) and Sport TV, which is described below, consist principally of programming that is in Portuguese or that has been dubbed or subtitled in Portuguese. The rest of the channels are mainly in English, with some channels in other European languages such as Spanish, French and German.

Broadband Internet Service. As of 30 June 2007, TV Cabo had approximately 381 thousand subscribers for its broadband Internet access product. In addition to its postpaid service, TV Cabo launched the first prepaid broadband product in Portugal in 2004 under the brand name "Zzt". TV Cabo was also the first operator to offer 1Mbps downstream speed. In 2006, TV Cabo enhanced its position by being the first ISP to lift the traffic limits on its 4Mbps and 8Mbps products. TV Cabo launched a 24Mbps Internet access product, positioning Netcabo as the fastest broadband service in the Portuguese market. Simultaneously, the broadband portfolio was updated with the launch of a 1Mbps product and the doubling to 8Mbps of the download speed of the Netcabo standard broadband product, known as "Netcabo Mega Plus".

Fixed Telephony. In the first half of 2007, fixed telephony subscribers reached 24 thousand. TV Cabo launched its telephony services on 23 January 2007, establishing itself as an integrated triple-play operator under the brand name "3 Play". Currently, this service is only available to customers that subscribe TV Cabo's Pay-TV services.

Digitalisation. In the first half of 2007, PT Multimédia continued its efforts to digitalize its Pay TV services. Digitalisation provides higher security levels in controlling illegal access to content (TV Cabo uses NAGRA's ALADIN conditional access system) and will allow PT Multimédia to make available to customers additional TV channels and services, such as VoD (video-on-demand), EPG (electronic programming guide), multi-game and multi-camera services, which add value to customers and create a competitive advantage. PT Multimédia aims to stimulate the migration of its clients from analog to digital services by offering a greater selection of content and services, as in the introduction of its Funtastic Life package in 2005. TV Cabo completed the digitalisation of its set top boxes during the first half of 2006, with the total number of digital set top boxes reaching 682 thousand at the end of December 2006. In 2006, "TV Cabo Funtastic Life", TV Cabo's 65-channel digital package, performed strongly and continued to drive new customer additions as well as ARPU expansion by enhancing the quality of the existing customer base. The digital package reached 270 thousand subscribers by the end of December 2006, with 160 thousand net additions in 2006.

Network. TV Cabo has made significant investments in the development of a hybrid fiber-coaxial broadband distribution network. TV Cabo's television signals are transmitted through fiber optic cables owned by PT's fixed line business under a service agreement regulated by ANACOM. In addition, TV Cabo has used PT Comunicações' existing ducts, wherever possible, to build its network. The network has a bandwidth of 750 MHz and 860 MHz in certain areas, and is sufficient to permit gradual migration to digital signals. The current design of the network allows it to increase capacity without significant additional capital expenditure. TV Cabo continued to invest in the expansion and upgrade of its network during 2006. The implementation of the "fiber to the hub" access network architecture in the greater Lisbon area was concluded, and five high-capacity optical fiber rings are now fully functional. At present, 98 per cent. of homes passed are bi-directional and therefore broadband and digital TV-enabled and 94 per cent. are VoIP-compliant.

Marketing. TV Cabo is pursuing aggressive marketing campaigns. It is promoting its premium channels, and highlighting the high level of Portuguese-language content on its channels, the new

Funtastic Life service and its broadband Internet access (NetCabo). TV Cabo markets its services through door-to-door selling, telemarketing and through Portugal Telecom shops, its own shops, supermarkets and other retail shops. PT believes the alliance with SIC, Sport TV and other content producers has been contributing to the increased penetration of TV Cabo, as the agreement contemplates cross promotions between free and cable TV, and increased advertising initiatives.

PT Conteúdos

PT Multimédia created PT Conteúdos to manage the Portuguese-language audiovisual programming activities previously managed by TV Cabo. After restrictions on cable operators engaging in any programming business were lifted in 1997, TV Cabo formed two joint ventures to develop programming channels in Portugal (Sport TV and Premium TV) and launched SIC Notícias, as described above. These ventures were aggregated under PT Conteúdos, which is 100 per cent. owned by PT Multimédia.

Until June 2003, PT Conteúdos owned 54 per cent. of Premium TV, a partnership with Globo and SIC. In June 2003, PT Conteúdos acquired the remaining 46 per cent. of the share capital of Premium TV held by Globo and SIC, which produced two premium movie channels-Telecine Premium and Telecine Gallery – using the film libraries of Globo. Until May 2003, these channels were distributed via cable and satellite, through TV Cabo’s platforms. In June 2003, PT Conteúdos replaced Telecine Premium and Telecine Gallery with two premium movie channels (Lusomundo Premium and Lusomundo Gallery), produced in-house using the film libraries of Lusomundo. PT Conteúdos launched Lusomundo Action in 2004 and Lusomundo Happy in 2005, as described above, and in December 2004, Premium TV was merged into PT Conteúdos and ceased to exist as a separate company.

PT Conteúdos also owns 50 per cent. of Sport TV Portugal, S.A., or Sport TV, a joint venture with PPTV-Publicidade de Portugal e Televisao, S.A., or PPTV. PPTV is a subsidiary of Olivadesportos, a Portuguese sports marketing firm. This joint venture produces Sport TV, a premium sports channel, which is distributed by Portuguese cable and satellite operators in exchange for a per-subscriber fee. Sport TV holds a licence to distribute most league matches of Portugal’s leading football league through 2008 and certain other European football leagues through 2006. Until November 2003, 33.33 per cent. of Sport TV was owned by each of PT Conteúdos, PPTV and Rádio Televisão Portuguesa, S.A., or RTP, the Portuguese state television operator. In November 2003, PT Multimédia entered into an agreement to purchase, through PT Conteúdos, an additional 16.67 per cent. stake in Sport TV from RTP for €16.3 million, thereby increasing its ownership in Sport TV to 50 per cent. The remaining 50 per cent. is now held by PPTV. The purchase was completed in April 2004. The agreement guarantees Sport TV exclusive broadcasting rights to Portuguese football league matches from 2004 through 2008.

PT Conteúdos also holds PT Multimédia’s 40 per cent. interest in Lisboa TV, the owner of SIC Notícias. See “– *TV Cabo*”, above.

PT Conteúdos is engaged in the wholesale business for content. From 2002 onwards, this company has been responsible for negotiations with content producers of the acquisition of rights to carry pay TV channels and other content. It resells that content to different distribution platforms, including TV Cabo’s pay TV and Internet platforms, as well as those of other operators.

PT Conteúdos sells advertising on some of the channels it distributes, where it has acquired the right to sell advertising as part of its content acquisition contracts. PT Conteúdos also manages the sale of advertising for TV Cabo’s channels in exchange for an agency fee.

Lusomundo Audiovisuals

Lusomundo’s Audiovisuals acquires rights for cinema, DVD, video, pay-per-view and television. It also produces its own Pay TV premium movie channels and distributes DVDs, videos and videogames. Lusomundo Audiovisuals has the right to distribute the following audiovisual content in Portugal:

- Theatrical Exhibition: Universal, Paramount (including Dreamworks), BUENA Vista International (Touchstone, Walt Disney Pictures) and independent producers; and

- Video: BVHE (Walt Disney), Paramount (including Dreamworks) and independent producers.

In the first half of 2007, PT Multimedia's market position in the area of cinema distribution remained broadly stable in 50 per cent of market share, primarily due to the launch of a significant number of films with high potential and the increase in the number of films released. In the first half of 2007, PT Multimédia had 13 of the top 20 most seen films.

Lusomundo Cinemas

Lusomundo Cinemas is the market leader in Portuguese cinema exhibition, with a 48.6 per cent. market share. In 2007, PT Multimédia continued its policy of market analysis, seeking opportunities for expansion and increased profitability of its business. As at the end of June 2007, PT Multimédia had 28 film complexes, with a total of 188 screens. In the first half of 2007, the number of tickets sold in Portugal increased 4.9 per cent. year on year, reaching 3,817 thousand tickets.

As discussed above under “– Multimedia Business,” PT Multimédia completed the disposal of its interest in Lusomundo Serviços in August 2005, following clearance from the Portuguese competition authority. As from that date, PT Multimédia ceased to operate in the newspapers and magazine publishing and distribution business and in the radio programming business.

International Investments

In 2004, PT created Portugal Telecom Investimentos Internacionais – Consultoria Internacional, S.A., or PT II, to manage all of PT's international businesses other than PT's investment in Vivo described above.

Investments in Brazil

Portugal Telecom has certain additional investments in Brazil, in addition to its investment in Vivo described above, including, most significantly, Mobitel, a call centre company, and UOL, a leading Internet Service Provider.

Mobitel. Mobitel provides call centre services in Brazil primarily to Vivo. Mobitel's operating revenues were R\$267 million in 2006 and R\$255 million in 2005. As of 30 June 2007, PT's participation in Mobitel was 100 per cent. and revenues were R\$136 million.

UOL. UOL is a leading Internet Service Provider in Brazil. In December 2005, PT sold a 16 per cent stake in UOL in its initial public offering in Brazil and received net proceeds of R\$201.0 million. As of 30 June 2007, PT's participation in UOL was 29 per cent. Revenues in 2006 were R\$480.7 million.

Investments in Africa

PT has certain investments in Africa, including most significantly, investments in Angola, Cape Verde Islands, Namibia and Morocco. In addition to these investments, on 13 August 2007 Portugal Telecom established a strategic partnership with Helios Investors LP (**Helios**), a leading African private equity firm operating sub-Saharan Africa, in relation to the sub-Saharan telecommunications market. Under the terms of the agreement, Helios initially acquired a 22 per cent stake in “Africa Holding”, the holding company that will hold all of PT's current interests in sub-Saharan Africa.

The common objective of the strategic partnership is to create and further develop a unified, coherent, multi-country telecommunications service provider across sub-Saharan Africa, by combining certain assets and the telecoms strength of PT with Helios' African knowledge, contacts and expertise, as well as its financial and telecoms management know-how. Apart from managing the current portfolio of assets, “Africa Holding” will also focus on selectively expanding its business in the region, with the view to creating additional value for its shareholders.

Unitel in Angola. At the end of 2000, PT acquired 25 per cent. of the share capital of Unitel, a GSM mobile operator in Angola. Unitel's other shareholders are Sonangol, which holds 25 per cent., and other local partners, which hold the remaining 50 per cent. PT is the operational manager of the venture, which began operations in Luanda in April 2001. As of 31 December 2006, Unitel had 2,049 thousand subscribers of which 99.6 per cent. were prepaid cards. At the end of June 2007, Unitel had 2,503 thousand subscribers.

Unitel's total gross operating revenues were US\$649.3 million in 2006 (€517.1 million) and US\$445 million in 2005 (€357.5 million). In the first semester of 2007, Unitel's gross operating revenues were US\$375.2 million (€281.2 million).

Cabo Verde Telecom. PT owns 40 per cent. of the share capital of Cabo Verde Telecom. Cabo Verde Telecom provides fixed, mobile and data services in the Cabo Verde Islands, a Portuguese speaking country off the coast of West Africa.

At 30 June 2007, Cabo Verde Telecom had 74.3 thousand fixed lines in service, which represents approximately 15 fixed main lines per 100 inhabitants. Cabo Verde Telecom had 119 thousand active mobile telephone cards at 30 June 2007 (approximately 25 active mobile telephone cards per 100 inhabitants), of which 99.4 per cent. were prepaid customers. At 30th June 2007, Cabo Verde Telecom reached 6.6 thousand active Internet users.

Cabo Verde Telecom's total gross operating revenues were €32.1 million in the six months ended 30 June 2007, €63.3 million in 2006 and €55.3 million in 2005.

MTC in Namibia. In September 2006, Portugal Telecom acquired 34 per cent. of the capital of MTC, the Namibian mobile operator. In connection with this transaction, PT entered into an agreement with the other shareholders of MTC that allows PT to set and control the financial and operating policies of this company. As of 31st December, 2006, MTC had 610,000 customers, of which 91.6 per cent. were customers under prepaid plans. MTC revenues were 999.6 million Namibian dollars (€116 million) in 2006 and 824.8 million Namibian dollars (€104.3 million) in 2005. At the end of June 2007, MTC had 705,153 customers. Its revenues were 545.9 million Namibian dollars (€57.0 million) in the first half of 2007.

Medi Telecom in Morocco. In August 1999, Medi Telecom, a consortium made up of Portugal Telecom, Telefónica Móviles and certain Moroccan entities, bid for and won a license to operate a GSM mobile network in Morocco. This was the second such license issued by the Moroccan government. The license fee was 9.0 billion Moroccan dirhams (€929 million). Medi Telecom entered into a €1 billion project financing facility. PT initially held 34.5 per cent. of Medi Telecom, having invested approximately €166 million, but in January 2000 PT sold 4 per cent. of its interest in compliance with a condition of the bid process for the same license. At the end of 2002, following a capital increase, Portugal Telecom raised its equity share to 31.34 per cent., equal to Telefónica's position. During the fourth quarter of 2003, following another share capital increase, Portugal Telecom raised its equity share to 32.18 per cent. At the end of 2005, Medi decreased its share capital from 8.834 million Dirhams (€803.0 million) to 4.683 million Dirhams (€425.0 million) in order to fulfil required capital ratios in Morocco. Portugal Telecom's share of Medi Telecom's capital remained the same (32.18 per cent.).

Medi Telecom began operations at the end of March 2000. As of 30 June 2007, it had 5,800 thousand subscribers, which corresponds to an estimated market share of approximately 33.6 per cent. Approximately 97.3 per cent. of its active mobile telephone cards are prepaid. PT manages the operations of Medi Telecom jointly with Telefónica.

Medi Telecom's total gross operating revenues were 2,367 million Dirhams (€212.2 million) in the six months ended 30 June 2007, 4,691 million Dirhams (€425.1 million) in 2006 and 4,373 million Dirhams (€397.0 million) in 2005.

Investments in Asia

PT has certain investments in Asia, including, most significantly, investment in CTM.

CTM. PT has a 28 per cent. interest in Companhia de Telecomunicações de Macau, or CTM, the exclusive provider of fixed line services and a provider of mobile telephone services in Macau. Macau, an enclave situated near Hong Kong on the coast of the Guangzhou Province, China, was a territory administered by the Portuguese government until December 1999 when its administration was transferred to the People's Republic of China. The other shareholders of CTM are Cable & Wireless plc and CITIC Pacific.

At 31 December 2006, CTM had 177.3 thousand fixed main lines in service. This figure represents approximately 39 fixed main lines per 100 inhabitants. CTM's mobile telephone services are

growing rapidly, with 316.8 thousand active mobile telephone cards at 30 June 2007 and 70 active mobile telephone cards per 100 inhabitants. CTM uses GSM digital mobile technology.

CTM's total gross operating revenues were 1,052 million Patacas (€98 million) in the six months ended 30 June 2007, 2,101 million Patacas (€209.1 million) in 2006 and 1,895 million Patacas (€190.0 million) in 2005.

Instrumental Companies

PT SI. PT SI is the group unit responsible for data centers, information systems and information technology activities of PT's business units in Portugal. PT SI provides integrated information systems and information technology services to Portugal Telecom's business units in Portugal, as well as to its existing and new customers. Portugal Telecom holds 100 per cent. of the share capital of PT SI. In recent years, PT SI has subcontracted certain information technology services to DCSI-Dados, Computadores e Soluções Informáticas, or DCSI, an information technology company controlled by IBM. In March 2006, Portugal Telecom signed a contract with IBM to purchase DCSI.

PT Inovação. PT Inovação is the group unit responsible for research and development activities. Portugal Telecom's research and development programs focus on intelligent networks, network management systems, advanced services and systems and network integration. Its research and development activities have been responsible for the introduction of innovative products and services and for the development of in-house technology. These activities have allowed Portugal Telecom's employees to remain up-to-date in terms of technology and technological development in the telecommunications sector on both a European and a worldwide level. PT Inovação's activities have been a driving force behind the development of new products and services, telecommunications infrastructure and information systems.

PT Contact. PT Contact is the group unit responsible for call center operations in Portugal. PT Contact takes advantage of economies of scale and process alignments to reduce costs in Portugal Telecom's call center operations.

PT PRO. In February 2003, Portugal Telecom created PT PRO to aggregate all its back-office activities in Portugal. PT PRO takes advantage of economies of scale and process alignments throughout the group to reduce costs in back-office activities. The creation of PT PRO has also allowed for a reduction of the execution risk of Portugal Telecom's financial reporting function through standardisation of processes and implementation of best practices.

PT Compras. In May 2003, Portugal Telecom created PT Compras and transferred its newly created central purchasing unit to this company. PT Compras is optimising Portugal Telecom's purchasing function on an integrated basis. Taking advantage of scale and specialisation, PT Compras is increasing pressure in reducing suppliers' prices and improving the levels of quality and service.

Strategic Alliances

Alliance with Telefónica

In April 1997, Portugal Telecom entered into a cooperation agreement with Telefónica. The main focus of the agreement is cooperation in international investments, particularly in Latin America. In 1999, Portugal Telecom commenced operations with Telefónica in Morocco.

On 23 January 2001, Portugal Telecom entered into a strategic agreement with Telefónica to create a mobile services joint venture company in Brazil that would aggregate all of Portugal Telecom's mobile assets with those of Telefónica Móviles, the former mobile subsidiary of Telefónica that has merged into Telefónica, to the extent permitted under Brazilian law. The joint venture was formed on 27 December 2002. See “– *Domestic Mobile Business.*” PT and Telefónica transferred all of their respective interests in Brazilian mobile services companies to the joint venture, named Brasilcel and operating under the brand name Vivo since April 2003, with its head office in the Netherlands. PT hold its interest in Brasilcel through PT Móveis, and Telefónica holds its interest through Telefónica Móviles. PT's agreements governing the ownership and management of Brasilcel have been entered into by those entities.

Brasilcel is managed by a Managing Board of four members and a Supervisory Board of 12 members. PT and Telefónica each appoint two members of the Managing Board and six members of the Supervisory Board, and in each case the Chairman is appointed by Telefónica and the Vice Chairman is appointed by PT. The Managing Board acts by unanimous decision so long as each party holds at least a 40 per cent. interest in Brasilcel, and for certain important decisions, the Managing Board requires the approval of the Supervisory Board. The Supervisory Board acts by majority vote, except that generally so long as each party holds at least a 40 per cent. interest in Brasilcel and for six months following the dilution of a party's interest below 40 per cent. due to a capital increase, at least one member of the Supervisory Board appointed by each party must approve any action by the Supervisory Board.

In the event that either PT's or Telefónica's interest is diluted below 50 per cent., but not lower than 40 per cent., due to a capital increase, the diluted party can re-build its interest to 50 per cent. within 12 months from the date of dilution. During such period, Brasilcel would be managed on an equal basis. PT or Telefónica can maintain their share ownership percentage by contributing with cash or liquid assets. Should the percentage of the share capital in Brasilcel that PT or Telefónica holds fall below 40 per cent. and remain below 40 per cent. for six consecutive months thereafter, PT's respective numbers of directors on the board will be changed to reflect PT's proportional shareholdings and the diluted shareholder will lose its right to appoint the CEO or CFO of Brasilcel's subsidiaries, as applicable, as described below.

If a deadlock over an important issue in the decision-making of Brasilcel cannot be resolved by the chairmen and CEOs of PT and Telefónica, then the issue will be settled by reference to a committee of third party "wise persons".

Potential acquisitions of wireless and mobile telephone operators in Brazil may be pursued by Brasilcel or by PT or Telefónica and subsequently contributed to Brasilcel. New acquisitions by Brasilcel require the approval of a majority of the Board of Directors of Brasilcel. If either PT or Telefónica acquire a mobile operator in Brazil, the acquiring party must offer the right to a 50 per cent. participation in the acquisition to the other party.

Under the agreement, PT selects the CEO of each subsidiary of Brasilcel, including Vivo Participações S.A. (formerly known as TCP), and Telefónica selects the CFO. So long as the Board of Directors of any subsidiary of Brasilcel consists of nine members (as is the case with Vivo Participações S.A.), PT and Telefónica will each nominate three members to the Board of Directors. PT and Telefónica have agreed to coordinate their votes for meetings of the boards of directors of Brasilcel's subsidiaries at the level of Brasilcel.

In the event of a change of control of either PT or Telefónica, the unaffected party shall have the right to sell the shares that it owns in Brasilcel to the affected party at a value determined pursuant to an independent appraisal. A change of control occurs if 15 per cent. or more of the voting rights of Portugal Telecom or Telefónica S.A. are acquired by another telecom operator not acting in concert with the other party, if a corporate transaction is affected by virtue of which the voting share capital of Portugal Telecom or Telefónica S.A. is at least doubled and there is a change in the majority of the Board of Directors of that party or, in the case of any entity or affiliate of the Portugal Telecom or Telefónica group that holds an interest in Brasilcel (other than Portugal Telecom and Telefónica S.A.), if the majority of the voting rights of that entity or affiliate is transferred to another telecom operator and there is a change in the majority of its Board of Directors. In addition, if PT is diluted to below a 40 per cent. interest in Brasilcel and fail to increase PT's interest to 40 per cent. within a six-month period, PT will have the right to sell its interest in Brasilcel to Telefónica within one year from the expiration of the applicable six-month period at a price to be determined by a third party.

If either party wishes or is required to transfer all or part of its equity interest in Brasilcel to a third party, the non-transferring party will have a right of first refusal to purchase the equity interest or, alternatively, a tag-along right to sell its equity interest under specified conditions.

As part of its initial agreement with Telefónica, PT acquired 1.0 per cent. of Telefónica's share capital and Telefónica acquired 3.5 per cent. of PT's share capital. PT and Telefónica also gave each other a right of first refusal on any transfer of their respective interests. In addition, a member of

PT's board who is an executive officer is serving on Telefónica's board as a non-executive director and a member of Telefónica's board who is an executive officer is serving on PT's board as a non-executive director. Under the terms of its strategic agreement with Telefónica, PT may acquire up to 1.5 per cent. of Telefónica's share capital, and Telefónica may increase its ownership interest in PT's share capital up to 10 per cent. As of 31 December 2006, Telefónica's interest in PT's share capital was 9.96 per cent. Neither party controls the operations or management of the other.

Alliance with Banco Espírito Santo and Caixa Geral de Depósitos

PT announced on 5 April 2000 the signing of a strategic partnership agreement with the Banco Espírito Santo group ("BES") and Caixa Geral de Depósitos ("Caixa") for the development of "new economy" initiatives. This agreement involved an increase of BES's stake in PT to 6 per cent., PT having taken a 3 per cent. stake in BES. Under the agreement, PT launched various initiatives in business-to-consumer and business-to-business e-commerce and new mobile service areas. As of 31st December, 2006, BES owned 7.77 per cent. of Portugal Telecom's share capital. In accordance with this arrangement, an executive officer of BES serves as a non-executive member of Portugal Telecom's Board of Directors. An executive member of Portugal Telecom's Board of Directors also serves as a non-executive member of the Board of Directors of BES.

Under this strategic partnership agreement, PT launched various initiatives in business-to-consumer and business-to-business e-commerce and new mobile service areas in business-to consumer and e-finance, business-to-business and M-commerce and payment services.

