PORTUGAL TELECOM SGPS SA
Form 20-F
May 06, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

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

OR

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

For the fiscal year ended December 31, 2010

OR

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

OR

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

Commission file number 1-13758

PORTUGAL TELECOM, SGPS, S.A.

(Exact name of Registrant as specified in its charter)

The Portuguese Republic

(Jurisdiction of incorporation or organization)

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

(Address of principal executive offices)

Nuno Vieira, Investor Relations Director, Tel. +351 21 500 1701, Fax +351 21 500 0800
Av. Fontes Pereira de Melo, 40, 1069-300 Lisboa, Portugal

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

Title of each class	Name of each exchange on which registered
American Depositary Shares, each representing one ordinary share, nominal value €0.03 per share	New York Stock Exchange
Ordinary shares, nominal value €0.03 each	New York Stock Exchange*

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

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

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

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

Ordinary shares, nominal value €0.03 per share	896,512,000
Class A shares, nominal value €0.03 per share	500

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ý No o

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes o No ý

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o (Note: None required of the registrant)

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer ý Accelerated filer o Non-accelerated filer o Smaller reporting company o

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP o International Financial Reporting Standards as issued by the International Accounting Standards Board ý Other o

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. Item 17 o Item 18 ý

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No ý

TABLE OF CONTENTS

Table of Contents

CERTAIN DEFINED TERMS

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

PRESENTATION OF FINANCIAL INFORMATION

Our consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as endorsed by the EU ("EU-IFRS"). EU-IFRS may differ from IFRS as issued by the International Accounting Standards Board ("IASB") if, at any point in time, new or amended reporting standards have not been endorsed