Developments Relating to PT's Share Capital

In September 2003, PT announced its intention to buy back 10.0 per cent. of its share capital by the end of 2004, subject to financial and market conditions. Pursuant to its share buyback program, PT reduced its share capital in December 2004 by 7.0 per cent. through the cancellation of 87,799,950 treasury shares acquired during 2003 and 2004, at an average price of €7.87 per share. In addition to treasury shares repurchased directly by PT, PT entered into equity swap contracts to buy 21,551,006 shares during 2004.

In December 2005, PT reduced its share capital from €1,166,485,050 to €1,128,856,500 through the cancellation of 37,628,550 treasury shares that PT purchased during 2005. The number of treasury shares cancelled was equivalent to 3.0 per cent. of the initial share capital prior to the 7.0 per cent. cancellation in December 2004, thus completing the 10.0 per cent. share buyback announced in September 2003.

A new share buyback program was approved by PT's shareholders in April 2005, providing for the acquisition of up to 3.0 per cent. of PT's share capital. PT's purchases under this share buyback program was suspended while the tender offer by Sonacom for PT's ordinary shares was pending. As of 31 December 2006, PT had entered into equity swaps for 20,640,000 shares with a notional amount of €187.6 million under this share buyback program, corresponding to 1.83 per cent. of PT's share capital.

On 21 April 2006, PT's shareholders approved a share capital increase in the amount of €338,656,950. At the same time, PT's shareholders approved a share capital reduction to €395,099,775 carried out through a reduction in the par value of PT shares to €0.35 per share.

As part of the share buyback program approved at the Annual General Meeting held on 27 April 2007, Portugal Telecom has entered into equity swap agreements with several financial institutions over a total of 69,689,692 shares, representing 6.17 per cent. of PT's share capital, as at 26 July 2007.

On 22 May 2007, Portugal Telecom completed both its share capital increase and reduction approved at the Annual General Meeting held on 27 April 2007. The share capital increase amounted to €79,019,955 and was realized through the incorporation of legal reserves. The share capital reduction amounted to €440,254,035 and its amount was transferred to the caption "Accumulated earnings". Following these transactions, the par value of Portugal Telecom shares decreased from €0.35 to €0.03.

As of the date of this Offering Circular, Portugal Telecom's share capital is €33,865,695, consisting of 1,128,856,000 issued ordinary shares and 500 A class shares, each with a nominal value of €0.03 per share.

Privatisation

On 4 December 2000 and 18 December 2000, the fifth phase of the privatisation of Portugal Telecom was completed. The Portuguese Government sold 111,267,645 ordinary shares and Portugal Telecom's share capital was simultaneously increased from €1,045,000,000 by the issuance of 156,749,500 new ordinary shares. After the conclusion of these offerings, the Portuguese State's ownership of the share capital of Portugal Telecom was reduced from approximately 11 per cent. to less than 1 per cent. The Portuguese State continues to hold all 500 A shares, which give it the right, under PT's Articles of Association, to veto a number of important actions, including, among other things, dividends in excess of 40 per cent. of Portugal Telecom's distributable net income in any year and capital increases and other amendments to Portugal Telecom's Articles of Association.

Employees

Portugal Telecom had a total of 12,462 employees in its domestic business at 30 June 2007; 12,666 employees at 31 December 2006; 13,101 employees at 31 December 2005 and 13,886 employees at 31 December 2004. PT has not experienced material work stoppages over the last five years. These figures include temporary workers employed under fixed-term contracts.

The table below sets forth the breakdown in the total number of Portugal Telecom's employees in the years 2004 through 2006. It does not include employees seconded to other entities, but does include temporary workers with fixed-term contracts.

	<i>At 31st December</i>		
	<u>2004</u>	<u>2005</u>	<u>2006</u>
Wireline.....	8,311	7,682	7,181
TMN.....	1,133	1,184	1,140
PT Multimédia.....	1,302	1,388	1,376
Vivo ⁽¹⁾	3,175	3,042	2,948
Other Businesses ⁽²⁾	13,858	19,094	19,413
TOTAL⁽³⁾.....	<u><u>27,780</u></u>	<u><u>32,389</u></u>	<u><u>32,058</u></u>

(1) The number of employees corresponds to 50 per cent. of the employees of Vivo.

(2) The increase in 2005 resulted primarily from employees working in call center operations in Brazil (Mobitel), which were outsourced externally in previous years. Mobitel had 15,232 employees at the end of 2005, as compared to 7,991 employees at the end of 2004. The increase in 2006 is mainly related to the consolidation of MTC, which had 322 employees at the end of 2006.

(3) Of this total, PT employed 13,886, 13,101 and 12,666 respectively, 2004, 2005 and 2006 in PT's domestic businesses and 13,894, 19,289 and 19,392 respectively, 2004, 2005 and 2006 in PT's international businesses.

The net reduction in the number of Portugal Telecom's employees since 2001 in the wireline business results primarily from voluntary severance arrangements, retirement programmes and suspension of employment contracts. Portugal Telecom reduced its fixed line telephone service workforce by 792 employees in 2006. The total costs of these reductions during 2006 were approximately €229 million.

Competition

PT faces substantial and increasing competition. The Portuguese telecommunications sector has been open fully to competition since 1 January 2000. PT has competitors able to compete with it in each of its service areas. In response to the competition PT is already experiencing and in anticipation of intensified competition, PT is pursuing a range of strategic initiatives. Through these, PT intends to reposition, modernise and prepare itself for the challenging new environment in which it operates.

Portugal

Competition Facing PT's Wireline Business

Since 1 January 2000, PT no longer has the exclusive right to provide domestic and international public switched fixed line telephone services or to install and operate the related telecommunications networks in Portugal.

Retail. PT's wireline business faces increasingly strong competition from new fixed-line operators as well as from mobile telephone service providers, including its own mobile service provider, TMN. The number of subscribers to mobile services in Portugal now outnumbers the number of wire lines in Portugal. At the end of 2006, there were approximately 115.7 active mobile telephone cards per 100 inhabitants in the Portuguese market. This growth is a result of residential subscribers adding mobile cards for family members and businesses adding mobile cards for their employees. Vodafone Portugal and Optimus are already marketing their mobile services as an alternative to PT's wireline telephone services, and PT competes with them for market share. For example, Optimus and Vodafone have launched services called "Optimus Home" and "Vodafone Casa," respectively, that use their GSM mobile networks but use fixed line phone numbers. TMN requested an authorisation to launch a similar service and received that authorisation in 2007. The low-cost brands launched by TMN, (Uzo) Optimus, (Rede 4) and Vodafone (Directo) are designed to reach the lower end segment of the mobile market and have also had an effect on PT's fixed line retail service, exacerbating the trend among consumers toward switching from fixed line to mobile service.

Vodafone Portugal and Optimus (owned by Sonaecom and France Telecom) have major shareholders that can provide them with substantial resources. In addition to strengthening their position in the mobile telephone market, these resources enable them to compete directly and aggressively with PT's fixed-line telephone services.

According to ANACOM figures, on 31 December 2006, PT Comunicações, which provides retail services as part of PT's wireline business, had an estimated 78.7 per cent. market share of access lines (89.3 per cent. in 2005). According to ANACOM figures and PT's estimates at 31 December 2006, PT Comunicações had an estimated 78.2 per cent. market share of total outgoing traffic (in minutes), a decrease of 6.3 percentage points from 31 December 2005. In addition, PT Comunicações had an estimated 70.5 per cent. market share of domestic outgoing voice traffic (in minutes), a decrease of five percentage points from 31 December 2005.

PT's primary competitors in the wireline voice market include Tele 2 (recently acquired by Sonaecom), Novis (owned by Sonaecom and France Telecom), Oni Telecom – Infocomunicações, S.A. (owned by certain investment funds), AR Telecom (formerly Jazztel) and Colt. All of the new entrants have focused on providing their customers with national and international services over their networks without direct interconnection. These customers must still connect to PT's competitors' services through PT's fixed lines.

The cable operator, Cabovisão, offers a package of Internet, cable TV and voice services to the residential segment. Cabovisão has attracted some of PT's local customer market and may continue to do so.

Measures such as call-by-call selection (introduced on 1 January 2000) and carrier pre-selection (introduced on 1 October 2000), as well as number portability (introduced on 1 July 2001), make it easier for PT's competitors to attract PT's customers to their services. At 31 December 2006, PT estimates that there were approximately 430 thousand lines in pre-selection. For example, Tele 2 has been effective in using carrier pre-selection to increase its market share.

PT is losing revenues from its international telephone services because PT no longer has the exclusive right to provide fixed-line telephone services, and large telecommunications users lease lines through which they connect to networks outside Portugal. At 31 December 2006, according to ANACOM data and PT's estimates, PT Comunicações had an estimated 76.4 per cent. market share of international traffic (in minutes), an increase of 4.7 percentage points from 31 December 2005, although the market share of PT Comunicações decreased by an estimated 4.4 percentage points from 31 December 2004 to 31 December 2005. In addition, PT is losing revenues from its international telephone services as mobile operators establish direct international interconnections with mobile or fixed-line networks outside of Portugal, enabling them to offer international telephone services

without using PT's network. PT also faces indirect competition in international fixed-line telephone services from calling cards and rerouting of calls by other international operators. Together with falling international call prices worldwide, these factors put pressure on PT to reduce international fixed-line telephone prices.

In response to full competition, PT has been lowering the prices of its wireline telephone services. In 2006, prices reduced by 5.9 per cent. for regional calls and 16.0 per cent. for domestic long distance on average, compared with 2005. PT believes its price structure is now competitive and that it is meeting the challenge of full competition.

The overall effect of full competition partly depends on the prices that other mobile and wireline network operators pay PT to interconnect with PT's network. Portuguese law requires PT to lease lines to PT's competitors. It also obliges PT to interconnect our network with PT's competitors' networks or lines leased by them. PT's interconnection rates are subject to regulatory review. See "*Regulation – Portugal – Pricing of Wireline Services – Interconnection Prices*". New entrants and resellers of lines leased from existing operators have made very rapid inroads into other EU telecommunications markets that have also opened up to full competition, and PT sees the same trends in Portugal.

Wholesale. Mobile operators, other than TMN, are establishing direct international interconnections with mobile or wireline operators outside Portugal, enabling them to offer international telephone services without using PT's network. This is reducing PT's wholesale revenues generated from connecting mobile operators in Portugal to operators abroad.

PT's interconnection business faces more direct competition now that other operators may install and operate their own public wireline telephone networks. Mobile and wireline networks, which are PT's interconnection customers, can interconnect with these new networks rather than with PT's. Other competitors may also establish local networks using other technologies such as local radio systems, fiber optic technologies and new mobile systems that may be used to complete calls which are currently made to PT's subscribers.

Data and Corporate. PT faces significant competition from several operators. PT's principal data communications and business solutions competitors include companies associated with Oni Telecom, Novis, Colt, AR Telecom (formerly Jazztel) and Vodafone Portugal. These companies compete with PT in providing data communications, voice, services and Internet services to business customers. Such service providers can use lines leased from PT or PT's own networks. This market is now highly competitive. These customers tend to have large volumes of traffic and complex virtual private network services with data, voice and video integration.

PT's competitors may use satellite-based networks, the infrastructure of public network operators, leased lines and their own infrastructure to offer telecommunications services to customers. These are all alternatives to leasing lines from PT for data communications. As a result of competition, PT has reduced its prices for leased lines and is focusing on value-added solutions based on Internet Protocol Virtual Private Networks, or IP VPN.

Competition Facing TMN in Portugal

TMN competes with Vodafone Portugal and Optimus, the two other mobile operators licensed to provide mobile telephone services in Portugal. According to figures from ANACOM, at the end of 2006, in terms of the number of active mobile telephone cards in the Portuguese market, TMN had a 46.7 per cent. market share. TMN has made maintaining its market share a priority. As a result of a very competitive market, TMN's market share of mobile subscribers increased 0.3 percentage points in 2006 compared to 2005.

TMN's competitive strategy includes focusing on excellent subscriber care and innovative services. As a result of its customer service, TMN received the "Call Centre 2006" awards for best practices. In addition, TMN and Tektronix Inc., which designed the software that allows TMN to evaluate the performance and efficiency of its second and third generation networks, received an award for the "Best Network Quality Initiative" at the GSM Association Awards 2006 in February 2006.

Vodafone Portugal and Optimus each have major shareholders that could provide them with substantial resources to compete aggressively against PT in the Portuguese mobile telephone market. Sonaecom and France Telecom are the major shareholders in Sonaecom, the holding company that controls Optimus.

Competition is increasing in the mobile services sector in Portugal as TMN and its competitors develop new services. In addition, the commercial introduction in Portugal of third generation mobile services has heightened competition and reduced the profitability of providing third generation services. Moreover, ANACOM may open the mobile market to mobile virtual network operators, or MVNOs, which do not have their own network infrastructure and thus would not have the fixed cost burdens facing PT's current GSM and UMTS services. Competition from companies providing WLAN services, which can deliver wireless data services more cheaply than UMTS in concentrated areas, may also affect the market and pricing for third generation services. PT believes that its mobile competitors, Vodafone and Optimus, will continue to market their services aggressively. In mid-2005, Optimus introduced a low-cost brand "Rede 4" in response to PT's new brand "Uzo". Vodafone also launched a similar product called Directo in mid-2005 targeting the same market as Uzo and Rede 4.

Competition Facing PT Multimédia's Pay TV and Broadband Internet Business

Certain cable television operators are authorized to provide services in Portugal in addition to PT Multimédia's subsidiary, TV Cabo. PT Multimédia's competitors operate principally in Portugal's major cities and include Cabovisão, Pluriconel Santarem, Pluricanel Leiria, TV TEL and Bragatel. According to ANACOM figures, PT estimates that at the end of 2005, TV Cabo's competitors had approximately 17 per cent. of the total number of subscribers in the pay-TV market.

TV Cabo currently has control over nine cable authorisations covering 125 counties in seven regions in continental Portugal and the Madeira and Azores Islands, all of which expire in May 2009. In February 2004, a new regulatory framework was introduced under which no specific authorisations or licenses for the provision of cable television services are required. After the current authorisations expire, the existing licenses will not be renewed, and the new regulatory framework will apply. See "*Regulation – TV Cabo's Cable Television Authorisations*". PT therefore expects competition to increase as a result of this regulatory flexibility.

PT Multimédia competes for advertising revenue with terrestrial television companies (free-to-air channels) and other forms of media such as newspapers, magazines, radio, billboards and the Internet. It also competes with terrestrial television companies for the acquisition of programming to attract viewers. Such competition can increase program acquisition costs.

PT Multimédia competes with cable companies, such as Cabovisão, in the provision of broadband Internet services.

In August 2001, the Portuguese government granted an authorisation to Plataforma de Televisão Digital Portuguesa, S.A., or PTDP, to provide digital terrestrial television services. ANACOM instructed PTDP that it must begin operations before 1 March 2003. As PTDP had difficulty complying with this instruction, ANACOM, with PTDP's agreement, proposed to the Ministry of Economy that PTDP's authorisation be revoked. By order of the Minister of Economy, dated 25 March 2003 (Ministerial order 6973/2003, published on 9 April 2003), the authorisation was revoked. In 2005, the Portuguese government announced that it intends to reopen competitive bidding for a license to provide digital terrestrial television services in Portugal, which could result in increased competition for TV Cabo. In 2007, the Portuguese government is expected to open competitive bidding for one or more licenses for the provision of digital terrestrial television services.

As existing technology develops and new technologies emerge, competition is likely to intensify, in particular with regard to products and services related to subscription TV and the Internet. PT Multimédia's cable and satellite business faces competition from broadband local loop access based on wireless technologies (Broadband Wireless Access). In 2005, Ar Telecom (formerly Jazztel), a direct competitor, launched broadband wireless service in the geographic areas where it operates. Also, PT expects video over ADSL to increase competition. Novis launched an IP television offer in 2006 that competes with PT Multimédia's television services, and Portugal Telecom launched an IPTV service through PT Comunicações in June 2007.

Competition Facing PT Multimédia's Audiovisuals Business

In the four main sub-segments of this business segment (film distribution, cinema exhibition, video distribution and distribution of rights for TV broadcasting), PT Multimédia faces competition from various entities that differ from segment to segment, as follows:

- Film distribution: Filmes Castello Lopes, LNK Filmes, Columbia Tristar Warner Filmes de Portugal, Atlanta Filmes and Sociedade Distribuidora Vitoria Filmes;
- Cinema exhibition: Socorama-Sociedade Comercial de Cinemas, Medeia Filmes, New Lineo – Cinemas de Portugal, UCI Cinemas – United Cinemas international and AMC;
- Video distribution: LNK Filmes, Ecovideo, Universal Home Video, Warner Home Video; Castello Lopes, Selecções Readers Digest and Planeta Agostini; and
- Distribution of rights for TV broadcasting: Warner Television, Columbia Television, Fox Television, Paramount Television, Buena Vista International Television, Universal Television, LNK, Ecofilmes and Castello Lopes.

In all of the activities mentioned above, except in the distribution of rights for TV broadcasting, where the free-to-air TV stations are basically supplied by the international market, Lusomundo Audiovisuais and Lusomundo Cinemas are market leaders in Portugal in terms of the number of movie titles distributed and the number of movie theaters owned, according to ICAM, the Portuguese Cinema, Audiovisual and Multimedia Institute.

Brazil

Competition Facing Vivo in Brazil

Vivo faces intense competition in all the areas in which it operates, principally from other mobile service providers and also from fixed-line operators. Many of these competitors are part of large, national or multinational groups and therefore have access to financing, new technologies and other benefits that are derived from being a part of such a group. Fixed-line operators generally charge much lower tariffs than mobile service providers.

Vivo's main mobile competitor in the state of São Paulo is Claro. Claro is controlled by a consortium led by the Telecom Américas Ltd. (controlled by América Móvil S.A. de C.V.). Claro began providing cellular telecommunications services in this region at the end of 1998. Although Claro provides only digital service, its customers use TDMA dual mode cellular handsets that can operate on an analog network and GSM handsets. The main fixed-line operator in this state is Telecomunicações de São Paulo S.A. – Telesp, known as Telefónica.

Vivo's principal cellular competitor in the states of Paraná and Santa Catarina is Tele Celular Sul Participações S.A., or TIM Sul. The main fixed-line operator in those states is Brasil Telecom S.A. Vivo's principal mobile competitor in the region encompassing the states of Mato Grosso do Sul, Mato Grosso, Goiás, Tocantins, Rondônia and Acre and the Federal District is Claro, and its principal competitor in the region encompassing the states of Amazonas, Roraima, Pará, Amapá and Maranhão is TIM. The main fixed-line operators in this area are Brasil Telecom S.A., in the region encompassing the states of Mato Grosso do Sul, Mato Grosso, Goiás, Tocantins, Rondônia and Acre and the Federal District, and Telemar Norte Leste S.A. – Telemar, in the region encompassing the states of Amazonas, Roraima, Pará, Amapá and Maranhão. Other competitors include Oi, the Telemar mobile operator.

In the Salvador and Sergipe service areas, Vivo's main mobile competitor is Oi (TNL PCS S.A.). Other mobile competitors are TIM (Maxitel S.A.), which also operates in the state of Minas Gerais, and Claro (Stemar Telecomunicações Ltda.). The principal fixed-line competitor in this area is Telemar Norte Leste S.A.

In the Rio de Janeiro and Espírito Santo service areas, Vivo's main mobile competitor is Claro. The principal fixed-line operator in this area is Telemar Norte Leste S.A. Oi also competes in the mobile market and is integrated with Telemar.

In Rio Grande do Sul, Vivo's primary mobile competitor is Claro, and its other mobile competitors are Brasil Telecom S.A. and TIM. Vivo's main fixed-line competitor in this area is Brasil Telecom.

Vivo also competes with certain other wireless telecommunications services in specific segments, such as mobile radio (including digital trunking technology, offered by Nextel), paging and beeper services, which are used by some operators in its areas as a substitute for cellular telecommunications services. These competing wireless telecommunications services are generally less expensive than mobile telecommunications services.

Satellite operated services, which provide nationwide coverage, are also available in Brazil. Although these services have the advantage of covering much larger areas than those covered by the cellular telecommunications services, they are considerably more expensive than the mobile telecommunications services Vivo offers and do not provide competitive coverage inside buildings.

Regulation

In addition to the descriptions of regulatory matters set forth below, see the description of certain legal proceedings, including judicial and administrative proceedings relating to regulatory matters, set forth in “*General Information – Litigation.*”

The telecommunications industry has traditionally been heavily regulated in most countries of the world, including Portugal and Brazil. Over the last several years, both countries (Portugal beginning in 1990 and Brazil in 1998) have substantially privatised their state-held telecommunications operators and have been opening their telecommunications markets to competition. Portugal, a member of the European Union, opened its telecommunications market to full competition as of 1 January 2000. Portugal is pursuing further EU-led initiatives aimed at increasing the competitiveness of its market. Brazil has also been introducing further measures designed to increase competition.

Regulation – Portugal

In the increasingly competitive Portuguese telecommunications market, the regulatory measures which most affect PT’s operations, its revenues and its costs, relate to:

- restrictions on the products PT Comunicações offer and the prices it charges in its wireline retail business;
- obligations to allow PT’s competitors to interconnect with and use its wireline network;
- certain wireline services, which PT Comunicações is obliged to provide to the public under its “universal service obligation”;
- measures that are intended to make it easier for PT’s customers to migrate to PT’s competitors’ services, including carrier pre-selection, number portability and unbundling of the local loop, and beginning in 2005, wholesale line rental; and
- the terms of PT’s Concession and its licences, including the third generation mobile licence that TMN received at the end of 2000.

In February 2002, the European Union agreed upon a new regulatory framework for electronic communications networks and services, consisting of five directives governing procedures, authorisations, access, universal service and data protection; one decision on the availability and use of radio spectrum; and a recommendation on relevant product and service markets within the electronic communications sector subject to “ex ante” regulation in accordance with Directive 2002/21/EC of the European Parliament and Council on a common regulatory framework for electronic communications networks and services. Four of the five directives that make up the new EU framework were adopted into law in Portugal on 10 February 2004 as part of Law 5/2004, the Law of Electronic Communications, or “Law 5/2004”. The fifth directive was adopted into law on 18 August 2004. In 2006, the European Commission began a review of the new EU framework, and a new version of the European directives is expected by the end of 2007.

The implementation of the new EU framework is changing the current regulatory framework applicable to PT. The new EU directives and recommendations, which adopt competition law principles such as market dominance for the designation of significant market power and the definitions of relevant product and geographic markets which may be subject to “ex ante” regulation, will result in significant changes and refinements to the current regulatory regime applicable to PT in Portugal.

Under the new regulatory regime, regulatory obligations can be imposed on operators having significant market power in any one of 18 relevant retail and wholesale markets identified by the European Commission. Since PT is active in all of these markets, the new regulatory regime could result in an increase in the regulatory measures affecting PT's businesses and operations. Under the EU framework directive, ANACOM is required to analyze the 18 retail and wholesale markets and identify which electronic communications operators and service providers it considers to have significant market power in such markets in Portugal and notify the European Commission with respect to its findings.

ANACOM has analyzed 16 of the 18 retail and wholesale markets. ANACOM considers the Portugal Telecom group to have significant market power in all the markets it has analyzed except for one in which it did not find any operator to have significant market power (wholesale transit services). These markets include the following: (1) retail markets-access to the public telephone network at a fixed location (residential and business), publicly available local and/or national telephone services provided at a fixed location (residential and business), publicly available international telephone services provided at a fixed location (residential and business), and leased lines; and (2) wholesale markets – call origination on the fixed telephone network provided at a fixed location, call termination on individual public telephone networks provided at a fixed location and wholesale unbundled access to local metallic loops, wholesale leased lines (trunk segments and terminating segments) and wholesale broadband access. ANACOM has notified the European Commission regarding its conclusions about the markets it has already analyzed. In addition, ANACOM added a nineteenth market, covering telephone services at a fixed location using non-geographic numbers, such as toll-free numbers, and has declared the Portugal Telecom group to have significant market power in this area.

In addition to the Portugal Telecom group, all other wireline operators in Portugal were determined to have significant market power in the call termination on individual public telephone networks provided at a fixed location wholesale market. Likewise, all mobile network operators were found to have significant market power in the call termination on individual mobile networks. ANACOM has not yet started the analysis of the two remaining wholesale markets, which are roaming services and access and call origination on mobile telephone networks. Final decisions with respect to the existence of significant market power in access and call origination on the mobile networks market is expected during the course of 2007.

In addition, Law 5/2004 has made more flexible certain other aspects of the former regulatory scheme, such as the basis upon which PT and other operators in Portugal can use public rights-of-way and the rules governing access to ducts.

Regulatory Institutions

ANACOM. ANACOM, created in January 2001 (formerly the Instituto das Comunicações de Portugal, or ICP), is the Portuguese telecommunications regulator. Since it commenced operations in 1989, it has been closely involved in developing the telecommunications regulatory framework in Portugal. It advises the Portuguese government on telecommunications policy and legislation and monitors compliance with concessions, licenses and permits granted to telecommunications providers in Portugal.

ANACOM is accountable to the Ministry of Public Works, Transport and Communications. The Ministry of Public Works, Transport and Communications retains basic responsibility for telecommunications policy in Portugal. Together with the Ministry of Finance, it has ultimate responsibility for monitoring PT's compliance with PT's Concession. It also has certain supervisory powers with respect to PT's activities. The Portuguese government delegated a significant number of those powers and functions to ANACOM in PT's Concession.

Over the past several years, the Portuguese government has substantially increased the autonomy of ANACOM and allowed it to become a more effective and independent regulatory body. ANACOM acts on complaints against PT by PT's competitors, PT's customers and other interested parties. It can impose fines on PT if PT does not meet its obligations under its Concession, including PT's obligations to supply public switched wireline telephone services, leased lines and other services to PT's competitors on a timely basis. ANACOM has, from time to time, addressed complaints

against PT by its competitors. However, such complaints have been resolved in a manner that has not had a material adverse effect on PT's businesses or operations. ANACOM's decisions are subject to possible reconsideration and can be submitted for judicial review.

European Commission. Most of the EU competition rules have the force of law in all EU member states and therefore apply to PT in Portugal. The current priority of the European Commission is to ensure that EU member states fully and correctly implement EU requirements in national law. The European Commission routinely monitors the status of EU member states in implementing EU directives.

The Directorate-General for Competition of the European Commission is responsible for considering, on its own initiative as well as in response to complaints by interested parties, potential claims that PT's business activities or Portuguese government regulations are inconsistent with the key provisions of the Treaty of Amsterdam, also known as the EC Treaty, relating to competition in the EU. Article 81 of the treaty prohibits agreements or coordinated action between competitors that may affect trade between EU member states and have as their objective or effect the prevention, restriction or distortion of competition within the EU. Article 82 of the treaty prohibits any abuse of a market dominating position within the EU, or a substantial part of the EU, that may affect trade between EU member states. The Directorate-General for Competition enforces these rules in cooperation with the national competition authorities. In addition, national courts have jurisdiction over violations of EU competition law. In 2005, Sonaecom filed a complaint with the Directorate-General for Competition of the European Commission relating to PT's activities and the regulatory framework of the Portuguese government. However, the Commission responded that the complaint should be addressed by the Portuguese Autoridade da Concorrência. To PT's knowledge, proceedings before the European Commission relating to this complaint are now closed.

PT understands that at the end of 2001 the Directorate-General for Competition and the Directorate-General for Information Society of the European Commission requested information from the Portuguese government regarding the telecommunications rights-of-way regime in Portugal, which provided PT Comunicações with the exclusive right to use public rights-of-way free of municipalities' fees and taxes. However, the rights-of-way regime was modified in 2004 through Law 5/2004, as described below in “– *Summary of PT's Concession and Existing Licenses*”. Since PT has not been party to the communications between the Directorates-General and the Portuguese government, PT is unable to assess whether or not Law 5/2004 has resolved any concerns the Directorates-General may have had regarding the regulation of rights-of-way in Portugal. PT further understands that the Directorate General for Information Society of the European Commission requested information from the Portuguese government regarding the designation of the universal service provider (currently, PT Comunicações) and regarding the Portuguese government's intention to launch a transparent procedure in order to appoint the universal service provider.

In April 2006, the European Commission sent to the Portuguese government a formal request to abandon the special rights the Portuguese government holds as the sole owner of PT's A shares. The European Commission believes that the special powers granted to the Portuguese government through the sole ownership of PT's A shares act as a disincentive for investment by other EU member states in a manner that violates European Community Treaty rules. Should the Portuguese authorities not take satisfactory steps to remedy the alleged infringement of EU law, the European Commission may decide to refer the case to the European Court of Justice.

Autoridade da Concorrência. PT's activities are also overseen by Autoridade da Concorrência (formerly Direcção Geral do Comércio e da Concorrência, or DGCC), which is responsible for enforcement of Portuguese competition law. It is also responsible for considering complaints relating to PT's business practices or other business arrangements. PT expects the Autoridade da Concorrência to take a more active role in matters related to pricing, the determination of which companies have “dominant position” and the regulatory implications for such companies.

On 10 and 11 February 2004, the Autoridade da Concorrência conducted an unannounced search of the offices of PT Comunicações and PT Prime, seizing several documents, in order to investigate alleged abusive practices, including predatory pricing, price discrimination at the wholesale level, price discrimination at the retail level in the wireline telephone market and margin squeezes. The potential penalty for such practices could be as high as 10 per cent. of PT's turnover in the

preceding fiscal year. This administrative investigation is still in a preliminary stage involving document collection and review. The Autoridade da Concorrência periodically requests that PT provides it with additional information regarding the documents they seized in February 2004, which PT has responded to in a timely manner. PT expects that the next phase could involve the Autoridade da Concorrência formally charging PT with the alleged abusive practices, which would result in an administrative proceeding, referred to as a “statement of objections”, in which PT would defend its position before the competition authority. If PT is unsuccessful in its defense, the competition authority could issue a fine in connection with such abuses. PT is permitted under Portuguese law to appeal any adverse decision of the Autoridade da Concorrência to the Commerce Court. To PT’s knowledge, the Autoridade da Concorrência has not yet reached any decision on this matter. However, in March 2004, PT appealed to the Courts regarding the seizing of the documents by Autoridade da Concorrência, and in July 2007 the Courts confirmed that Autoridade da Concorrência is obliged to immediately return all the documents illegally seized and ruled that the potential proof obtained by those documents is null.

To PT’s knowledge, there are also several other complaints related to PT’s activities pending before the Autoridade da Concorrência, including complaints against: (i) PT.com (this complaint was formerly against Telepac, which merged with PT.com in December 2004) and TV Cabo regarding alleged anti-competitive practices in the broadband Internet market; (ii) TV Cabo and Sport TV by TV TEL, a cable TV company operating in the Oporto area, for alleged refusal to supply advertising space; and (iii) PT Comunicações for alleged anti-competitive practices in the public wireline telephone market and for granting discriminatory discounts on leased lines.

In addition, in 2004, the Autoridade da Concorrência initiated a proceeding against PT Comunicações, referred to as a “statement of objections”, alleging that PT Comunicações was denying access to the ducts in which the basic telecommunications network is installed. In June 2005, the Autoridade da Concorrência issued a revised “statement of objections” on this matter. PT Comunicações has responded to those “statement of objections” and does not believe it has violated applicable law and regulations. However, on the 1st of August 2007, Autoridade da Concorrência imposed a fine of 38 million euros on PT Comunicações. PT Comunicações will appeal to the Court (Tribunal do Comercio) by the 30th of August 2007. The appeal will suspend the decision of Autoridade da Concorrência.

In April 2007, Autoridade da Concorrência, also accused PT Comunicações of alleged abuse of dominant position for granting discriminatory discounts on lease lines. In response to this accusation PT Comunicações contested the allegations made by Autoridade da Concorrência. PT Comunicações is permitted under Portuguese law to appeal any adverse decision of the Autoridade da Concorrência to the courts. The appeal will suspend the decision of Autoridade da Concorrência.

PT Multimédia and TV Cabo have also been accused, in September 2005, of an allegedly forbidden practice under article 4 of Law 18/2003 (Portuguese Competition Law), following the execution, on 27 March 2000, of a “Partnership Agreement” between PTM, TV Cabo and SIC-Sociedade Independente de Comunicação, SA (SIC), under the framework of the acquisition, submitted for prior notification, by SIC of Lisboa TV - Informação e Multimédia, SA. In response to this accusation, PTM and TV Cabo contested the allegations by Autoridade da Concorrência. In August 2006, Autoridade da Concorrência imposed a fine of 2.5 million euros on PT Multimédia. PT Multimédia and TV Cabo appealed to the Commerce Court of Lisbon on 8 September 2006, and consequently the decision of Autoridade da Concorrência was suspended. On 14 August 2007, PTM was notified of the Commerce Court’s decision pursuant to the appeal procedure. According to such decision, the Commerce Court declared the decision of the Autoridade da Concorrência null and void and, accordingly, declared that the Autoridade da Concorrência should commence new proceedings solely.

Pricing of Wireline Services

ANACOM established a new pricing regime for wireline services on 14 December 2004 in accordance with the terms of the new EU regulatory framework. This pricing regime created the following regulatory obligations for the retail market for telephone services at a fixed location:

- In 2005, the price-cap applying to residential access and domestic calls is CPI minus 2.75 per cent. (new prices for 2005 within this price cap became effective as of 1 July 2005);
- The fixed component of fixed-to-mobile calls (residential and non-residential) is required to be in line with the cost orientation principle;
- The tariffs of domestic payphone calls are required to correspond to a maximum of three times the tariff of a residential phone call; and
- PT was released from its obligations under the low user scheme, as well as certain discount schemes for retired people, except for the monthly fee discount for retired people, which was financed by the Portuguese government until December 2006.

In 2006, PT's wireline business, PT Comunicações, submitted to the regulator a new pricing scheme that included a flat-rate plan with unlimited off-peak calls on weekdays.

In addition, general regulatory obligations of transparency, non-discrimination, cost orientation, cost accounting and account separation apply to access to the fixed line network and to the telephone services at a fixed location.

Interconnection Prices. Law 5/2004 establishes the new access and interconnection regime in Portugal in accordance with the requirements of the new EU regulatory framework. During 2006, PT Comunicações published its reference interconnection offer for the provision of interconnection at a flat rate. See also “– *Interconnection*” below.

Prices for Leased Lines. Prices for PT's leased lines are subject to price controls as a result of obligations imposed by ANACOM, based on its finding that PT has significant market power in retail leased lines, wholesale termination and trunk segments. PT's leased line prices must be cost-oriented and follow the retail minus rule (which provides for a 26 per cent. minimum margin between PT's wholesale and retail leased line prices).

Universal Service Obligations

Law 5/2004 and the Concession impose universal service obligations on PT in Portugal. These obligations include providing connection to the public telephone network at a wireline location. They also include providing access to public switched wireline telephone services, including enabling users to make and receive local, national and international telephone calls, facsimile communications and data communications. They also include providing public pay telephones, publishing directories and making available at least one telephone directory enquiry service covering all public voice telephone subscribers' numbers.

According to Law 5/2004, if ANACOM determines that the provision of universal service obligations has become an excessive burden, it may compensate PT accordingly. PT Comunicações has submitted to ANACOM the annual universal service costs (from 1996 to 2003) in order to obtain compensation. Since 2004, it has been the responsibility of ANACOM to calculate the costs of providing the universal service. PT believes that obtaining significant compensation under this provision of the law will be very difficult and may not be possible.

Interconnection

The Interconnection Framework. The EU Access and Interconnection Directive requires that interconnection services be made available in a non-discriminatory manner. The EU Access and Interconnection Directive encourages commercial negotiations among operators but requires national regulatory authorities to establish mechanisms for effective dispute resolution. According to the EU Access and Interconnection Directive, all telecommunications companies with significant market power in the call origination or termination markets must:

- make interconnection access to their networks available to other network operators;
- not discriminate between interconnection customers;
- provide to those requesting interconnection the information and technical specifications necessary for them to interconnect their networks;
- offer interconnection prices that are transparent and cost-oriented and do not discriminate between interconnection customers; and

- maintain a separate accounting system for interconnection activities.

Law 5/2004 implemented the EU Access and Interconnection Directive in Portugal and established the general conditions for access and interconnection among telecommunications operators in competitive markets. It guarantees the rights of new entrants to obtain interconnection from telecommunications operators with significant market power.

Pursuant to Law 5/2004, ANACOM is entitled to review and modify PT's proposed interconnection rates and arrangements in PT's reference interconnection offer. ANACOM has established in Portugal an overall interconnection framework based on cost and consistent with the EU legal framework for both wireline and mobile services.

Wireline Interconnection. As a result of the enactment of Law 5/2004, ANACOM adopted a measure in March 2004 on call origination on fixed telephone networks provided at a fixed location and call termination on individual public telephone networks provided at a fixed location and on significant market power designation in these fixed locations, declaring the Portugal Telecom group to have significant market power in these markets. As a result, PT is subject to price controls in these markets based on PT's costs and other factors and must publish a reference offer that includes these prices and quality of service standards.

Mobile Interconnection. In February 2005, all mobile operators were declared to have significant market power in call termination in mobile networks market. ANACOM has accordingly imposed price controls on interconnection rates for the termination of calls on mobile networks. In 2005, interconnection rates (both fixed-to-mobile and mobile-to-mobile) were reduced by an average of 23.5 per cent. compared with 2004 rates. In 2006, these rates were reduced by an average of 18.5 per cent. compared to the 2005 rates. These reductions have had, and are expected to continue to have, a significant impact on TMN's interconnection revenues and consequently its earnings.

ANACOM is in the process of analyzing call origination on the mobile networks market in order to determine who has significant market power in such market. A decision is expected in 2007.

Internet Access. The interconnection regime for access to PT's network by ISPs provides for a number of different billing structures. Under the first method, ISPs pay PT a call origination charge, and, if the ISPs request that PT invoices customers on their behalf, they also pay PT the corresponding charge for the invoicing service. Under a second method, PT charges the ISPs a wholesale flat rate and the ISPs bill their own customers. On 23 September 2003, ANACOM decided that data traffic and Internet traffic should be included in PT's Reference Interconnection Offer, which previously applied only to interconnection for voice telephony services. Accordingly, PT now offers two access regimes to ISPs: (1) the Reference Offer for Internet Access, which includes the two pricing methods described above, and (2) the Reference Interconnection Offer, which includes a pricing method based on call origination. On 16 March 2004, ANACOM issued a new administrative decision regarding the billing structure for PT's Reference Interconnection Offer. As a result, the call origination pricing arrangements with ISPs now include two billing structures. The primary differences between the two billing structures relate to origination prices, the manner in which ISP infrastructures are connected to PT's wireline network and billing arrangements. The regime introduced in March 2004 has lower origination charges, involves the use of leased lines and does not require PT to maintain billing arrangements with ISPs. The ISPs determine which billing regime will apply to their arrangements to connect with PT's wireline network.

Number Portability and Carrier Selection

An amendment in September 1998 to the EU Interconnection Directive required member states to introduce number portability among telecommunications operators in most EU countries by 1 January 2000. Where implemented, number portability allows a subscriber at a specific location to change service providers without having to change telephone numbers. PT Comunicações introduced number portability for wireline services on 1 July 2001. Number portability for mobile services was introduced in January 2002.

ANACOM has required call-by-call carrier selection to be offered by PT for long distance and international calls since 1 January 2000. PT has been offering it for local and regional calls since 1st

January, 2001 and for fixed-to-mobile calls since 1 October 2000. Call-by-call carrier selection enables customers to select the carrier of their calls by dialing a code connecting them to the selected carrier.

Law 5/2004 requires that all wireline network operators with significant market power must offer carrier pre-selection. Carrier pre-selection allows customers to select the carrier that will be their default carrier. They then do not need to dial any code to connect to their selected carrier when they make their calls. ANACOM introduced interim carrier pre-selection using auto dialers on 1 July 2000 and full carrier pre-selection has been available throughout Portugal since 15 October 2000.

Number portability regulations were revised in 2005 through Regulation 58/2005 of 18 August 2005, but the revisions did not have a significant impact on PT's business. New regulations for carrier pre-selection were also published in early 2006, extending carrier pre-selection to non-geographic services.

Unbundling of the Local Loop

On 18 December 2000, the European Commission approved a regulation requiring wireline network operators to make the local loop between their customers and the local switches on their networks available to competitors. Such a requirement also exists in Law 5/2004. This allows such competitors to connect their networks to the copper "local loop" and use it to provide their services directly to those customers without having to rely upon the network operator's relationship with the customers. According to the regulation and Law 5/2004, PT is required to maintain a reference offer for unbundled access to its local loops and related facilities and to meet reasonable requests for unbundled access to its local loops and related facilities under transparent, fair and non-discriminatory conditions. Prices charged must be cost-oriented. ANACOM has announced that unbundling of the local loop should be available in Portugal in accordance with the terms of the EC regulation and Law 5/2004. PT's PT Comunicações wholesale unit regularly published updated versions of the reference offer for unbundled access to PT's local loops in accordance with terms established by ANACOM.

PT has made available to its competitors all of the local switches for remote and physical co-location where technical and space conditions are available. Co-location means providing space and technical facilities to competitors to the extent necessary to reasonably accommodate and connect the relevant equipment of the competitor.

Other Requirements

The regulatory framework requires PT Comunicações to submit periodic reports on quality of service and comply with specified indicators. Penalties may occur if PT do not achieve such indicators. PT must also provide white page directories and certain other facilities to certain specified categories of subscribers free of charge. In addition, a new Regulation of Quality of Service for voice services at fixed locations was published in June 2005 (Regulamento 46/05).

Internet and Related Services

Various regulatory developments may affect PT's Internet business. Portugal has adopted Decree Law 290-D/99 regarding digital signatures, which established a legal framework for electronic documents and digital signatures. This framework is a key component for developing e-commerce business. Portugal is expected to enact further measures pursuant to the EU Electronic Signature Directive, adopted in December 1999. The EU Electronic Commerce Directive, which was implemented in January 2002, further promotes the free movement of electronically provided services and commerce within the EU. For example, it requires EU member states to absolve information carriers and host-services providers from liability for the content of information transmitted over the Internet. Such provisions provide PT with legal protection that is important in carrying out PT's business. The 1995 EU Data Protection Directive, which was implemented in Portugal in 1998, places restrictions on the use by Internet companies of personal data stored on their networks. A new Data Protection Directive was adopted by the European Commission in 2006, imposing data-retention obligations on operators. It is not possible at this time to ascertain the burden that data protection schemes or other self-regulation and content monitoring requirements may impose on PT's Internet business.

EU Competition Directive

The European Commission issued a directive on 16 September 2002 (Directive 2002/77/EC) that requires member states to enact legislation directing incumbent telecommunications operators to separate their cable television and telecommunications network operations into distinct legal entities. PT believes that steps already taken to operate its cable television business in Portugal through PT Multimédia, a separate legal entity that has independent shareholders, satisfy the requirements of the directive implemented in Portugal. In addition, PT believes that the proposed spin-off of its interest in PT Multimédia will address the long-standing objections of the Portuguese regulators in this regard.

Licensing Framework

The EU Authorisation Directive (Directive 2002/20/EC of 7th March, 2002) prohibits any limitation on the number of new entrants in telecommunications markets, except as required to ensure an efficient use of radio frequencies.

Pursuant to this Directive, which is part of the EU electronic communications framework, Law 5/2004 has established a new authorisation regime, whereby an operator must have a general authorisation for the provision of electronic communications networks or services. A license can be required for the use of radio frequencies or numbering resources. ANACOM is responsible for issuing regulations to implement this authorisation regime.

Summary of PT's Concession and Existing Licenses

PT's Concession is for the provision of universal service and for the operation of the terrestrial broadcasting network in Portugal, and it permits PT to provide public switched wireline telephone, packet switched data (the rights to which were transferred to PT's subsidiary PT Prime) in X.25 mode, leased lines and telex and telegraphy services in Portugal. PT also provides mobile telephone services, cable television and data communications services under licenses granted to PT's subsidiaries by the Portuguese government. The subsidiaries holding the licenses are subject to separate financial reporting and other requirements.

PT Comunicações Wireline Concession

The Portuguese government granted Portugal Telecom a Concession on 20 March 1995. The Concession had an initial term of 30 years, expiring in 2025. As part of the reorganisation of PT's business, it transferred the Concession to PT Comunicações. The Council of Ministers approved this transfer in a Decree Law that came into effect upon publication in the Portuguese Official Journal on 9 September 2000.

The Concession granted PT the right to install, manage and operate the infrastructure that forms part of the basic telecommunications network and the terrestrial broadcasting network for a fee of up to 1 per cent. of its operating revenues from the services provided under the Concession, after certain deductions. Some of PT's assets that are part of the basic telecommunications network (as defined in Portuguese legislation) were treated as being within the "public domain" under the terms of the Concession. During the term of the Concession, PT was permitted to receive economic benefits from the use of public domain assets as if it owned them completely. However, such public domain assets would have reverted to the Portuguese government without compensation when the Concession expired.

On 11 December 2002, PT agreed to prepay the future rental payments due under the Concession in exchange for full ownership of the basic telecommunications network and to ensure that there will be no reversion of the assets related to the provision of Concession services to the government in 2025. On 27 December 2002, PT acquired full ownership of the basic telecommunications network for €365 million, which included the 2002 Concession fee in the amount of €16.6 million. As a result of this acquisition, the terms of the Concession have been modified so that PT Comunicações no longer is obligated to pay a Concession fee to the Portuguese government and ownership of the network and assets related to the Concession will not revert back to the Portuguese government in 2025. On 17 February 2003, Decree Law 31/2003 was enacted, establishing the basic regulatory principles supporting the terms of PT's modified Concession. On 3 April 2003, PT entered into an agreement formally modifying the terms of its Concession with the Portuguese government.

The Portuguese government retains the ability to suspend or terminate PT's rights under the Concession. In cases of serious non-performance by PT of its obligations under the Concession, the Portuguese government may, on a provisional basis, take over the development and operation of services authorized under the Concession. The Concession may also be terminated in cases of "severe, continual or unremedied" failure to perform PT's obligations. PT believes that it has the resources to fulfill all its obligations under the Concession.

In addition, after 2010 the Portuguese government may revoke the Concession upon at least one year's notice if it deems such action to be justified in the public interest. In that event, PT would be entitled to compensation equaling its annual average net profits for the five years prior to notification of revocation multiplied by the number of years remaining before the Concession expires.

PT's modified Concession provides that PT is exempt from all taxes, fees and charges with respect to the usage of public rights-of-way for PT's telecommunications infrastructure. However, Law 5/2004 establishes a new rights-of-way regime in Portugal whereby each municipality may establish a fee, up to a maximum of 0.25 per cent. of each wireline services bill, to be paid by the customers of those wireline operators whose network infrastructures are located in each such municipality. This regime was implemented in 2005 pursuant to Regulation No. 38/2004, which was published in September 2004. The new regime replaces Law 91/97, which granted PT an exemption from municipal taxes and rights-of-way and other fees with respect to access to and installation and use of PT's telecommunications network in connection with PT's obligations under the Concession. PT's exemption from municipal taxes prior to the enactment of Law 91/97 is still being challenged in the Portuguese courts by the Municipality of Oporto.

PT is required to provide special telephone prices to certain eligible retired and pensioner Portuguese citizens. Until 31 December 2006, the costs of providing these special prices were directly reimbursed by the Portuguese government. In May 2007, ANACOM has determined that PT Comunicações should bear the costs of providing said special prices, as part of its universal obligations. In addition, PT offers supplementary discounts to certain retired and pensioner Portuguese citizens without reimbursement from the Portuguese government. The cost of these discounts for PT's wireline business was approximately €7.8 million in 2005 and €6.4 million in 2006.

The Concession imposes a universal service obligation on PT. See "*– Universal Service Obligations*", above.

The Ministry of Finance is responsible for monitoring financial issues with respect to the Concession. The Ministry of Economy is responsible for all other issues under the Concession. ANACOM is authorized to monitor and assess penalties up to a maximum of €5,000,000 if PT fails to fulfill its obligations under the Concession or other obligations imposed by law. Disputes concerning the application and interpretation of the Concession are dealt with by arbitration.

PT Prime's Data Licences and Registrations

PT Prime holds:

- a non-exclusive licence to provide wireline services;
- a non-exclusive licence to be a "Public Telecommunications Networks" operator; and
- due to PT's reorganisation all the former Telepac licences, including a data communications licence.

PT's data communications license authorizes PT to provide X.25/X.32 synchronous services and X.28 asynchronous services and other switched and non-switched data communications services, including frame relay and virtual private networks for data communications. The license also authorizes PT to provide value-added services such as electronic data interchange and videotext services. In addition, the license authorizes PT to construct certain network infrastructures in connection with licensed services. With respect to packet switched data, the data communications license is valid for 30 years, unless PT's wireline Concession is terminated earlier. Licenses have also been granted to other providers of data communications and Internet access services, including companies associated with major international telecommunications providers. However, under Law 5/2004, and in accordance with the EU licensing regime, companies are not required to have a license

to provide data communications services and Internet access. Instead, it is sufficient to register their intended services with ANACOM under its service registration scheme.

In April 1997, ANACOM granted PT Prime a license to provide data communications services using satellite infrastructure.

In April 1997, ANACOM also granted PT Prime a license to offer voice services to corporate networks and other closed groups of users.

TMN's Mobile Service Licence

Mobile telephone service licenses are valid for 15 years and are issued by ANACOM under Law No. 5/2004 (which revoked Decree Law 381-A/97). These licenses authorize the use of radio spectrum and the installation of base stations, base station controllers and control switching centers and require the licensee to construct networks capable of reaching at least 75 per cent. of Portugal's population within a specified period of time. Charges for the provision of mobile telephone services are not subject to regulation.

Through TMN, PT holds a renewable, non-exclusive license to provide traditional and GSM digital mobile telephone services throughout Portugal. The authorization for the use of GSM radio spectrum was renewed in December 2006 and is now valid until 2021. Two other operators hold licenses to provide GSM digital mobile telephone services on substantially the same terms as those applicable to TMN. Vodafone Portugal was awarded its license in 1991. Optimus was awarded a license in 1997 and began operations in September 1998.

PT is required to comply with a number of mobile telephone service criteria. These include satisfying minimum quality standards regarding blocked call rates, network effectiveness and servicing time, and providing certain services. PT is also required to provide ANACOM with information about its mobile telephone operations, including the number of customers, number and average duration of calls on a quarterly basis. PT is also required to provide annual information to ANACOM about the development of infrastructure.

In 2000, ANACOM conducted a tender for four licenses for universal mobile telecommunications services, known as UMTS. UMTS services are the European version of the globally accepted technical standards for "third generation" mobile communications. UMTS constitutes a significant advance over the "second generation" digital GSM mobile services currently provided. The "first generation" services were traditional analog mobile services. The broadband capacity of the frequency spectrum to be allocated under the UMTS licenses enables operators to supply video and Internet content to mobile handsets at higher transmission speeds.

The UMTS licenses were issued by ANACOM at the end of 2000. The licenses cover all of Portugal and are valid for 15 years. The license fee was €100 million per license. TMN and the other two main mobile operators in Portugal were each awarded one of these licenses at the end of 2000, and TMN's license expires in January 2016. In addition, TMN and the other mobile operators have committed to making contributions to the Portuguese information society. One of the licenses was also awarded to Oniway, a new entrant in the Portuguese mobile market. However, Oniway decided not to participate in the provision of third generation mobile services, and TMN, Vodafone and Optimus requested that the Oniway license be transferred to them, dividing the cost and the resulting spectrum. This request was granted by a special ministerial order in January 2003.

In April 2004, TMN launched UMTS in Portugal with an emphasis on new services, such as video telephony and high-speed data. In 2004 and 2005, PT pursued a strategy of gradual improvements to network coverage, using existing GSM sites where possible in order to minimize the need to install costly new sites.

UMTS License holders are required to offer their services to:

- at least 50.7 per cent. of the Portuguese population by the end of the first year;
- 65.7 per cent. by the end of the third year; and
- 77.3 per cent. by the end of the fifth year.

TV Cabo's Cable Television Authorisations

Under the new regulatory framework set out in Law No. 5/2004, of 10 February 2004, the provision of cable television networks and services is subject only to a general authorisation regime, which depends on the compliance with the rules provided for in the law and regulations. That is, the new framework does not require specific authorisations or licenses from ANACOM.

Currently, TV Cabo and its subsidiaries Cabo TV Açoreana and Cabo TV Madeirense, hold nine cable television authorisations to provide cable television services in 125 counties in continental Portugal and the Madeira and Azores Islands. All of these authorisations expire in May 2009 and will not be renewed, allowing the new regulatory framework to take effect. Currently, certain other operators are also authorized to provide cable television services in Portugal. See “– *Competition – Competition Facing PT Multimédia's Pay TV and Broadband Internet Business*”. All these authorisations permit the construction of cable distribution centers and networks. They also contain quality of service standards and, in most cases, obligations to construct networks capable of reaching 80 per cent. of the population of the authorized area. The charges for the provision of cable television services are not subject to regulation.

Under Portuguese law, advertising on TV Cabo's channels is generally restricted on the same terms as on broadcast TV. These restrictions include a ban on alcohol advertisements before 10 p.m. and a complete ban on tobacco advertisements. Advertising on premium channels cannot take up more than 10 per cent. of each period of two hours (i.e. 12 minutes every two hours), and advertising on basic channels cannot take up more than 20 per cent. of each period of two hours (i.e. 24 minutes every two hours).

Portuguese law currently permits television operators to produce and broadcast their own television programming if they have national coverage. In addition, Portuguese legislation permits the use of two-way signaling capability over cable television networks. The ability to transmit and receive signals allows the introduction of pay-per-view, home shopping and similar products in Portugal.

Regulation – Brazil

General. Vivo's mobile business, the services it provides and the prices it charges are subject to regulation under the General Telecommunications Law and various administrative enactments, which regulate the services provided by Brazilian telecommunications operators.

ANATEL is the agency that regulates telecommunications under the General Telecommunications Law and the July 2001 Regulamento da Agência Nacional de Telecomunicações, known as the ANATEL Decree. ANATEL is financially autonomous, and administratively independent of the federal government. ANATEL maintains a close relationship with the Ministry of Communications. Any regulation proposed by ANATEL is subject to a period of public comment, which may include public hearings. ANATEL's actions may be challenged in the Brazilian courts under Brazilian administrative law. On 25 November 1998, ANATEL enacted “Resolution 73 – Regulation of Telecommunication Services” which regulates in detail the new comprehensive framework for the provision of telecommunications services in Brazil established by the General Telecommunications Law.

Concessions and Authorisations. Prior to January 2000, ANATEL had only authorized two mobile service providers in each of the ten franchise areas under bands A and B. Band A and band B mobile service providers, including Vivo's operating subsidiaries, were granted concessions pursuant to the *Lei Mínima*, or the Minimum Law. Each concession is a specific grant of authority to supply cellular telecommunications services, subject to certain requirements contained in the applicable list of obligations appended to each concession. If a mobile service provider wishes to offer any telecommunications service other than those authorized by its concession, it may apply to ANATEL for an authorisation to offer such other services.

In accordance with the General Telecommunications Law, a concession relates to the provision of telecommunications services under the public regime, as determined by the public administration. A concession may only be granted upon a prior auction bidding process. As a result, regulatory provisions are inserted in the relevant concession agreements and the concessionaire is subject to public service principles of continuity, changeability and equal treatment of customers. The

government authority is also entitled to direct and control the performance of the services, to apply penalties and to declare the expiration of the concession and the return of assets of the concessionaire to the government authority upon termination of the concession. Another distinctive feature is the right of the concessionaire to maintain an economic and financial balance of the concession agreement. The concession is granted for a limited duration and is generally renewable once.

An authorisation is a permission granted by the public administration under the private regime, which may or may not be granted upon a prior auction bidding process, to the extent that the authorized party complies with the objective and subjective conditions deemed necessary for the exploitation of the relevant type of telecommunications service in the private regime. The authorisation is granted for an indeterminate period of time. Under an authorisation, the government will not guarantee an economic and financial balance, as guaranteed under a concession.

SMP Regulation. In November 2000, ANATEL adopted certain regulations for the issuance of new licenses to provide wireless communications services through SMP rules to compete with the then existing cellular operators in the various regions of Brazil. These regulations divided Brazil into three main regions covering the same geographic area as the concessions for the fixed-line telecommunications services. ANATEL organized auctions for three new licenses for each of those regions. The new licenses provided that the new services would be operated in the 1800 MHz radio frequency bands, and they were denominated band C, band D and band E. These new licenses were auctioned by ANATEL and awarded during the first quarter of 2001, at the end of 2002, in September 2004 and in March 2006. In July 2006, the Bill & Keep regime was discontinued. The current rule is “full billing”, pursuant to which the SMP operator pays the entire call termination fee of the other mobile network. The partial “Bill and Keep” rule is still used between the SMP and SME (trunking) networks.

Under these new licenses:

- services are to be provided using the 1,800 MHz frequency;
- each operator may optionally provide domestic and international long-distance services in its licensed area;
- existing cellular service providers, as long as they do not have partnerships with fixed-line operators, as well as new entrants into the Brazilian telecommunications market, can bid for band C, band D and band E licenses. However, fixed-line operators, their controlling shareholders and affiliated cellular providers can only bid for band D and band E licenses;
- a cellular operator, or its respective controlling shareholders, may not have geographical overlap between licenses; and
- current band A and band B cellular service providers can apply for an extra frequency range.

Pursuant to the SMP services regulation, each of the three main regions is divided into registration areas, or tariff areas.

Vivo’s operating subsidiaries all held concessions prior to the introduction of the SMP regime. Subsequent to its introduction, they have migrated to the new SMP regime, and their concessions have been converted into licenses to use the radio frequency spectrum in their respective bands and provide services in the regions in which they operate. See “– *Brazilian Mobile Business*”. In order to migrate services to the SMP regime, Vivo’s operating subsidiaries were required to comply with several technical and operational conditions, including, among others, the adoption of a carrier selection code for long distance calls originating from their networks.

Each SMP license consists of two licenses – one to provide mobile telecommunications services, and another to use the frequency spectrum for a period of 15 years. The frequency license is renewable for a second 15-year period upon the payment of an additional license fee.

According to the General Telecommunications Law and Decree No. 2056/96, control of a concession can only be transferred after five years from the date of privatization in the case of band A concessions, or the commencement of services in the case of band B concessions. On the other hand, under the SMP system, a licensee can be transferred through merger or incorporation of the relevant mobile service provider, whether they are providing services under the band A or band B.

Interconnection. Under the General Telecommunications Law, telecommunications service providers are classified as providers of either collective or restricted services. All mobile operators, including SMP service providers, are classified by ANATEL as collective service providers. All providers of collective services are required to provide interconnection upon request to any other collective service providers. The terms and conditions of the interconnection agreements are freely negotiated between parties, subject to price caps and other rules established by ANATEL. Providers must enter into interconnection agreements, regarding, among other things, tariffs, commercial conditions and technical issues, with all requesting parties on a non-discriminatory basis. If the parties cannot agree on the terms and conditions of interconnection, ANATEL may determine the terms and conditions by arbitration. Interconnection agreements must be approved by ANATEL and may be rejected if they are contrary to the principles of free competition and the applicable regulations.

In 2005, ANATEL further standardized interconnection regulations to facilitate negotiation of interconnection agreements between wireline operators and mobile operators, referred to as the Sistema de Telefonia Fixa Comutada (*Fixed Telephony Interconnection System, or STFC*).

Obligations of Telecommunications Companies. As telecommunications service providers, the companies operating under the Vivo brand are subject to regulations concerning quality of service and network expansion, as established in their SMP licenses and their original concession agreements.

Any breach by the companies of telecommunications legislation or of any obligation set forth in their authorizations may result in a fine of up to R\$50 million.

Vivo's SMP licenses impose obligations to meet quality of service standards, such as the system's ability to make and receive calls, call failure rates, the network's capacity to handle peak periods, failed interconnection of calls and customer complaints. ANATEL published the method for assessing these quality service standards on 23 April 2003 (ANATEL Resolution No. 335/03).

Rate Regulation. SMP licenses continue to provide for a price-cap mechanism to set and adjust rates on an annual basis. The cap is a maximum weighted average price for a package of services. The package consists of the services in Vivo's Basic Plan, including activation fees, monthly subscription fees, and certain roaming charges, which are charged for the use of mobile services under the SMP regime. The price cap is revised annually to reflect the rate of inflation as measured by the IGP-DI. However, mobile operators are able to freely set the rates for alternative service plans.

The initial price cap agreed to by ANATEL and Vivo's operating subsidiaries in their SMP licenses was based on the previously existing or bidding prices, and was adjusted annually on the basis of a formula contained in their licenses. The price cap has been revised to reflect the rate of inflation as measured by the IGP-DI.

Internet and Related Services. In Brazil, Internet service providers, or ISPs, are deemed to be suppliers of value added services and are not considered telecommunications service providers. ANATEL's Resolution 190 requires cable operators to act as carriers of third party Internet service providers. The Brazilian House of Representatives is considering a law that would penalize Internet service providers for knowingly providing services that allow illegal goods or services to be sold on the Internet and would impose confidentiality requirements on Internet service providers regarding nonpublic information transmitted or stored on their networks. This would affect Vivo indirectly because mobile phones are used extensively for Internet traffic.

Competition Issues. ANATEL is required to consult with the Brazilian competition authority, Conselho Administrativo de Direito Econômico, or CADE, in carrying out certain of its responsibilities, including those related to the review of acquisitions and joint venture agreements entered into by telecommunications operators. In turn, CADE does not exercise its responsibilities without initially seeking the views of ANATEL and would not intervene with respect to any proposed acquisition or agreement affecting competition in the telecommunications sector without first seeking the views of ANATEL. Telecommunications operators must concurrently seek review from ANATEL and CADE of acquisitions and joint venture agreements.

The European Union

Portugal is a member state of the EU and, as such, is required to enact legislation, regulations, directives and decisions from the European Commission and other EU bodies into Portuguese domestic law.

Management

The names of current members of Portugal Telecom's Board of Directors, their principal past affiliations and certain other information are set forth below.

The following directors are members of the Executive Committee:

Henrique Manuel Fusco Granadeiro. First elected 2003. Term expires 31 December 2008. Aged 63. Chief Executive Officer and Chairman of the Board of Directors of Portugal Telecom, SGPS S.A. since April 2006; Chairman of the Board of Directors of PT Centro Corporativo S.A., since March 2006; Chairman of the Board of Directors of PT Portugal, SGPS S.A., since March 2006; Chairman of the Board of Directors of PT Rede Fixa, SGPS S.A., since April 2006; Member of the Strategic Council of Banco Finantia since 2001; Member of the Board of Directors of PT Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A. since 2001; Member of the Board of Directors of Fundação Eugénio de Almeida since 1992; Chief Executive Officer of Lusomundo Media, SGPS S.A. from 2002 until 2004; Chief Executive Officer of Diário de Notícias from 2002 until 2004; Chief Executive Officer of Jornal de Notícias from 2002 until 2004; Chief Executive Officer of TSF from 2002 until 2004; Chief Executive Officer of Jornal do Fundão from 2002 until 2004; Chief Executive Officer of Açoreana Ocidental from 2002 until 2004; Chief Executive Officer of DN da Madeira from 2002 until 2004; Chairman of the Board of Directors of Aleluia – Cerâmica Comércio e Indústria S.A. from 2001 until 2004; Member of the Board of Directors of Parfil SGPS S.A. from 2001 until 2004; Chairman of the Board of Directors of Margrimar Mármore e Granitos S.A. from 1999 until 2005; Chairman of Marmetal – Mármore e Materiais de Construção S.A. from 1999 until 2005; Member of the Board of Directors of Controljornal SGPS S.A. from 1990 until 2001; Member of the Board of Directors of Sojornal – Sociedade Jomalística e Editorial S.A. from 1990 until 2001; Member of the Board of Directors of Marcepor – Mármore e Cerâmicas de Portugal S.A. during 1990; Chairman of Fundação Eugénio de Almeida from 1989 until 1992; President of IFADAP – Instituto Financeiro de Apoio ao Desenvolvimento da Agricultura e Pescas from 1987 until 1990; Delegate Chairman of Fundação Eugénio de Andrade from 1981 until 1987; Member of the Board of Directors of M.N. Tiago, Construções S.A. during 1981; Member of the Board of Directors of Standart Electrica during 1981; Ambassador of Portugal near O.C.D.E.; and Chief of the Civil House of the President of Portugal from 1976 until 1979.

Zeinal Abedin Mahomed Bava. First elected 2000. Term expires December 31 2008. Age 41. Vice President of the Executive Committee of Portugal Telecom, SGPS S.A. since April 2006; Chairman of the Board of Directors of TV Cabo Portugal, S.A. since March 2004; Chief Executive Officer of PT Multimédia – Serviços de Telecomunicações e Multimedia, SGPS S.A. since May 2003; Member of the Board of Directors of PT Centro Corporativo S.A., since March 2006; Member of the Board of Directors of PT Portugal, SGPS S.A. since March 2006; Member of the Board of Directors of PT Rede Fixa, SGPS S.A. since March 2006; Chief Executive Officer of TMN – Telecomunicações Móveis Nacionais, S.A. since December 2005, Chairman of the Board of Directors of Previsão – Sociedade Gestora de Fundos de Pensões, S.A. since March 2003; Chairman of the Board of Directors of PT PRO Serviços de Gestão S.A. since February 2003; Member of the Board of Directors of Brasilcel, N.V. since December 2002; Vice-Chairman of the Board of Directors of PT Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A. since November 2002; Executive Vice-Chairman of the Board of Directors of PT Comunicações, S.A. from January 2004 until December 2005; Member of the Board of Directors of PT Corporate – Soluções Empresariais de Telecomunicações e Sistemas S.A. from June 2003 until 2006; Member of the Board of Directors of PT Compras – Serviços de Consultoria e Negociação S.A. from May 2003 until 2005; Member of the Board of Directors of Fundação Portugal Telecom from March 2003 until December 2004; Member of the Board of Directors of Portugal Telecom Brasil, S.A. from July 2002 until March 2004; Member of the Board of Directors of BEST – Banco Electrónico de Serviço Total, S.A. from May 2001 until October 2004; Member of the Board of Directors of Telesp Celular Participações S.A.

from April 2001 until December 2003; Member of the Board of Directors of Tele Sudeste Participações, S.A. from 2003 until 2005; Member of the Board of Directors of CRT Celular Participações, S.A. from 2003 until 2005; Member of the Board of Directors of Tele Leste Participações, S.A. from 2003 until 2005; Member of the Board of Directors of Tele Centro Oeste Celular Participações, S.A. from 2003 until 2005; Vice-Chairman of the Board of Directors of PT Ventures, SGPS, S.A. (formerly Portugal Telecom Internacional, SGPS, S.A.) from 2000 until 2002; Executive Director and Relationship Manager for Portugal of Merrill Lynch International from 1998 until 1999; Executive Director of Deutsche Morgan Grenfell from 1996 until 1998; Executive Director of Warburg Dillon Read from 1989 until 1996.

Rodrigo Jorge de Araújo Costa. First elected 2005. Term expires 31 December 2008. Aged 47. Vice President of the Executive Committee of Portugal Telecom, SGPS S.A. since April 2006; Chairman of the Board of Directors of PT Comunicações S.A. since March 2006; Member of the Board of Directors of PT Centro Corporativo S.A., since March 2006; Member of the Board of Directors of PT Portugal, SGPS S.A., since March 2006; Member of the Board of Directors of PT Rede Fixa, SGPS S.A., since April 2006; Chairman of the Board of Directors of PT.com Comunicações Interactivas, S.A. April 2006; Chairman of the Board of Directors of PT Prime – Soluções Empresariais de Telecomunicações e Sistemas S.A. April 2006; Chairman of the Board of Directors of PT Sistemas de Informação, S.A. since May 2006; Chairman of the Board of Directors of PT Corporate – Soluções Empresariais de Telecomunicações e Sistemas, S.A. since May 2006; Chairman of the Board of Directors of Portugal Telecom Informação S.A. since June 2006; Member of the High Council for Foreign Investment since 2004; Advisor of the Government Technology Plan since 2005; Corporate Vice President of Microsoft Corporation's OEM Division from 2002 until 2005; General Manager of Microsoft Corporation (Portugal) from 1990 until 2001; General Manager of Microsoft Brazil from 2001 until 2002; Vice President of the Portuguese-American Chamber of Commerce from 1996 until 2001.

Luís Miguel da Fonseca Pacheco de Melo. First elected 2006. Term expires 31 December 2008. Aged: 41. Chief Financial Officer and Executive Director of Portugal Telecom, SGPS S.A. since April 2006; Member of the Board of Directors of Previsão – Sociedade Gestora de Fundos de Pensões, S.A. since 2006; Chairman of the Board of Directors of Cabo TV Açoreana S.A. since 2004; Member of the Board of Directors of Cabo TV Madeirense S.A. since 2003; Member of the Board of Directors of PT PRO – Serviços Administrativos e de Gestão Partilhados, S.A. since 2003; Executive Director of PT Multimédia – Serviços de Telecomunicações e Multimedia, SGPS S.A. from June 2002 until 2006; Member of the Board of Directors of TV Cabo Portugal S.A. from 2002 until 2006; Member of the Board of Directors of Lusomundo Audiovisuais S.A. from 2002 until 2006; Member of the Board of Directors of Lusomundo Cinemas S.A. from 2002 until 2006; Member of the Board of Directors of PT Conteúdos S.A. from 2002 until 2006; Member of the Board of Directors of PT Televisão por Cabo SGPS, S.A. from 2002 until 2006; Member of the Board of Directors of Sport TV from June 2002 until November 2005; Manager of Lusomundo España S.L. from 2002 until 2006; Executive Director of BES Investment, a subsidiary of Banco Espírito Santo Group, one of PT's major shareholders, from 1998 to 2002; Director of UBS Limited from 1995 to 1998.

João Pedro Amadeu Baptista. First elected 2006. Term expires 31 December 2008. Aged 49. Member of the Executive Committee of Portugal Telecom, SGPS S.A. since April 2006; Chairman of the Board of Directors of PT Ventures, SGPS, S.A. (formerly Portugal Telecom Internacional, SGPS, S.A.) since 2006; Chairman of the Board of Directors of PT Móveis – Serviços de Telecomunicações, SGPS S.A. since 2006; Chairman of the Board of Directors of PT Acessos de Internet WI-FI, S.A.; Vice-Chairman of Vivo Participações since 2006; Vice-Chairman of the Board of Directors of Brasilcel, N.V. since 2006; Member of the Board of Directors of Unitel, SARL since 2006; Member of the Audit Committee of the Victoria and Albert Museum in London since 2005; Lead Partner of Booz Allen Hamilton from 2005 to 2006; Global Head of the Technology, Information and Entertainment Industry Group at Marsh & McLennan Companies Inc. from 2004 to 2005; Global Head of the Technology, Information and Entertainment Group and Co-Leader for the United Kingdom of Mercer Management Consulting from 2000 until 2005; Member of the Executive Committee of Mercer Management Consulting from 1997 until 2005.

António Aleixo Caludino Caria. First elected 2006. Term expires 31 December 2008. Aged 55. Member of the Executive Committee of Portugal Telecom, SGPS S.A. since April 2006; Chairman of the Board of Directors of PT Compras – Serviços de Consultoria e Negociação, S.A. since 2006; Chairman of the Board of Directors of PT Contact – Telemarketing e Serviços de Informação, S.A. since 2006; Member of the Board of Directors of Cabo TV Açoreana since 2003; Member of the Board of Directors of TV Cabo Portugal from 2000 until 2006; Managing Director of the Board of TV Cabo Lisboa from 2000 until 2002; CEO of TV Cabo Tejo from 1998 until 2000; Member of the Council of Fundação CulturSintra from 1998 until 2006; Member of the Board of Directors of INESC from 1997 until 2006; Member of the Council of AERSET, Associação Empresarial da Região de Setúbal, from 1996 until 1998; CEO of TV Cabo Sado from 1996 until 1997; Member of the Executive Committee of Portugal Telecom, SGPS S.A. from 1995 until 1996; Regional Managing Director of Portugal Telecom from 1990 until 1995; Manager of Customer Premise Equipment from 1987 until 1990; Manager of National Network Switching Planning from 1983 until 1987.

Rui Pedro Oliveira Barroso Soares. First elected 2006. Term expires 31 December 2008. Aged 34. Member of the Executive Committee of Portugal Telecom, SGPS S.A. since April 2006; Chairman of the Board of Directors of Portugal Telecom Imobiliária, S.A. since 2006; Vice-President of AIP – Associação Industrial Portuguesa since 2006; Member of the Executive Committee of PT Compras – Serviços de Consultoria e Negociação, SA from 2005 to 2006; Consultant to PT Multimédia's Board for Business Intelligence, Quality of Service, Security and Real Estate Management from 2001 to 2004; In the Banque Nationale de Paris/Paribas Executive in Business Intelligence on market and competition analysis; Consultant to the Socialist Group in the European Parliament from 1998 to 2000.

The following directors are not members of the Executive Committee:

Joaquim Anibal Brito Freixial de Goes. First elected 2000. Term expires 31 December 2008. Aged 40. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Board of Directors of PT Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A. since August 2002; Member of the Board of Directors of Companhia de Seguros Tranquilidade – Vida, S.A. since 2002; Member of the Board of Directors of BEST – Banco Electrónico de Serviço Total, S.A. since May 2001; Member of the Board of Directors of Banco Espírito Santo, S.A. since 2000; Chairman of the Board of Directors of E.S. INTERACTION, Sistemas de Informação Interactivos, S.A. since 2000; Member of the Board of Directors of ESDATA, Espírito Santo Data, SGPS, S.A. since 1999; Head of the Strategic Marketing Department of Banco Espírito Santo, S.A. from 1995 until 1999; Head of the Strategic Planning Department of CIMPOR – Cimentos de Portugal, S.A. from 1994 until 1995; Senior Consultant of Roland Berger & Partner from 1991 until 1993; Consultant to Roland Berger & Partner from 1989 until 1991.

Jorge Humberto Correia Tomé. First elected 2002. Term expires 31 December 2008. Aged 52. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Chief Executive Officer of Caixa – Banco de Investimento, S.A. since 2001; Chairman of the Board of Directors of TREM II – Aluguer de Material Circulante, ACE since 2002; Member of the Board of Directors of Caixa – Banco de Investimentos, S.A. since 2001; Member of the Board of Directors of Caixa Gestão de Patrimónios since 2001; Member of the Board of Directors of Insurance Companies of BANIF Group: Açoreana, O Trabalho, O Trabalho Vida and Pension Fund Companies from 1996 until 2001; Partner of Coopers & Lybrand from 1995 until 1996; Manager of International Division of Banco Pinto & Sotto Mayor, S.A. in 1995; Member of the Board of Directors of Banco Pinto & Sotto Mayor, S.A. from 1994 until 1995; Member of the Board of Directors of SULPEDIP, S.A. (currently PME Investimentos, S.A.) from 1989 until 1994; Junior Manager and Principal Manager of Capital Market Division of Banco Pinto & Sotto Mayor, S.A. from 1986 until 1989; Senior Auditor with Coopers & Lybrand from 1980 until 1983; Junior Economist in IAPMEI (Institute for Small and Medium Companies and Investment) from 1979 until 1980.

Fernando Abril-Martorell. First elected 2001. Term expires 31 December 2008. Aged 44. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Chief Executive Officer of Credit Suisse Spain since 2005; Member of the Board of Directors of Telecomunicações de São Paulo – Telesp from 2001 until 2003; Chief Operating Officer of Telefónica S.A. from 2000 until 2003; Chief Executive Officer of Telefónica Publicidad e Informação from 1999 until 2000; Chief Financial Officer

of Telefónica, S.A. from 1997 until 1999; Director-General of Corporate Finance of Telefónica Publicidad e Informação from 1997 until 1999; Head of Treasury Department of JP Morgan from 1987 until 1997.

Antonio Pedro de Carvalho Viana Baptista. First elected 2000. Term expires 31 December 2008. Aged 49. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Chairman of the Board of Directors and Chief Executive Officer of Telefónica de España, S.A.U.; Chairman of the Board of Directors and Chief Executive Officer of Telefónica Móviles España, S.A.U.; Member of the Board of Directors and of the Executive Committee of Telefónica, S.A., holding of Telefónica Group since 2006; Member of the Board of Directors of O2 PLC, and Telefónica Latinoamérica since 2006. Member of the Board of Directors of Telesp Celular Participações, S.A., Tele Leste Celular Participações, S.A., Tele Sudeste Celular Participações, S.A., Tele Centro Oeste Participações, S.A. and Celular CRT Participações, S.A. from 2003 until 2006; Member of the Board of Directors of Telefónica de Argentina, S.A. from 2003 until 2006; Chairman of the Board of Directors and Chief Executive Officer of Telefónica Moviles S.A. from 2002 until 2006; Member of the Board of Directors of Telefónica International, S.A. from 1998 until 2002; Member of the Board of Directors of Latinoamérica, from 1998 until 2002; Member of the Board of Directors of Telesp, S.A. from 2001 until 2006; Member of the Board of Directors of BPI from 1991 until 1996; Principal partner of McKinsey & Company from 1985 until 1991 (Madrid/Lisbon office).

João Manuel de Mello Franco. First elected 1997. Term expires 31 December 2008. Aged 60. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; President of Audit Committee of Portugal Telecom, SGPS S.A.; Member of the Board of Directors of José de Mello Participações, SGPS, S.A. since 2000; Vice-Chairman of the Board of Directors of José de Mello Imobiliária from 2001 until 2004; Chairman of the Board of Directors of José de Mello Residências e Serviços from 2001 until 2004; Chairman of the Board of Directors of Imópolis (SGFII) from 2001 until 2004; Chairman of the Board of Directors of Engimais from 2001 until 2004; Member of the Board of Directors of International Shipowners Reinsurance Cofrom 1998 until 2005; Member of the Superior Board of Portugal Telecom, SGPS S.A. from 1996 until 1997; Chairman of the Board of Directors of Soponata – Sociedade Portuguesa de Navios Tanques, S.A. from 1997 until 2001; CEO and Vice-Chairman of the Board of Directors of LISNAVE from 1995 until 1997; Chairman of the Board of Directors of Marconi from 1994 until 1995; Chairman of the Board of Directors of Guiné Telecom from 1994 until 1995; Chairman of the Board of Directors of Companhia Santomense de Telecomunicações from 1994 until 1995; Member of the Board of Directors of CN – Comunicações Nacionais S.A. from 1993 until 1995; Chairman of the Directorate of the Portuguese Association for the Development of Communications from 1993 until 1995; Chairman of the Board of Directors of TMN – Telecomunicações Móveis Nacionais, S.A. from 1991 until 1994; Chairman of the Board of Directors of TLP – Telefones de Lisboa e Porto S.A. from 1989 until 1994; Director of TDC – Tecnologia das Comunicações, Lda. from 1986 until 1989.

Gerald Stephen McGowan. First elected 2003. Term expires 31 December 2008. Aged 60. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Ambassador of the United States to Portugal from 1997 until 2001; Member of the Board of Directors of the Overseas Private Investment Corporation (OPIC) in 1996; Member of the Board of Directors of Virginia Port Authority in 2002; Member of Board of Directors of Cellular Telecommunications Industry Association from 1990 until 1998.

Tomaz de Mello Paes de Vasconcellos. First elected 2003. Term expires 31 December 2008. Aged 49. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Audit Committee of Portugal Telecom, SGPS S.A. since 2003; Managing Partner of TPV, Lda. since 1998. Member of the Board of Directors of Grupo Santogal from 1989 until 1998; Controller of Hubbard Group from 1987 until 1988.

Franquelim Fernando Garcia Alves. First elected 2006. Term expires 31 December 2008. Aged 52. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Board of Directors of Cinveste Group; Chairman and Chief Executive Officer of IGCP – Instituto de Gestão do Crédito Público from 2004 until 2006; State Secretary Deputy of Economy Minister from 2003 until 2004; Chairman of the Board of Directors of SIMAB – Sociedade Instaladora de Mercados Abastecedores, S.A. since 2002 until 2003; Chief Financial Officer of Lusomundo Group from 2000

until 2002; Member of the Board of Directors of Lusomundo, SGPS S.A., Lusomundo Net, Diário de Notícias, Lusomundo Media, SGPS S.A. and Lusomundo Audiovisuais, SGPS S.A., from 2000 until 2002; Member of the Board of Directors of PT Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A. from 2000 until 2002; Member of the Board of Directors and Chief Financial Officer of Lusomundo, during 1992; Director of Research and Corporate Finance of Socifa & Beta, during 1991; Director of Banco Português do Atlântico, during 1987; Partner of Ernst & Young Portugal, during 1971.

Fernando Henrique Viana Soares Carneiro. First elected 2006. Term expires 31 December 2008. Aged 57. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Economic Council Member at Portuguese Embassy on London since 2003; Consultant from 2002 until 2003; Chairman of the Board of Directors of Somincor – Sociedade Mineira de Neves – Corvo, S.A. and of EDM, Empresa de Desenvolvimento Mineiro, S.A., from 1998 until 2002; Member of the Board of Directors of BERD, Banco Europeu de Reconstrução e Desenvolvimento, from 1993 until 1998; Member of the Board of Directors of Banco Mundial Group; Economic Council Member at Portuguese Embassy on Washington DC, before 1988; Director of SEDES and of DECO, before 1988.

Nuno Rocha dos Santos de Almeida e Vasconcellos. First elected 2006. Term expires 31 December 2008. Aged 42. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Board of several companies; Member of the Remuneration Committee of a bank and Director of the Automóvel Clube de Portugal; devotes his full time running his personal businesses, in Portugal and abroad, through Ongoing Strategy Investments, SGPS, S.A.; In 1995 launched the Portuguese branch of the multinational Heidrick & Struggles; Senior Partner and Managing Partner of Heidrick & Struggles until 2006; Senior Manager of Strategy and Change Management at Andersen Consulting (currently Accenture), from 1987 until 1995; Simultaneously engaged on non-executive responsibilities, at family owned companies; Manager and shareholder of Sociedade do Rosário, SGPS, S.A. from 1987 until 1995.

Luís Filipe Rolim de Azevedo Coutinho. First elected 2006. Term expires 31 December 2008. Aged 46. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Statutory Audit Board of Fundação EDP, since 2005; Member of Board of Directors and member of Audit Committee of EDP – Energias de Portugal S.A., since May, 2003; Consultant of Abrantina Group, since 1992; Director of AMEC – Associação Música Educação e Cultura, from 2003 until 2005; Consultant at Câmara Municipal de Lisboa from 2002 until 2003; Member of the Board of Directors of Valora – Serviços de Apoio à Emissão Monetária, S.A. from 1999 until 2002; Consultant of Banco de Portugal from 1998 until 1999 and from 1995 until 1996; Consultant of Fundação Calouste Gulbenkian from 1996 until 2000; Consultant of Finance State Secretary during 1994; Consultant of V.I/B.T.A Group from 1990 until 1993; Consultant of I.P.E. from 1989 until 1990.

Amílcar Carlos Ferreira de Morais Pires. First elected 2006. Term expires 31 December 2008. Aged 45. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Board of Directors of Banco Espírito Santo, S.A.; Member of the Board of Directors of Companhia de Seguros Tranquilidade – Vida, S.A.; Member of the Board of Directors of Banco Espírito Santo de Investimento, S.A.; Chairman of the Board of Directors of Banco Espírito Santo (International) Limited; Member of the Board of Directors of ESAF – Espírito Santo Activos Financeiros, SGPS, S.A.; Member of the Board of Directors of Espírito Santo PLC (Dublin); Member of the Board of Directors of Banco Espírito Santo Oriente, S.A.; Member of the Board of Directors of Espírito Santo Overseas Limited; Member of the Board of Directors of BES Finance Limited; Member of the Board of Directors of MTS Portugal – Sociedade Gestora do Mercado Especial de Dívida Pública – SGMR, S.A.; Member of Disciplinary Comité of ISMA (International Securities Markets Association); Member of the Board of Directors of Soginpar, Sociedade de Gestão de Fundos de Investimento Mobiliário, S.A. from 1991 until 1992; Member of the Board of Directors of ESER, from 1992 until 1995.

Armando António Martins Vara. First elected 2006. Term expires 31 December 2008. Aged 52. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Board of Directors of Caixa Geral de Depósitos; Chairman of the Board of Directors of IMOCAIXA, S.A.; Chairman of the Board of Directors of SOGRUPO, GI (ACE – CGD Group); Member of the Board of Directors of Caixa Participações, SGPS; Minister of the Youth and the Sport of the XIV

Constitutional Government from September 2000 until December 2000; Deputy Minister of the Prime Minister of XIV Constitutional Government from October 1999 until September 2000; Deputy Secretary of State of the Minister of the Internal Administration of XIII Constitutional Government from 1997 until 1999; Secretary of State of the Internal Administration of XIII Constitutional Government from 1995 until 1997; Member of the House of Representatives in the IV, V, VI e VII Legislatures; Vice President of the Legislative Committees of Social Equipment and Youth; Member of the Parliamentary Assembly of Council of Europe from 1987 until 1991; Member of the Parliamentary Assembly of UEO from 1989 until 1991; Member of the National Secretaryship and the Permanent Commission of the Socialist Party (PS) from 1992 until 2002; Chairman of the Board of Directors of Foundation José Fontana, from 1992 until 1996; Member of Câmara Municipal da Amadora; Member of the Direction of the Institute of the Democratic Press; Member of Instituto Luso – Árabe de Cooperação.

Francisco Teixeira Pereira Soares. First elected 2006. Term expires 31 December 2008. Aged 57. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; President of the Environment Commission of CEEP, Brussels, since 2000; Consultant of Civil House of the President of the Republic from 2005 until 2006; Chief Executive Officer of API Capital, Sociedade de Capital de Risco, S.A., from January 2003 until October 2004; Chairman of the Board of Directors of API Capital, Sociedade de Capital de Risco, S.A., from May until December 2004; Member of the Board of Directors of NAER – Novo Aeroporto, S.A. from 2002 until 2004; Member of the Board of Directors and Chief Executive Officer of I.P.E. – Tecnologias de Informação, SGPS S.A. from 2000 until 2001; Member of the Board of Directors and Member of Executive Committee of I.P.E. – Investimentos e Participações Empresariais, S.A. from 1996 until 2000; Chairman of the Board of Directors of I.P.E. Capital – Sociedade de Capital de Risco, S.A. from 1996 until 2000; Member of the Direction of AMBELIS – Agência para a Modernização Económica de Lisboa, S.A., from 1994 until 1996; Consultant at several companies and Consultant at NBIA (National Business Incubation Association, USA), RBN (European Business Network, Brussels), from 1994 until 1996; Chairman of the Board of Directors of AITEC – Tecnologias de Informação, S.A. from 1987 until 1994; Member of the Direction from 1987 until 1993 and Member of General Council during 1994 of UNINOVA, Instituto de Novas Tecnologias; Member of the Direction of ICTM, Instituto de Ciência e Tecnologia de Materiais from 1987 until 1992; Consultant of the Board of Directors of I.P.E, S.A. from 1987 until 1992; Consultant of IPE, Investimentos e Participações Empresariais, S.A. from 1984 until 1986; Main Assessor of Ministry of the Industry from 1982 until 1986; Director of Ministry of Industry from 1977 until 1981; Chief of Cabinet of the Minister of the Industry and Technology during 1975; Superior technician of the Ministry of the Industry from 1972 until 1977.

José Guilherme Xavier de Bastos. First elected 2007. Term expires 31 December 2008. Aged 68. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Audit Committee of Portugal Telecom SGPS S.A since June 2007; Member of the Centre of Studies of the Chamber of Chartered Accountants since 2003; Member of the Portuguese Privatizations Monitoring Board since December 1988; Lecturer at the Faculty of Law of the University of Coimbra until 2005; Lecturer at the Faculty of Economics of the University of Coimbra until 2004; Appointed as Member of the Board for the Development of the Portuguese Tax Reform in 1994; Member of the Committee drafting Portuguese legislation that implemented the European Directives on the VAT transitional period in the internal market in 1993; Member of the VAT Administration Service in 1992; Member of the Portuguese Tax Reform Board from 1984 until 1988; Appointed as President of the Portuguese VAT Commission in May 1980.

Rafael Luís Mora Funes. First elected 2007. Term expires 31 December 2008. Aged 41. Member of the Board of Directors of Portugal Telecom, SGPS S.A.; Member of the Board of Directors of Ongoing Strategy Investments, SGPS, S.A.; Member of the Remuneration Committee of Impresa Group; Member of the Sustainability and Governance Committee of Millennium BCP Group; Member of the Remuneration Committee of Banco Privado Português; Member of the Supervisory Board of the Business School of INDEG – ISCTE; Director of the Automóvel Clube de Portugal; In 1995 launched with Nuno Rocha dos Santos de Almeida e Vasconcellos the Portuguese branch of the multinational Heidrick & Struggles; Managing Partner of the Portuguese branch of Heidrick & Struggles since 1995.

The business address of each member of the Board of Directors is Av. Fontes Pereira de Melo, no. 40 – 1069-300 Lisbon, Codex.

There are no potential conflicts of interest between the duties to Portugal Telecom of the persons listed above and their private interest or duties.

FINANCIAL STATEMENTS OF PORTUGAL TELECOM

The selected consolidated balance sheet data as of 31 December 2006 and 2005 and selected consolidated statement of income and cash flow data for the years ended 31 December 2006 and 2005 have been derived from PT's audited consolidated financial statements prepared in accordance with International Financial Reporting Standards ("IFRS").

The information set forth below is qualified by reference to, and should be read in conjunction with, PT's audited consolidated financial statements and the notes thereto.

PT's consolidated balance sheet data as of 31 December 2006 and 2005 proportionally consolidate 50 per cent. of Vivo's assets and liabilities. PT's consolidated statement of income and cash flow data for the years ended 31 December 2006 and 2005 proportionally consolidate 50 per cent. of Vivo's income and cash flows.

CONSOLIDATED BALANCE SHEET
AS OF 31 DECEMBER 2005 AND 2006
(Amounts stated in thousands of euros – EUR)

	<i>Year Ended 31 December</i>	
	<i>2005</i>	<i>2006</i>
	<i>EUR</i>	<i>EUR</i>
Current assets	6,153,729.6	3,998,670.8
Non current assets.....	901,968.5	941,167.5
Investments in group companies.....	425,602.6	499,098.3
Other investments.....	96,079.1	132,391.1
Intangible assets, net	3,601,620.5	3,490,881.3
Fixed assets, net	4,062,003.1	3,942,033.2
Deferred taxes	1,387,811.0	1,167,007.2
Total assets	16,628,814.4	14,171,249.3
Current liabilities	4,947,519.5	3,888,379.3
Long-term debt.....	5,168,626.5	4,467,537.1
Other non-current liabilities	959,840.2	811,346.5
Accrued post-retirement liability.....	2,635,883.7	1,807,570.6
Deferred taxes	334,867.1	90,377.8
Total liabilities	14,046,737.0	11,065,211.4
Net assets.....	2,582,077.4	3,106,037.9
Shareholders' equity before Minority interest.....	1,828,391.3	2,255,249.7
Minority interests	753,686.1	850,788.2
Shareholders' equity	2,582,077.4	3,106,037.9
Total liabilities and shareholders' equity	16,628,814.4	14,171,249.3

CONSOLIDATED BALANCE SHEET⁽¹⁾
AS OF 31 DECEMBER 2006 AND 30 JUNE 2007
(Amounts stated in millions of euros – EUR)

	<i>30 June</i>	<i>31</i>
	<i>2007</i>	<i>December</i>
	<u>2006</u>	<u>2006</u>
Cash and equivalents.....	1,351.4	2,083.7
Accounts receivable, net.....	1,406.8	1,417.0
Inventories, net.....	152.1	130.3
Financial investments.....	520.0	631.5
Intangible assets, net.....	3,165.3	3,490.9
Tangible assets, net.....	3,566.3	3,942.0
Accrued post retirement asset.....	123.4	134.1
Other assets.....	963.9	1,050.5
Deferred tax assets and prepaid expenses.....	1,113.8	1,291.4
Assets of discontinued operations (PTM).....	1,105.9	0.0
Total assets	<u>13,468.9</u>	<u>14,171.2</u>
Accounts payable.....	889.4	1,115.1
Gross debt.....	5,631.9	5,840.3
Accrued post retirement liability.....	1,378.6	1,807.6
Other liabilities.....	1,830.6	1,995.7
Deferred tax liabilities and deferred income	300.1	306.5
Liabilities of discontinued operations (PTM)	549.7	0.0
Total liabilities	<u>10,580.2</u>	<u>11,065.2</u>
Equity before minority interests.....	2,003.0	2,255.2
Minority interests.....	885.7	850.8
Total shareholders' equity	<u>2,888.7</u>	<u>3,106.0</u>
Total liabilities and shareholders' equity	<u>13,468.9</u>	<u>14,171.2</u>

(1) Considering a Euro/Real exchange rate of 2.8118 at year-end 2006 and 2.6024 at the end of June 2007.

CONSOLIDATED STATEMENTS OF PROFIT AND LOSS
FOR THE YEARS ENDED 31 DECEMBER, 2005 AND 2006

(Amounts stated in euros – EUR)

	<i>Year Ended 31 December</i>	
	<u>2005</u>	<u>2006</u>
	<i>EUR</i>	<i>EUR</i>
CONTINUED OPERATIONS		
REVENUES		
Services rendered.....	5,836,879,781	5,783,556,158
Sales	447,461,824	461,218,596
Other revenues	101,076,689	98,172,268
	<u>6,385,418,294</u>	<u>6,342,947,022</u>
COSTS, EXPENSES, LOSSES AND INCOME		
Wages and salaries.....	667,331,163	668,383,435
Post retirement benefits.....	(21,605,155)	(72,114,978)
Direct costs	881,181,310	908,351,001
Costs of products sold	652,281,025	596,513,104
Support services	230,180,097	230,004,854
Marketing and publicity	184,409,651	155,401,134
Supplies and external services.....	958,527,829	1,025,503,161
Indirect taxes.....	166,036,274	177,251,170
Provisions and adjustments	171,477,441	230,193,672
Depreciation and amortisation	1,120,668,813	1,209,777,642
Impairment losses	—	—
Curtailed costs, net.....	314,309,785	20,302,638
Losses on disposals of fixed assets, net	1,178,075	8,123,362
Other costs, net	17,652,164	98,431,053
	<u>5,343,628,472</u>	<u>5,256,121,248</u>
Income before financial results and taxes.....	1,041,789,822	1,086,825,774
Net interest expense	257,637,731	227,245,692
Net foreign currency exchange gains.....	(41,335,993)	(4,891,607)
Losses (gains) on financial assets.....	8,765,259	(18,278,335)
Equity in earnings of associated companies, net	(238,226,177)	(131,354,166)
Net other financial expenses	64,453,097	52,289,059
	<u>51,293,917</u>	<u>125,010,643</u>
Income before taxes.....	990,495,905	961,815,131
Minus: Income taxes.....	323,273,235	7,687,318
Net income from continued operations.....	667,222,670	954,127,813
DISCONTINUED OPERATIONS		
Net income from discontinued operations.....	21,732,952	—
NET INCOME	688,955,622	954,127,813
Attributable to minority interests	34,970,803	87,368,156
Attributable to equity holders of the parent	653,984,819	866,759,657
Earnings per share from continued operations		
Basic.....	0.55	0.78
Diluted	0.54	0.77
Earnings per share from total operations		
Basic.....	0.57	0.78
Diluted	0.56	0.77

CONSOLIDATED STATEMENTS OF PROFIT AND LOSS⁽¹⁾
FOR THE YEARS ENDED 31 DECEMBER 2006 AND JUNE 2007

(Amounts stated in millions of euros – EUR)

	<i>Six months ended 30 June</i>	
	<u>2007</u>	<u>2006</u>
Operating revenues	2,955.8	2,805.7
Wireline	992.9	1,053.5
Domestic mobile TMN	728.1	719.9
Brazilian mobile Vivo ⁽¹⁾	1,140.3	1,014.4
Other and eliminations	94.4	17.9
Operating costs, excluding D&A	1,809.0	1,810.1
Wages and salaries	322.6	332.2
Post retirement benefits	(17.3)	23.9
Direct costs	428.1	312.6
Commercial costs	466.2	485.4
Other operating costs	609.4	655.9
EBITDA⁽²⁾	1,146.8	995.6
Depreciation and amortisation	540.6	557.2
Income from operations⁽³⁾	606.2	438.4
Other expenses (income)	111.1	44.8
Curtailment costs	84.4	25.0
Net losses (gains) on disposal of fixed assets	11.7	(0.4)
Net other costs	14.9	20.2
Income before financ. & inc. taxes	495.1	393.6
Financial expenses (income)	(89.1)	105.9
Net interest expenses	90.9	110.7
Equity in losses (earnings) of affiliates	(52.9)	(45.6)
Net other financial losses (gains)	(127.1)	40.8
Income before income taxes	584.3	287.7
Provision for income taxes	(141.1)	65.4
Income from continued operations	443.2	353.1
Income from discontinued operations	28.6	45.2
Losses (income) attributable to minority interests	(42.7)	3.2
Consolidated net income	<u>429.1</u>	<u>401.5</u>

(1) Considering a Euro/Real average exchange rate of 2.6925 in 1H06 and 2.7218 in 1H07.

(2) EBITDA = income from operations + depreciation and mortization.

(3) Income from operations = income before financials and income taxes + curtailment costs + losses (gains) on disposal of fixed assets + net other costs.

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED 31 DECEMBER 2005 AND 2006

(Amounts stated in Euro)

	<i>Year Ended 31 December</i>	
	<i>2005</i>	<i>2006</i>
	<i>EUR</i>	<i>EUR</i>
OPERATING ACTIVITIES		
Collections from clients.....	7,187,846,822	7,392,240,379
Payments to suppliers.....	(3,808,664,290)	(3,668,694,463)
Payments to employees.....	(660,821,689)	(711,353,490)
Payments relating to income taxes.....	(71,572,316)	(54,315,840)
Payments relating to post retirement benefits.....	(699,806,967)	(561,853,113)
Payments relating to indirect taxes and other.....	(554,681,592)	(608,188,638)
Cash flow from operating activities (1).....	<u>1,392,299,968</u>	<u>1,787,834,835</u>
INVESTING ACTIVITIES		
Cash receipts resulting from		
Short-term financial applications.....	10,933,899,233	20,265,545,874
Financial investments.....	391,815,749	6,895,804
Tangible fixed assets.....	12,699,978	11,480,821
Subsidies for investments.....	1,572,005	129,093
Interest and related income.....	262,021,737	238,967,185
Dividends.....	21,424,425	36,110,881
Other investing activities.....	12,365,601	53,796,064
	<u>11,635,798,728</u>	<u>20,612,925,722</u>
Payments resulting from		
Short-term financial applications.....	(12,727,737,929)	(18,501,169,649)
Financial investments.....	(27,168,785)	(95,036,377)
Tangible fixed assets.....	(760,210,386)	(818,459,845)
Intangible assets.....	(16,216,709)	(21,061,568)
Other investing activities.....	(15,205,147)	(29,382,265)
	<u>(13,546,538,956)</u>	<u>(19,465,109,704)</u>
Cash flow from investing activities (2).....	<u>(1,910,740,228)</u>	<u>1,147,816,018</u>
FINANCING ACTIVITIES		
Cash receipts resulting from		
Loans obtained.....	24,239,836,385	16,283,725,363
Increases in share capital and paid-in surplus.....	12,798,336	39,292
Subsidies.....	1,913,794	3,795,801
Other financing activities.....	18,189,355	282,301
	<u>43,126,085,870</u>	<u>16,287,842,757</u>
Payments resulting from		
Loans repaid.....	(22,276,187,094)	(18,024,793,291)
Lease rentals (principal).....	(12,928,273)	(32,959,253)
Interest and related expenses.....	(487,392,109)	(560,221,757)
Dividends.....	(445,415,157)	(581,488,701)
Acquisition of treasury shares.....	(340,455,888)	—
Other financing activities.....	(120,171,654)	(81,046,856)
	<u>(42,535,898,175)</u>	<u>(19,280,509,858)</u>
Cash flow from financing activities (3).....	<u>590,187,695</u>	<u>(2,992,667,101)</u>
Change in cash and cash equivalents (4)=(1)+(2)+(3).....	71,747,435	(57,016,248)
Change in cash and cash equivalents of discontinued operations.....	8,442,819	—
Effect of exchange differences.....	103,849,227	(6,677,620)
Cash and cash equivalents at the beginning of the period.....	428,119,004	612,158,485
Cash and cash equivalents at the end of the period.....	612,158,485	548,464,617

PORTUGAL TELECOM INTERNATIONAL FINANCE B.V.

Portugal Telecom International Finance B.V. (the “**Issuer**”) is a direct wholly-owned subsidiary of Portugal Telecom. The Issuer was incorporated on 26 November 1998 under the laws of The Netherlands as a private company with limited liability (*besloten vennootschap met beperkte aansprakelijkheid*) having its statutory seat in Amsterdam, The Netherlands and is registered with the Amsterdam Commercial Register under No. 34108060. The Issuer has its registered office at Locatellikade 1, 1076 AZ Amsterdam, The Netherlands (Telephone: + 31205 755600). The Issuer’s principal activity is to act as a finance company for the Portugal Telecom group. The Issuer has no subsidiaries.

Management

The Directors of the Issuer, all of which are Managing Directors, at the date of this Offering Circular are:

<i>Name</i>	<i>Business Address</i>	<i>Outside Activities</i>
Carlos Manuel Mendes Fidalgo Moreira da Cruz	Av. Fontes Pereira de Melo, 40 Lisbon, Portugal	Executive Board Member of Portugal Telecom Investimentos Internacionais – Consultoria Internacional, S.A. since May 2006; Manager of the Financial Department of Portugal Telecom, SGPS, S.A. since 2001; Managing Director of Portugal Telecom International Finance BV since 2002; Member of the Portuguese Privatisation Commission from 1999 until 2001; Advisor to the Secretary of State for Treasury and Finance from 1996 until 1998; Lecturer of Financial Strategy from 1996 until 2001 at IEP/EGP MBA Program; Assistant Lecturer of Corporate Finance and Macroeconomics at Oporto University from 1987 until 1996; Assistant Lecturer of Firm Valuation from 1994 to 1997 at IESF; Analyst in the Mergers and Acquisitions Department of BPI from 1990 until 1994; Author of “Obrigações: Mercado, Avaliação e Risco de Taxa de Juro” published by Instituto do Mercado de Capitais/Euronext Lisbon (1995-1999).
Francisco José Meira Silva Nunes	Av. Fontes Pereira de Melo, 40 Lisbon, Portugal	Chief Accounting Officer of Portugal Telecom since 2003; Executive Board Member of PT Multimédia since April 2006; Executive Board Member of PT Pro, S.A. since March 2004; Partner of Audit and Business Advisory Services of Andersen from 1999 until 2002; Manager of Audit and Business Advisory Services of Andersen from 1992 until 1999.
Jan Reint de Vos van Steenwijk	Locatellikade 1 1076 AZ Amsterdam The Netherlands	Managing Director of TMF Group

<i>Name</i>	<i>Business Address</i>	<i>Outside Activities</i>
Maria Christina van der Sluijs- Plantz	Locatellikade 1 1076 AZ Amsterdam The Netherlands	Chief Executive Officer of TMF Group
TMF Management B.V.	Locatellikade 1 1076 AZ Amsterdam The Netherlands	N/A

There are no potential conflicts of interest between the duties to the Issuer of the persons listed above and their private interest or duties

Capitalisation and Indebtedness of Portugal Telecom International Finance B.V.

The table below sets out the capitalisation and indebtedness of Portugal Telecom International Finance B.V. as at 31 December 2005 and 2006 and as adjusted to give effect to the offering of the Bonds. This financial information has been accurately extracted from the audited financial statements of Portugal Telecom International Finance B.V. as at 31 December 2005 and 2006. Amounts are stated in thousands of euros.

	<i>Year Ended 31 December</i>		
	<i>2006 (asadjusted)</i>	<i>2006 (actual)</i>	<i>2005</i>
Short term and current portion of medium and long term debt		0.0	1,289,835.0
Medium and long term debt:			
Bonds	3,629,500.0	2,879,500.0	2,879,500.0
Bank loans	185,000.0	185,000.0	575,000.0
Total medium and long term debt	3,814,500.0	3,064,500.0	3,454,500.0
Total debt	3,814,500.0	3,064,500.0	4,744,335.0
Shareholder's equity:			
Share capital.....	21	21	21
Share premium reserve.....	252,090.4	252,090.4	252,090.4
Accumulated results.....	3,423.7	3,423.7	0.0
Net income.....	2,024.8	2,024.8	3,423.7
Total shareholder's equity	257,559.8	257,559.8	255,535.1
Total capitalisation	4,072,059.8	3,322,059.8	4,999,870.1

PT COMUNICAÇÕES, S.A.

PT Comunicações, S.A. (“PTC”) is a direct wholly-owned subsidiary of PT Portugal SGPS, SA which is a direct wholly owned subsidiary of Portugal Telecom. PTC was incorporated as a Sociedade Anónima under the laws of the Portuguese Republic and registered with the Lisbon Commercial Registry on 18 September 2000 under registration No. 09406. Its registered office is at Rua Andrade Corvo, no. 6, Lisbon (Telephone: +351215001000). PTC’s principal activity is to hold and operate Portugal Telecom’s wireline network. Its business is described above under “*Portugal Telecom – Wireline Business*”. Its business is subject to regulation as described above under “*Portugal Telecom – Regulation Portugal*”.

Management

The following sets out the names, functions and outside activities of the Board of Directors of PTC:

Board of Directors

<i>Name</i>	<i>Function</i>	<i>Outside Activities</i>
Rodrigo Jorge de Araújo Costa	Chairman	See “ <i>Portugal Telecom – Management</i> ”
Carlos Antonio Alves Duarte	Board Member for Corporate Business	CEO of PT SI since 2006; CEO of PT Corporate since 2004; Board Member of PT Comunicações, PT Prime and PT WiFi since 2004; Vice Chairman of Entigere since 2005; Board Member of Banco Best since 2006; Vice Chairman of Caixanet since 2003; CEO of ONI Telecom, ONI Solutions and Brisatel from 2000 until 2003; Chairman of ONI Acores, ONI Madeira and ONI Grandes Redes; President of EDS Iberia during 2000; Managing Director of EDS Portugal, Board Member of EDS Ibéria from 1996 until 1999; General Manager and Board Member of IBM Portugal; Chairman of Rigorsoft and Board Member of Compensa from 1986 until 1996.
José Pedro Pereira da Costa	Chief Financial Officer and Board Member for Human Resources and Legal Affairs	CFO of PT Comunicações since 2002; CFO of PT Prime since 2006; CFO of PT.COM since 2003; Board Member of PTSI since 2006; Board Member of PT PRO since 2003; Board Member of Previsão since 2004; Board Member of PT Prestações since 2004; Board Member of Páginas Amarelas since 2003; Board Member of Telesp Celular Participações from 2001 until 2002; Executive Officer of Telesp Celular Participações and the PT/Telefónica joint venture in Brazil from 2001 to 2002; Executive Board Member of PT Móveis, SGPS, S.A. from 2000 until 2002; CFO of Jazztel Portugal in 2000; Board Member and Head of Corporate Finance of Banco Santander de Negócios

<i>Name</i>	<i>Function</i>	<i>Outside Activities</i>
		Portugal from 1997 until 2000; Engagement Manager of Mckinsey & Co. from 1990 until 1996; Corporate Finance Analyst at Banco Português de Investimento during 1990.
Alfredo José Silva de Oliveira Baptista	Board Member for Infrastructures, SI/TI, National and International Wholesale	Board Member of PT Comunicações since 2004; COO of PT Sistemas de Informação during 2003; CEO of PT Prime, SA from 2001 until 2002; Executive Vice-Chairman of PT Prime, SA from 1999 until 2001; General Manager of the Business Communications Unit of PT from 1996 until 1999; Board Member of PTI from 1996 until 1997; Board Member of PT from 1994 until 1996; Manager of the Major Accounts Business Unit of TLP from 1992 until 1994; Manager of the Planning Dept of TLP from 1987 until 1992; Commercial Manager of TLP from 1982 until 1986.
Luís Miguel Gonçalves Lopes	Board Member for Marketing, Sales and Residential Business	Board Member of PT Comunicações, PT.com and Páginas Amarelas SA since 2006; Manager of distribution channels of PT Comunicações from 2004 until 2006; Associate Principal of McKinsey & Company from 1998 until 2006; Senior Analyst of Procter & Gamble from 1995 until 1998.

The business address of each member of the Board of Directors is Rua Andrade Corvo, no. 6, Lisbon.

There are no potential conflicts of interest between the duties to PTC of the persons listed above and their private interest or duties.

Capitalisation and Indebtedness of PTC

The following table sets out the capitalisation and indebtedness of PTC as at 31 December 2006 and 31 December 2005. This financial information has been accurately extracted from the audited financial statements of PTC as at 31 December 2006 and 2005. Amounts are stated in thousands of euros.

	<i>Year Ended 31 December</i>	
	<i>2006</i>	<i>2005</i>
Total debt	—	—
Shareholders' equity:		
Share capital.....	150,000	150,000
Supplementary capital contribution	948,966.2	948,966.2
Revaluation reserve	124,886.4	138,221.3
Net income	282,488.5	247,254.4
Legal reserves and other.....	86,550.3	71,675.1
Total shareholders' equity	<u>1,592,891.4</u>	<u>1,556,117.0</u>
Total capitalisation	<u><u>1,592,891.4</u></u>	<u><u>1,556,117.0</u></u>

DESCRIPTION OF CONSTITUTION AND SHARE CAPITAL OF PORTUGAL TELECOM

Set forth below is certain information concerning the authorised and issued capital stock of Portugal Telecom and a brief summary of certain significant provisions of Portugal Telecom's Memorandum and Articles of Association and the Portuguese Companies Code. This description does not purport to be complete and is qualified by reference to Portugal Telecom's Memorandum and Articles of Association and to the Portuguese Companies Code.

General

Portugal Telecom is a limited liability holding company organized under the laws of the Portuguese Republic. Portugal Telecom's corporation number is 503 215058.

The company's registered offices are at Avenida Fontes Pereira de Melo, number forty, Lisbon, Portugal.

Portugal Telecom's object and purpose is to manage holdings in other companies as an indirect means of performing economic activities. Portugal Telecom manages ownership interests in operating companies. Portugal Telecom may, without restriction, acquire or hold quotas or shares in any company, as defined under Portuguese law, hold participations in complementary groups of companies or in European economic interest groups of companies and form or participate in any temporary or permanent association with public or private companies.

Share capital and denomination

The issued share capital of Portugal Telecom as of the date hereof is €33,865,695.00 represented by 1,128,856,500 fully paid and issued shares, being 1,128,856,000 fully paid and issued Ordinary shares and 500 fully paid and issued A shares, with a par value of €0.03 each.

The majority of A shares are held by the State or bodies belonging to the public sector.

All the Ordinary shares and A shares are fully paid and registered with the Central de Valores Mobiliários (CVM), the Portuguese central securities depository and in Portugal Telecom's register of shareholders.

Ordinary shares and A shares are in registered form and are ordinarily held in book – entry form. Upon request by the relevant holder to the CVM and after compliance with various Portuguese legal requirements, shares certificates representing Ordinary shares will be issued if certificates are necessary for trading the Ordinary shares outside Portugal.

Portugal Telecom shares are listed on the Euronext Lisbon Stock Exchange. Portugal Telecom shares are listed on the New York Stock Exchange, as ADRs – American Depository Receipts. One ADR represents one ordinary share. Holders of ADRs are entitled to the same rights as ordinary shareholders. Portugal Telecom ADRs depository bank is the Bank of New York.

Voting rights

Shareholders are entitled to one vote per 500 shares held. Only shareholders with voting rights may attend general meetings.

Except for the special voting powers of the A shares described below, matters are decided at a shareholders' meeting by a simple majority of votes. However, resolutions for the amendment of the articles of association, reorganization, dissolution, or merger of Portugal Telecom and certain other matters mandated by Portuguese law, require the approval of two-thirds of votes cast at a shareholders' meeting. A quorum of not less than one-third of the share capital entitled to vote must be present. If the quorum requirement is not met at the first meeting, then matters may be approved on a later day at a second call of such meeting by (i) a two-thirds majority of the votes cast at the meeting or (ii) a simple majority of the votes cast if at least one half of the share capital is represented.

Under the articles of association, the voting rights exercised by a single shareholder, except those of the Portuguese State and certain entities owned by the Portuguese State, are limited to a maximum of 10 per cent. of Portugal Telecom's share capital. As a result, no single shareholder other than the Portuguese State can exercise voting rights in his own name or on behalf of other

shareholders representing more than 10 per cent. of Portugal Telecom's share capital. Holders of ADRs are treated as holders of the ordinary shares represented by the ADRs for purposes of determining the applicability of the 10 per cent. limitation on voting rights. Voting instructions of an individual ADRs holder will not be accepted by Portugal Telecom as votes of the ordinary shares to the extent that such votes, together with any votes cast by such ADRs holder as holder of ordinary shares, exceed 10 per cent. of the voting power of Portugal Telecom.

Under the Portuguese Companies Code, all rights attached to treasury stock are suspended, including voting rights. As a result, treasury stock is not counted for the purpose of calculating any minimum quorum nor for determining a majority of votes cast. The purchase by Portugal Telecom of its own shares generally must be approved by its shareholders in accordance with the articles of association and the Portuguese Companies Code. Under Portuguese law, a Portuguese company may not, except under certain limited circumstances (such as the repurchase of its own shares for the purpose of reducing the share capital), purchase more than 10 per cent. of its nominal share capital as treasury stock. At the General Meeting of Shareholders held on April 27 2007, Portugal Telecom approved a share buyback program with the purpose of reducing the share capital by up to 16.5 per cent.

Special Approval Rights of the A Shares

The majority of Portugal Telecom's A shares must be held by either the Portuguese State or bodies belonging to the public sector.

Under the articles of association, the holders of Portugal Telecom's A shares, based on a majority voting as a class, may veto a number of actions of the shareholders of Portugal Telecom, including the following:

- Authorization for the acquisition of ordinary shares representing more than 10 per cent. of the share capital by shareholders that directly or indirectly perform competing activities with those of the companies within a control relationship with Portugal Telecom, SGPS S.A;
- Amendments to the by-laws and share capital increases, as well as the limitation or suppression of pre-emptive rights and the establishing of standards for share capital increases to be resolved by the Board of Directors;
- Issuing of bonds or other securities, establishing the issue value for these securities to be resolved by the Board of Directors and limitation or suppression of pre-emptive rights in the issuing of bonds convertible into shares, as well as establishing the standards for the issuing of bonds of such nature to be resolved by the Board of Directors;
- The passing of resolutions on the application of the financial year results, in the event of a dividend distribution to the shareholders in a percentage superior to 40 per cent. of distributable profits;
- Election of the chairman of the audit committee and the statutory auditor, as well as the members of the General Meeting Board;
- Approval of the general goals and fundamental principles of the Company's policies; and
- Definition of the general policy of shareholdings in companies, as well as, in cases where authorized by a prior General Shareholders' Meeting, the passing of resolutions on the respective acquisitions and sales.

Additionally, the election of one-third of the directors, including the chairman of the board of directors, must be resolved with the majority of the votes cast of the ordinary shareholders and with the approval of the Portuguese State, as the holder of A shares. In April 2006, the European Commission sent the Portuguese government a formal request to abandon the special rights the Portuguese State holds as sole owner of Portugal Telecom's A shares. The European Commission believes that the special powers granted to the Portuguese State through sole ownership of A shares act as a disincentive for investment by other EU member states in a manner that violates European Community Treaty rules. Should the Portuguese authorities not take satisfactory steps to remedy the

alleged infringement of EU law, the European Commission may decide to refer the case to the European Court of Justice.

Dividends

Determination of dividends

Portugal Telecom's ordinary shares and A shares carry the same dividend rights.

Portugal Telecom's policy has been to propose an annual dividend subject to its financial and economic condition, but in no event less than 40 per cent. of its distributable net income, excluding income from subsidiaries and affiliates that has not yet been distributed to Portugal Telecom.

At the Annual General Shareholders' Meeting on 27 April 2007, shareholders approved the distribution of gross dividends in the amount of €0.475 per share with respect to the fiscal year ended 31 December 2006.

The board of directors has sole discretion over the proposal of dividends. Under the articles of association, Portugal Telecom must pay dividends of at least 40 per cent. of its annual distributable net income to shareholders, subject to the ability of a two-thirds majority of the votes cast at a shareholders' meeting to decide to reduce the dividend or not pay a dividend. Any dividend exceeding 40 per cent. of Portugal Telecom's distributable net income in any year may not be distributed if holders of the A shares vote against the distribution.

Dividends are payable from net income and free reserves (i.e., reserves other than the legal reserve). Portuguese law requires net income and free reserves to be applied against accumulated losses for the given financial year, and only thereafter may share issuance premium be applied against accumulated losses.

The share issuance premium is the amount corresponding to the subscription price paid for a share over the par value of the share. This requirement was amended by Ministerial Order, dated 19 February 2003 ("Portaria n° 106/2003"), so that companies listed on a stock exchange and under the supervision of the Portuguese Securities Commission are permitted to apply share issuance premium against accumulated losses after applying net income but before applying free reserves.

Under Portuguese law and the articles of association, distributable net income is net income after covering accumulated losses and setting aside not less than 5 per cent. in the legal reserve, on an annual basis until this reserve represents 20 per cent. of share capital. As of 31 December 2006, Portugal Telecom's legal reserve was equal to approximately 20.9 per cent. of share capital.

Portuguese law also prohibits the payment of dividends if, following the dividend, a company's net worth would be less than the sum of its share capital, the legal reserve and other similar reserves established by Portuguese law or by the articles of association. The category of other similar reserves includes, among other things, the portion of the revaluation reserve related to assets not yet amortized and the reserve equivalent to the book value of treasury shares. Portugal Telecom's articles of association do not provide for any other reserves.

The ADR depository converts Euros into U.S. dollars and pays the net proceeds to ADR holders.

Limitation for payment of dividends

According to the new rules established by article 96 of the Portuguese Securities Code (as amended by the Decree-Law no 8/2007, of 17 January 2007), for one month from the publication of the registration of a share capital reduction, Portugal Telecom will not be able to distribute assets to its shareholders. Given that the recording of the share capital decrease in the commercial registry was published on 22 May 2007, Portugal Telecom will be free to distribute its assets beginning 22 June 2007.

Interim dividends

The board of directors, subject to certain conditions, including the consent of Portugal Telecom's audit committee and the certification of the statutory auditor, may also authorize the payment of interim dividends.

Payment of dividends

The holder of record of ordinary shares or A shares on the date of payment of any dividend is entitled to receive that dividend. The settlement of a trade and the transfer of ownership record of shares traded on the regulated market Eurolist by Euronext Lisbon takes place on the third business day after the trade. As a result, any person making a trade for the purchase of ordinary shares during the three-day period prior to the record date for a dividend payment will not be entitled to receive such dividend.

Shareholders' meetings

Shareholders' meetings may be held at Portugal Telecom's registered office or, when the registered office does not have satisfactory conditions for the meeting, at another location within the Portuguese territory. Shareholders' meetings are called by publication of a notice on a journal, on the Ministry of Justice's website (<http://publicacoes.mj.pt>), the CMVM's website (www.cmvm.pt) and Portugal Telecom's website (www.telecom.pt). An annual shareholders' meeting must be held before the end of May and must be convened on not less than one month's notice. The annual shareholders' meeting usually takes place in April. At the annual shareholders' meeting, the annual accounts, including a report on Portugal Telecom's activities during the previous year and any proposal for the payment of dividends, are presented to the shareholders for approval. Meetings may also be called upon the request of the board of directors, the audit committee or shareholders holding at least 5 per cent. of share capital.

To attend a shareholders' meeting in person or by proxy or to vote by courier, shareholders must demonstrate that the ordinary shares they hold are registered in a securities account for ordinary shares at least five business days in advance. Shareholders may appoint proxies in writing. No shareholder may be represented by more than one representative. Shareholders' meetings are presided over by a chairman appointed by the shareholders.

Rights of major shareholders

Portugal Telecom's major shareholders do not have different voting rights than other Portugal Telecom ordinary shareholders or ADRs holders.

Transfer of Ordinary Shares, Limitations on Shareholdings

There are no restrictions on the transferability of the ordinary shares, other than certain limitations on ownership. Under the Portuguese Securities Code, any person making a purchase or sale of shares that results in that person either reaching, exceeding or holding less than 2 per cent., 5 per cent., 10 per cent., 20 per cent., 1/3, 1/2, 2/3 or 90 per cent. of Portugal Telecom's voting rights must notify Portugal Telecom, the managing entity of the regulated market Eurolist by Euronext Lisbon and the CMVM within three calendar days.

The articles of association contain limitations on ownership, as well as enforcement mechanisms, designed to prevent an unauthorized change in control of Portugal Telecom. The articles of association provide that no shareholder performing, directly or indirectly, an activity which competes with any of Portugal Telecom's activities may hold or control ordinary shares representing in the aggregate more than 10 per cent. of Portugal Telecom's share capital, without the authorization of a shareholders' meeting. An entity will be deemed to be performing an activity which competes with Portugal Telecom's activities if they, a company of which they own at least 10 per cent. of the share capital or a company that owns at least 10 per cent. of the share capital of them (i) offers, in or outside of Portugal, "public telecommunications services" (except "audiotext services") or "network services," as such terms are defined under Portuguese law or (ii) engages in any other activity of the same type and nature as that being performed by entities in which Portugal Telecom holds more than 50 per cent. of the share capital or voting power or has the power to appoint more than 50 per cent. of the governing body or of the supervisory body. The Bank of New York, as ADRs depositary, and its nominees are excluded from this requirement.

In addition, under the articles of association, the voting rights exercised by a single shareholder, except the Portuguese government and certain entities owned by the Portuguese government, are limited to a maximum of 10 per cent. of Portugal Telecom's share capital. As a result, no single

shareholder other than the Portuguese government can exercise voting rights, in his own name or on behalf of other shareholders, representing more than 10 per cent. of Portugal Telecom's share capital.

If any such shareholder holds or controls ordinary shares exceeding 10 per cent. of Portugal Telecom's share capital, the shareholders may decide at a shareholders' meeting to require the cancellation of the ordinary shares held exceeding such 10 per cent. limit. In such case, Portugal Telecom must compensate the shareholder for the lesser of the nominal value of the cancelled ordinary shares or their market value. However, within five days of receipt of notice of such a decision by the shareholders' meeting, a shareholder may request the permission of the board to reduce the number of ordinary shares held to 10 per cent. or less of Portugal Telecom's share capital by sale or other form of transfer of the excess ordinary shares within 30 days. By making such request, such shareholder renounces, pending the conclusion of such sale or transfer, all voting and pre-emptive subscription rights connected to the excess ordinary shares.

Holders of ADRs will be treated as holders of the ordinary shares represented by the ADRs under these provisions.

There are no restrictions under Portuguese law with regard to the percentage of shares that a non-Portuguese resident may own in Portugal Telecom.

Pre-emptive rights. Rights Issue

Upon the issuance of additional ordinary shares by Portugal Telecom for cash, all holders of ordinary shares and A shares have a right to subscribe proportionately for such shares. Upon the issuance of additional A shares by Portugal Telecom, holders of A shares have a right to subscribe proportionately for such shares, and to the extent that all such shares are not sold, holders of ordinary shares may subscribe proportionately for the remainder of the shares. The pre-emptive rights of shareholders to subscribe for shares are freely transferable.

Such pre-emptive rights can be limited or waived by a shareholders' decision as long as corporate interest so determines.

There are no rights issued by Portugal Telecom that grant to the existing shareholders the right to buy a proportional number of additional shares at a given price within a fixed period.

Under Portuguese Law the most similar instruments to the rights issue are the preference rights described in the previous paragraphs in the context of an increase of the share capital and the subscription rights embodied in the warrants.

On 27 April 2007, the General Meeting of Shareholders approved the possible issue of convertible bonds which may be adopted by a resolution of the Board of Directors pursuant to the law and the articles of association and in accordance with the parameters set forth in that resolution of the General Meeting of Shareholders. Therefore, in order to ensure that the Board of Directors is able to perform all the share capital increases that may be necessary to guarantee the satisfaction of all requests for conversion into shares that may occur in respect of the convertible bonds that are permitted to be issued by the Company, the Board of Directors proposed that the General Meeting of Shareholders update the general authorization for the approval of share capital increases by the Board of Directors, as set forth in paragraph 3 of Article Four of the Articles of Association. This general authorization was approved at the General Meeting held on 22 June 2007, and the maximum amount of share capital increases was fixed at €15,000,000.

Rights of purchase and redemption of the Keep Well Provider's Ordinary Shares

According to Portugal Telecom's bylaws the ordinary shares may be redeemed without the need for consent of the following respective holders:

- (i) those held without the prior authorisation of the general meeting, by a shareholder who/ which is engaged in a competing activity and when such shares, in conjunction with the shares referred to in the following sub paragraph, exceed the amount of ten per cent of the share capital; and

- (ii) those held by entities whose shares, pursuant to the terms of the Securities Market Code, would be considered, in the case of a public take-over bid, as belonging to the shareholders referred to in the preceding sub paragraph, whose proportion, after the redemption referred to in this sub paragraph, exceeds the amount of ten per cent of the share capital, with the redemption being proportional to the number of shares held by each of the entities in question.

The shares referred to in the preceding sub paragraphs may be redeemed at their nominal or respective market value, if lower. The board of directors shall notify the respective shareholders that their shares shall be redeemed, within a maximum period of thirty days following the resolution to redeem the shares adopted at the general meeting.

Shareholders may suspend the redemption process if, within a period of five days from the notification, they have applied to the board of directors for permission to alienate the shares to be redeemed, within a period of time of no more than thirty days, with the aforementioned application implying the renunciation of their corresponding voting and preference rights in the event of any increase in share capital up until the effective date of sale.

The Board of Directors shall promote the performance of the acts and the fulfilment of the formalities legally required for the execution of the share capital reduction.

The consideration payable to the holders of the redeemed shares shall be paid after they have certified that the shares are no longer recorded in the respective book-entry securities accounts and shall be paid in a lump sum or be deferred over a period of no more than two years from the date of redemption.

When the redeemed shares are registered, in legally acceptable cases, the consideration payable to their respective holders shall be paid against the delivery of the respective securities pursuant to the conditions defined in the preceding number.

The purchase by Portugal Telecom of its own shares generally must be approved by its shareholders in accordance with the articles of association and the Portuguese Companies Code. Under Portuguese law, a Portuguese company may not, except under certain limited circumstances (such as the repurchase of its own shares for the purpose of reducing its share capital), purchase more than 10 per cent. of its nominal share capital as treasury stock. At the General Meeting of Shareholders held on April 27, 2007, Portugal Telecom approved a share buyback program with the purpose of reducing the share capital by up to 16.5 per cent.. As duly disclosed to the market, the Company has negotiated, with several financial institutions, the terms of the agreements of financial derivative instruments (equity swaps) over own shares, which provide for the possibility of physical settlement at the option of the Company. These agreements of financial derivative instruments (equity swaps) over own shares were authorised in the said General Meeting of Shareholders when it approved the buyback.

Disclosure of interests in shares

Under the Portuguese Securities Code, any person making a purchase or sale of shares that results in that person either reaching, exceeding or holding less than 2 per cent., 5 per cent., 10 per cent., 20 per cent., 1/3, 1/2, 2/3 or 90 per cent. of Portugal Telecom's voting rights (*qualified holding*) must notify Portugal Telecom, the managing entity of the regulated market Eurolist by Euronext Lisbon and the CMVM within three calendar days.

The Board of Directors must disclaim the number of ordinary shares that may be deemed to be beneficially owned by them, which include amounts that are beneficially owned by shareholders of Portugal Telecom with which the director in question is affiliated and the beneficial ownership of any shares they do not own directly.

The members of the Board of Directors and the members of the statutory audit must also communicate to the Company the number of shares and bonds owned by them, including the acquisitions, option agreements and agreements with similar effect, disposals and the creation of any securities over such shares and bonds, as well as over the shares representing the share capital of a company controlled by or with which the Company has established a group relation (as defined under Portuguese Law) and shares and bonds held by spouses and descendants are deemed to be included

in the number of shares and bonds owned by the members of the Board of Directors and the members of the statutory audit.

The annual report of the company should contain this information.

There are no share option plans currently in place.

Shareholder appointment and removal of directors

The rules governing the composition of the Board of Directors were changed at the General Meeting of Shareholders held on 22 June 2007. Under the new rules, the Board of Directors is composed of any odd or even number of 15 to 23 directors, including the Chairman. The board of directors currently consists of twenty – three directors.

The directors are elected by a majority of the votes cast at the annual shareholders' meeting following the expiration of their term. In addition, a majority of votes cast by holders of A shares is required to elect one-third of the members of the Board of Directors, including the Chairman of the Board. A minority of the shareholders representing, in the aggregate, at least 10 per cent. of Portugal Telecom's share capital, has the right to elect a director to substitute for the director previously elected by the fewest number of votes.

Members of the board of directors are elected for a three-year period and may be re-elected on one or more occasions. The term of office of the directors is three calendar years, being the year of election or appointment considered a full calendar year. There is no restriction on the re-election of directors.

The quorum for a meeting of the Board of Directors is a simple majority of directors. All directors have equal voting rights, and all resolutions of the Board of Directors are adopted by a majority of the votes cast. The Chairman has the deciding vote in the event of a tie.

The articles of association provide for an Executive Committee of the Board to which the Board of Directors can delegate the management of Portugal Telecom's affairs and the monitoring of the daily operation of Portugal Telecom's activities. However, the Board of Directors remains responsible for Portugal Telecom's overall management and operations. The Executive Committee may be comprised of five or seven directors selected by a majority of the Board of Directors. From among the directors elected with the approval of a majority of holders of A shares, at least one or two must be appointed to the Executive Committee (depending on whether the Executive Committee is composed of five or seven directors). The vote of a majority of the members of the Executive Committee is necessary for the taking of an action by the Executive Committee. All members have equal voting rights, and the President has the deciding vote in the event of a tie.

Directors' liability

The Board of Directors of Portugal Telecom is responsible for its management and affairs. Portugal Telecom's officers are either in charge of its various business and administrative departments and report directly to the Board of Directors or are in charge of Portugal Telecom's subsidiaries.

According to the Portuguese Companies Code, Directors are liable for damages caused to (i) the Company; (ii) the Company's creditors; and (iii) the shareholders or third parties which result from acts performed during the exercise of their office and pursuant thereto.

There are common aspects to the Director's liability as follows:

- The directors are only liable if they have acted wilfully or negligently, being the assessment of their wilfulness or negligence is made with reference to the high duty of care imposed on them by article 64 of the Portuguese Companies Code;
- The Director's Liability is joint and several, notwithstanding their right of redress in light of their fault in the event triggering the liability and its consequences;
- A Director's failure to vote or its vote against a given Board decision excludes his liability for damages arising from the same; and

- Neither a favourable opinion of the auditing board nor its consent for the performance of the act giving rise to damage or to an insufficiency of the company's estate to fulfil its obligations towards the creditors exonerates the directors from liability.

As mentioned above, there are three types of Director's liability:

- (i) Liability towards the Company – Directors shall be liable for any damages caused which arise from acts or omissions in breach of their legal or contractual duties. The burden of proof that damages were not due to the directors' wilful or negligent misconduct lies on the directors. It should be noted that directors are not liable towards the company if the act or omission from which damages arise is based on a General Meeting decision. It is important to mention that the 2006 reform of the Portuguese Companies Code, implemented by the Decree-Law nr. 76-A/2006, of 29 March 2006 introduced the "business judgment rule" as the pattern of diligence to which directors are submitted in the fulfilment of their duties.
- (ii) Liability towards the Company's creditors – Directors are liable towards the Company's creditors in the event that, as a result of a wilful or negligent breach of legal provisions aimed at protecting the creditor's interests becomes, the company's estate became insufficient to fulfil its obligations. This liability subsists, even if the act or omission is based on a shareholders' decision.
- (iii) Liability towards the shareholders or third parties – Directors are liable, under the general terms of the law, towards the shareholders or third parties, for damages caused to them directly in the exercise of the directors' activity. It should be noted that directors are not liable towards the shareholders or third parties if the act or omission from which damages arise is based on a General Meeting decision.

Foreign Investment and Foreign Exchange Controls

Portugal does not impose foreign-exchange controls. No restrictions are imposed on inbound or outbound investments.

There are no restrictions under Portuguese law with regard to the percentage of shares that a non-Portuguese resident may own in Portugal Telecom.

As long as the Portuguese government holds a majority of Portugal Telecom's A shares, it will have the right, under the articles of association, to veto any resolutions defining the general principles of the policy for investing in companies or deciding on acquisitions and alienations when, in accordance with these principles, the transactions are required to be authorized in advance by the general meeting.

Liquidation rights

The ordinary shares and A shares have *pro rata* rights to share in Portugal Telecom's assets upon its liquidation.

SHARE PRICE HISTORY

The table below sets out, for the periods indicated, the reported high and low closing sales prices per Ordinary Share on the Euronext Lisbon, the principal market for the Ordinary Shares. As at 21 August 2007, the closing price per Ordinary Share on the Euronext Lisbon was EUR 9.69.

Period	<i>Price per Share</i>	
	<i>High</i>	<i>Low</i>
	<i>(in EUR)</i>	
2004		
First Quarter	9.42	8.08
Second Quarter	9.28	8.20
Third Quarter	8.94	8.13
Fourth Quarter	9.27	8.78
2005		
First Quarter	9.73	8.90
Second Quarter	9.23	7.55
Third Quarter	8.16	7.44
Fourth Quarter	8.69	7.38
2006		
First Quarter	10.29	8.09
Second Quarter	10.18	9.16
Third Quarter	9.90	9.47
Fourth Quarter	9.90	9.65
2007		
January	10.29	9.80
February	10.29	10.07
March	10.13	9.60
April	10.50	10.09
May	10.50	9.92
June	10.39	9.87
July	10.41	10.10

(Source: Bloomberg)

Information about the past and the further performance of the Ordinary Shares and its volatility can be obtained from the Portugal Telecom website (www.telecom.pt).

Dividends

The following table sets out the total gross dividends paid by Portugal Telecom per Ordinary Share in respect of each year indicated:

<i>Year Ended 31 December</i>	<i>Total</i>
	<i>(in EUR)</i>
2003	0.22
2004	0.35
2005	0.475
2006	0.475

In February 2007, in connection with its response to the tender offer by Sonaecom, Portugal Telecom announced a shareholder remuneration package that also included a €0.475 per share dividend related to the year 2006 and a €0.575 per share dividend related to years 2007 and 2008.

Issued Share Capital

The following table sets out the issued share capital as at the dates indicated:

Dates	<i>Amount</i>
31 December 2005.....	€1,128,856,500
31 December 2006.....	€395,099,775
23 August 2007	€33,865,695

TAXATION

The following summary of certain taxation matters of Luxembourg, the Netherlands and Portugal is based on the laws and practice in force as of the date of this Offering Circular and is subject to any changes in law and practices (and the interpretation and application thereof) occurring after such date, which changes could be made on a retroactive basis. The following summary does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to purchase, own or dispose of the Bonds, or to exchange Bonds for Ordinary Shares, and does not purport to deal with the tax consequences applicable to all categories of investors, some of which (such as dealers in securities) may be subject to special rules. This summary is of a general nature based on the understanding of Portugal Telecom of current law and practice. Investors should consult their professional advisers on the possible tax consequences of their subscribing for, purchasing, holding, selling or redeeming Bonds and exchanging Bonds for Ordinary Shares under the laws of their country of citizenship, residence, domicile or incorporation.

Luxembourg

The following summary is of a general nature and is included herein solely for information purposes. It is based on the laws presently in force in Luxembourg, though it is not intended to be, nor should it be construed to be, legal or tax advice. Prospective investors in the Bonds should therefore consult their own professional advisers as to the effects of state, local or foreign laws, including Luxembourg tax law, to which they may be subject.

Please be aware that the residence concept used under the respective headings below applies for Luxembourg income tax assessment purposes only. Any reference in this section to a tax, duty, levy, impost or other charge or withholding of a similar nature refers to Luxembourg tax law and/or concepts only. Also, please note that a reference to Luxembourg income tax encompasses corporate income tax (*impôt sur le revenu des collectivités*), municipal business tax (*impôt commercial communal*), a solidarity surcharge (*contribution au fonds de chômage*) as well as personal income tax (*impôt sur le revenu*) generally. Investors may further be subject to net wealth tax (*impôt sur la fortune*) as well as other duties, levies or taxes. Corporate income tax, municipal business tax as well as the solidarity surcharge invariably apply to most corporate taxpayers resident of Luxembourg for tax purposes. Individual taxpayers are generally subject to personal income tax and the solidarity surcharge. Under certain circumstances, where an individual taxpayer acts in the course of the management of a professional or business undertaking, municipal business tax may apply as well.

Withholding Tax

(i) Non-resident holders of Bonds

Under Luxembourg general tax laws currently in force and subject to the laws of 21 June 2005 (the **Laws**) mentioned below, there is no withholding tax on payments of principal, premium or interest made to non-resident holders of Bonds, nor on accrued but unpaid interest in respect of the Bonds, nor is any Luxembourg withholding tax payable upon redemption or repurchase of the Bonds held by non-resident holders of Bonds.

Under the Laws implementing the Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments and ratifying the treaties entered into by Luxembourg and certain dependent and associated territories of EU Member States (the **Territories**), payments of interest or similar income made or ascribed by a paying agent established in Luxembourg to or for the immediate benefit of an individual beneficial owner or a residual entity, as defined by the Laws, which are resident of, or established in, an EU Member State (other than Luxembourg) or one of the Territories will be subject to a withholding tax unless the relevant recipient has adequately instructed the relevant paying agent to provide details of the relevant payments of interest or similar income to the fiscal authorities of his/her/its country of residence or establishment, or, in the case of an individual beneficial owner, has provided a tax certificate issued by the fiscal authorities of his/her country of residence in the required format to the relevant paying agent. Where withholding tax is applied, it will be levied at a rate of 15 per cent. during the first three-year period starting 1 July 2005, at a rate of 20 per cent. for the subsequent three-year period and at a rate of 35 per cent. thereafter. Responsibility for the withholding of the tax will be assumed

by the Luxembourg paying agent. Payments of interest under the Bonds coming within the scope of the Laws would at present be subject to withholding tax of 15 per cent..

(ii) Resident holders of Bonds

Under Luxembourg general tax laws currently in force and subject to the law of 23 December 2005 (the **Law**) mentioned below, there is no withholding tax on payments of principal, premium or interest made to Luxembourg resident holders of Bonds, nor on accrued but unpaid interest in respect of Bonds, nor is any Luxembourg withholding tax payable upon redemption or repurchase of Bonds held by Luxembourg resident holders of Bonds.

Under the Law payments of interest or similar income made or ascribed by a paying agent established in Luxembourg to or for the immediate benefit of an individual beneficial owner who is resident in Luxembourg will be subject to a withholding tax of 10 per cent.. Such withholding tax will be in full discharge of income tax if the beneficial owner is an individual acting in the course of the management of his/her private wealth. Responsibility for the withholding of the tax will be assumed by the Luxembourg paying agent. Payments of interest under the Bonds coming within the scope of the Law would be subject to withholding tax of 10 per cent..

The Netherlands

The following summary of certain Netherlands taxation matters is based on the laws and practice in force as of the date of this Offering Circular and is subject to any changes in law and the interpretation and application thereof, which changes could be made with retroactive effect. The following summary does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to acquire, hold or dispose of the Bonds, and does not purport to deal with the tax consequences applicable to all categories of investors, some of which (such as dealers in Bonds) may be subject to special rules. Save as otherwise indicated, this summary only addresses the position of investors who do not have any connection with the Netherlands other than the holding of the Bonds. Investors should consult their professional advisers on the tax consequences of their acquiring, holding and disposing of the Bonds.

Withholding Tax

All payments by the Issuer of interest and principal under the Bonds can be made free of withholding or deduction of any taxes of whatsoever nature imposed, levied, withheld or assessed by the Netherlands or any political subdivision or taxing authority thereof or therein.

Taxes on Income and Capital gains

A holder of a Bond who derives income from a Bond or who realises a gain on the disposal or redemption of a Bond will not be subject to Dutch taxation on such income or capital gains unless:

- (i) the holder is or is deemed to be resident in the Netherlands, or, where the holder is an individual, such holder has elected to be treated as a resident of the Netherlands; or
- (ii) such income or gain is attributable to an enterprise or part thereof which is either effectively managed in the Netherlands or carried on through a permanent establishment (*vaste inrichting*) or permanent representative (*vaste vertegenwoordiger*) in the Netherlands; or
- (iii) the holder is an individual and such income or gain qualifies as income from miscellaneous activities (*belastbaar resultaat uit overige werkzaamheden*) in the Netherlands as defined in the Dutch Income Tax Act 2001 (*Wet inkomstenbelasting 2001*).

Gift, Estate or Inheritance tax

Neither the fact that the Issuer is a Dutch tax resident entity nor any other feature of the Bonds as such gives rise to a liability to Dutch gift, estate or inheritance tax on the occasion of a transfer of a Bond by way of gift by a holder or on the death of a holder.

Dutch gift, estate or inheritance taxes will not be levied on the occasion of the transfer of a Bond by way of gift by, or on the death of, a holder, unless:

- (i) the holder is or is deemed to be resident in the Netherlands for the purpose of the relevant provisions; or
- (ii) the transfer is construed as an inheritance or as a gift made by, or on behalf of, a person who, at the time of the gift or death, is or is deemed to be resident in the Netherlands for the purpose of the relevant provisions; or
- (iii) such Bond is attributable to an enterprise or part thereof which is either effectively managed in the Netherlands or carried on through a permanent establishment or a permanent representative in the Netherlands.

Value Added Tax

There is no Dutch value added tax payable by a holder of a Bond in respect of payments in consideration for the issue of the Bonds or in respect of the payment of interest or principal under the Bonds, or the transfer of the Bonds.

Other Taxes and Duties

There is no Dutch registration tax, stamp duty or any other similar tax or duty payable in the Netherlands by a holder of a Bond in respect of or in connection with the execution, delivery and/or enforcement by legal proceedings (including any foreign judgement in the courts of the Netherlands) of the Bonds or the performance of the Issuer's obligations under the Bonds.

Residence

A holder of a Bond will not be treated as resident of the Netherlands by reason only of the holding of a Bond or the execution, performance, delivery and/or enforcement of the Bonds.

Portugal

General

The present summary is only a general description of the Portuguese relevant tax aspects related to the purchase of exchangeable bonds, including tax treatment of particular bondholders, namely institutional entities, such as pension funds, private equity entities, investment funds, banks and insurance companies. The statements do not deal with other Portuguese tax aspects regarding the Bonds and relate only to the position of persons who are absolute beneficial owners of the Bonds. It is not exhaustive and holders who are in doubt as to their tax position should consult their professional advisers.

Tax treatment on exchangeable bonds

Tax treatment of exchangeable bonds held by Corporate holders resident in Portugal

The description below is made with the assumption that the Bonds will be considered, by the Portuguese tax authorities, as debt instruments, such as corporate bonds ("obrigações").

Corporate holders, including Portuguese holding companies (SGPS) or Venture Capital Companies (SCR), of exchangeable bonds who are resident in Portugal for tax purposes are taxed in Portugal on interest received on the exchangeable bonds and gains obtained on their disposal, which should be included in its taxable income and subject to a corporate tax rate of 25 per cent., plus a municipality surcharge of a maximum of 1.5 per cent., giving a combined tax rate of 26.5 per cent..

If holders are special entities, such as Investment Funds, Pension Funds or Private Equity Funds, a special tax regime will be applicable, as such:

- (i) Pension Funds incorporated in accordance with Portuguese law – according to section 14 of Portuguese tax Benefit Statute (EBF), income obtained from exchangeable bonds will be fully exempt from Corporate Income Tax;
- (ii) Investment Funds – interest received by an Investment Fund is subject to a reduced rate of 20 per cent.; capital gains obtained by an Investment Fund from the disposal of exchangeable bonds are subject to a reduced tax rate of 10 per cent.;

- (iii) Private Equity Funds (“Fundos de Capital de Risco”) incorporated under the Portuguese law – according to section 22-A of EBF, income obtained from exchangeable bonds will be fully exempt from Corporate Income Tax.

Tax treatment of exchangeable bonds held by Individuals resident in Portugal

Interest received by resident individuals is subject to Portuguese personal income tax at progressive rates up to a maximum rate of 42 per cent.. These payments are in general not subject to Portuguese withholding tax except when the payment of the interests is made through a Portuguese resident entity. In this case, payments are subject to a withholding tax at a current final rate of 20 per cent., unless an option for aggregation is made by the tax payer.

Capital gains obtained by resident individuals from the disposal of exchangeable bonds are not subject to taxation in Portugal.

Tax treatment of dividends/gains on ordinary shares

Tax treatment of dividends/gains on ordinary shares held by individuals resident in Portugal

Dividends taxation

Dividends are, generally, subject to a withholding tax rate of 20 per cent., which is a final withholding, unless an option for aggregation is made in which case the amount to be included should only correspond to 50 per cent. of the total dividends received and the tax withheld at source is deemed as a payment in advance.

Capital Gains taxation

Gains obtained by an individual resident in Portugal on the disposal of shares are subject to taxation at a special tax rate of 10 per cent. when shares are held for a period less than 12 months.

If shares are held for a period that exceeds 12 months, gains obtained on its disposal are not subject to taxation in Portugal.

Tax treatment of dividends/gains on ordinary shares held by corporates resident in Portugal

Dividends taxation

If the shareholder holds a participation (i) of 10 per cent. or more of the company or (ii) of an acquisition price higher than € 20,000,000.00, it is entitled to fully deduct dividends received from this shareholding. In this case, payment of dividends is not subject to withholding at source.

If these conditions are not verified, the beneficiary of the dividends is entitled to deduct only 50 per cent. of the dividends received. In this case, dividends are subject to a withholding at source at a rate of 20 per cent. and the tax withheld at source is deemed as a payment in advance.

If the beneficiary of the dividends is a Portuguese SGPS or a Portuguese SCR, dividends received will be fully deductible from the respective taxable income, independently of the percentage held and/or of the acquisition price. If this is the case, dividends are not subject to withholding at source.

If the beneficiary of the dividends is a Pension Funds, dividends received are exempt from taxation and are consequently not subject to withholding at source when paid.

If the beneficiary is an Investment Fund, dividends will be subject to withholding at source at a definitive tax rate of 20 per cent.

If the beneficiary of the dividends is a Private Equity Fund, dividends received are exempt from taxation and consequently are not subject to withholding at source when paid.

Capital Gains Taxation

Gains obtained by a Corporation on the disposal of shares should be included in its taxable income and subject to a corporate tax rate of 25 per cent., plus a municipality surcharge of a maximum of 1.5 per cent., giving a combined tax rate of 26.5 per cent.

However, before the end of the second tax year subsequent to the sale of the shareholding, if the company reinvests the product of the sale in the acquisition of shares in other companies, in securities issued by the Portuguese State or in the acquisition of tangible fixed assets related to its

activity, then the company may only be able to integrate in its taxable income an amount corresponding to 50 per cent. of the gains obtained.

If the shareholder is a Portuguese SGPS or a Portuguese SCR, gains obtained from the disposal are exempt from taxation if the shares have been held for a period of 12 months or more, if the acquisition is made to an unrelated party. If the shares have been purchased by a related party, such exemption will only be applicable if the shares have been held for a period of at least three years. If these conditions (minimum holding period) are not met, the tax regime applicable to a SGPS is similar to the regime applicable to normal companies.

Gains obtained by a Pension Fund on the disposal of shares are exempt from taxation.

Gains obtained by an Investment Fund on the disposal of shares are subject to taxation at a special reduced tax rate of 10 per cent..

Gains obtained by a Private Equity Fund on the disposal of shares are exempt from taxation.

Tax treatment of dividends/gains on ordinary shares held by individuals non resident in Portugal

Dividends taxation

Dividends received by an individual non-resident in the Portuguese territory are subject to withholding tax in Portugal at a definitive tax rate of 20 per cent..

Capital gains taxation

Gains obtained buy an individual non-resident in Portugal on the disposal of shares of a Portuguese company are exempt from taxation in Portugal, except when those individuals are resident in a country, territory or region subject to a favourable tax regime included in a list approved by the Portuguese Ministry of Finance.

Tax treatment of dividends/gains on ordinary shares held by corporates non-resident in Portugal

Dividends taxation

Dividends paid to a non-resident corporation are subject to withholding at source in the Portuguese territory at the definitive tax rate of 20 per cent. This tax rate could be reduced if the beneficiary of the dividends is resident in a country with which Portugal has signed a Double Taxation Agreement (DTA).

If the beneficiary of the dividends is entitled to benefit from the Parent/Subsidiary Directive (90/435/CEE), which is already in force in Portugal, dividends will not be subject to withholding tax in Portugal.

Capital gains taxation

Gains obtained by a non-resident corporation on the disposal of shares of a Portuguese company are exempt from taxation in Portugal, except when:

- (i) 25 per cent. or more of the share capital of the non-resident entity is held, directly or indirectly, by a Portuguese resident entity; or
- (ii) the non-resident entity is domiciled in a country, territory or region subject to a more favourable tax regime; or
- (iii) the shares sold are representative of the share capital of a Portuguese company, at least 50 per cent. of the assets of which are made up from real estate properties located in Portuguese territory; or
- (iv) the Portuguese company is a SGPS and at least 50 per cent. of the assets of the target companies are made up of real estate properties located in the Portuguese territory.

Conversion of the Bonds

The acquisition of new shares upon conversion of the exchangeable bonds does not give rise to taxation on capital gains. The taxation will only occur on the subsequent transfer of the ordinary shares so acquired if the difference between the acquisition cost and the transfer price is positive.

EU Savings Directive

Under European Council Directive 2003/48/EC on the taxation of savings income, Member States are required to provide to the tax authorities of another Member State details of payments of interest (or similar income) paid by a person within its jurisdiction to an individual resident in that other Member State. However, for a transitional period, Belgium, Luxembourg and Austria are instead required (unless during that period they elect otherwise) to operate a withholding system in relation to such payments (the ending of such transitional period being dependent upon the conclusion of certain other agreements relating to information exchange with certain other countries).

SUBSCRIPTION AND SALE

Banco Espírito Santo de Investimento, S.A., Merrill Lynch International and Morgan Stanley & Co. International plc (the **Joint Lead Managers**) have, pursuant to a Subscription Agreement dated 3 July 2007 (the **Subscription Agreement**), agreed with the Issuer, subject to the satisfaction of certain conditions, to subscribe the Bonds on a several (but not joint) basis. The Issuer has agreed to pay certain costs and expenses in connection with the issue of the Bonds. The Subscription Agreement entitles the Joint Lead Managers to terminate it in certain circumstances prior to payment being made to the Issuer.

Each Keep Well Provider has agreed in the Subscription Agreement that, during the period of 90 days commencing on 3 July 2007, they will not, and the Issuer will procure that none of its subsidiaries will, without the prior written consent of the Joint Lead Managers (i) directly or indirectly, issue, offer, pledge, sell, contract to issue or sell, issue or sell any option or contract to purchase, purchase any option or contract to issue or sell, grant any option, right or warrant to purchase or otherwise transfer or dispose of, directly or indirectly, any Ordinary Shares or Relevant Securities or any securities convertible into or exercisable or exchangeable for Ordinary Shares or Relevant Securities or (ii) enter into any swap or any other agreement or any transaction that transfers, in whole or in part, directly or indirectly, any of the economic consequences of ownership of Ordinary Shares or Relevant Securities, whether any such swap or transaction described in paragraph (i) or (ii) above is to be settled by delivery of Ordinary Shares or Relevant Securities or such other securities, in cash or otherwise. The Subscription Agreement stipulates that the foregoing sentence shall not apply to (a) the issue of the Bonds or (b) any Ordinary Shares, securities, options, warrants or other rights or securities issued or delivered pursuant to the exchange of the Bonds or (c) the issue of Ordinary Shares pursuant to any options, warrants or other rights existing as at 3 July 2007 and described in this Offering Circular or (d) the issue of Ordinary Shares pursuant to any employee share schemes existing as at 3 July 2007 and described in this Offering Circular or (e) transactions entered in to pursuant to Portugal Telecom's Share BuyBack Programme as described herein. **Relevant Securities** means any participation certificates and any depositary or other receipt, instrument, rights or entitlement representing Ordinary Shares.

Selling Restrictions

General

No action has been or will be taken in any jurisdiction by any person that would permit a public offering of the Bonds, or possession or distribution of the Offering Circular or any other offering or publicity material relating to the Bonds, in any country or jurisdiction where action for that purpose is required.

United States

The Bonds and the Ordinary Shares have not been and will not be registered under the U.S. Securities Act of 1933, as amended (the **Securities Act**) and may not be offered or sold within the United States except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. The Bonds have not been nor will be offered or sold within the United States except in accordance with Rule 903 of Regulation S under the Securities Act. Accordingly, no person or its affiliates, or any persons acting on its or their behalf has engaged or should engage in any directed selling efforts with respect to the Bonds and the Ordinary Shares to be issued or delivered on exchange of the Bonds.

United Kingdom

Any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the **FSMA**)) in connection with the issue or sale of any Bonds has only been communicated or caused to be communicated and will only be communicated or caused to be communicated in circumstances in which section 21(1) of the FSMA does not apply to the Issuer.

In addition, anything done in relation to the Bonds in, from or otherwise involving the United Kingdom must be done in compliance with all applicable provisions of the FSMA.

Portugal

The offer of the Bonds has not been registered with the Portuguese Securities Market Commission (the **CMVM**). The Bonds have not been nor will be offered or sold in Portugal or to residents of Portugal otherwise than in accordance with applicable Portuguese Law.

No action has been or will be taken that would permit a public offering of any of the Bonds in Portugal. Accordingly, no Bonds may be offered, sold or delivered except in circumstances that will result in compliance with any applicable laws and regulations. In particular, no offer should be addressed to more than 100 non-qualified investors residing in Portugal or preceded or followed by promotion or solicitation to unidentified investors, or followed by publication of any promotional material. The offer of Bonds is intended for Qualified Investors only. Qualified Investors are expressly defined as including credit institutions, investment firms, insurance companies, collective investment schemes and the corresponding management companies, pension funds and pension fund management companies, other supervised financial institutions (including securitization funds and corresponding management companies and other financial companies, regulated venture capital companies and venture capital funds and corresponding management companies), financial institutions from non-EU countries that carry out similar activities, commodity dealers, national and regional governments, central banks, international and supranational institutions such as the International Monetary Fund, the European Central Bank, the European Investment Bank and other similar international organizations and other persons qualified as such by the Portuguese Securities Commission.

Purchase of Bonds and Stabilising Activities

The Bonds are a new issue of securities with no established trading market. Accordingly, the Issuer cannot assure the liquidity of the trading market for the Bonds.

Purchasers who purchase Bonds from the Joint Lead Managers may be required to pay stamp taxes and other charges in accordance with the laws and practices of the country of purchase in addition to the Issue Price set out on the cover page of this Offering Circular.

In connection with the offering of the Bonds, the Joint Lead Managers are permitted to engage in certain transactions that stabilise the price of the Ordinary Shares or the price of the Bonds. These transactions may consist of bids or purchases for the purpose of pegging, fixing or maintaining the price of the Ordinary Shares or the price of the Bonds.

In addition, if the Joint Lead Managers over-allot by selling more Bonds than are set out on the cover page of this Offering Circular, and thereby create a short position in the Bonds in connection with the offering, the Joint Lead Managers may reduce that short position by purchasing Bonds in the open market.

In general, purchases of a security for the purpose of stabilising or reducing a syndicate short position could cause the price of the security to be higher than it might otherwise be in the absence of such purchases.

Neither the Issuer nor the Joint Lead Managers makes any representation or prediction as to the direction or magnitude of any effect that the transaction described above may have on the price of the Ordinary Shares or the price of the Bonds. In addition, none of the Issuer or the Joint Lead Managers makes any representation that the Joint Lead Managers will engage in such transactions or that such transactions will not be discounted without notice, once they are commenced.

From time to time, the Joint Lead Managers and their respective affiliates have or may have provided, and may continue to provide, investment banking services to members of the Group for which they have been or will be paid customary fees.

In connection with the offering of the Bonds, the Joint Lead Managers and/or their respective affiliates may act as investors for their own account and may take up Bonds in the offering and in that capacity may retain, purchase or sell for their own account such securities and any securities of the Issuer or related investments and may offer or sell such securities or other investments otherwise than in connection with the offering. Accordingly, references herein to the Bonds being offered or

placed should be read as including any offering or placement of Bonds to the Joint Lead Managers and/or their respective affiliates acting in such capacity. Such persons do not intend to disclose the extent of any such investment or transactions otherwise than in accordance with any legal or regulatory obligation to do so.

GENERAL INFORMATION

1. The creation and issue of the Bonds will be authorised by a written resolution of the Board of Managing Directors of the Issuer dated on or prior to 28 August 2007 and the entering into of the Keep Well Agreements was duly authorised by the Executive Committee of Portugal Telecom dated 28 June, 2007 and the Board of Directors of PTC dated 2 July 2007 and will be authorised by a written resolution of the Board of Managing Directors of the Issuer dated on or prior to 28 August 2007.
2. Except as disclosed in this Offering Circular, there has been no significant change in the financial or trading position of each of Portugal Telecom, PTC and the Issuer or the Group since 30 June 2007, and no material adverse change in the financial position or prospects of each of Portugal Telecom, PTC and the Issuer or the Group since 31 December 2006.
3. Except as disclosed in this Offering Circular, neither Portugal Telecom, PTC, the Issuer nor the Group is or has been involved in any governmental, legal or arbitration proceedings (including any such proceedings which are pending or threatened of which Portugal Telecom, PTC or the Issuer is aware) in the 12 months preceding the date of this document which may have or have in such period had a significant effect on the financial position or profitability of Portugal Telecom, PTC, the Issuer or the Group.
4. The auditors of the Issuer are Deloitte Accountants B.V. The auditors are members of The Dutch Association of Certified Accountants (*Nederlands Instituut van Registeraccountants*). The auditors have audited the Issuer's accounts, without qualification, in accordance with generally accepted accounting principles in The Netherlands for the financial years ending 31 December 2005 and 31 December 2006, respectively. Deloitte Accountants B.V. have no material interest in the Issuer.
5. The auditors of Portugal Telecom are Deloitte & Associados, SROC S.A. The auditors are members of the Portuguese Institute of Statutory Auditors (Ordem dos Revisores Oficiais de Contas). The auditors have audited Portugal Telecom's accounts, without qualification, in accordance with IFRS, as adopted by the European Commission for use in the European Union, for the financial years ending 31 December 2005 and 31 December 2006, respectively. Deloitte & Associados, SROC S.A. have no material interest in the Issuer.
6. The auditors of PTC are Deloitte & Associados, SROC S.A. The auditors are members of the Portuguese Institute of Statutory Auditors (Ordem dos Revisores Oficiais de Contas). The auditors have audited PTC's accounts, without qualification, in accordance with generally accepted accounting principles in Portugal for the financial years ending 31 December 2005 and 31 December 2006, respectively. Deloitte & Associados, SROC S.A. have no material interest in the Issuer.
7. For so long as any Bonds are outstanding, executed copies of the following documents in respect of the Bonds will, when published, be available during usual business hours at the specified offices of the Principal Paying, Transfer and Exchange Agent:
 - (i) the Subscription Agreement;
 - (ii) the Trust Deed;
 - (iii) the Agency Agreement;
 - (iv) the constitutive documents of the Issuer, Portugal Telecom and PTC;
 - (v) the annual report of the Issuer for the financial years ended 31 December 2005 and 31 December 2006;
 - (vi) the annual report of Portugal Telecom for the financial years ended 31 December 2005 and 31 December 2006; and
 - (vii) the auditors report and audited annual financial statements of PTC for the financial years ended 31 December 2005 and 31 December 2006; and
 - (viii) the report on Form 20-F dated 29 June 2007 filed by Portugal Telecom with the Commission.

8. The yield to maturity of the Bonds is 4.125 per cent. per annum. The yield to maturity is calculated at the Issue Date on the basis of the initial issue price. It is not an indication of future yield.
9. The Bonds have been accepted for clearance through the Clearstream, Luxembourg and Euroclear systems with a Common Code of 030960084. The International Securities Identification Number for the Bonds is XS0309600848.

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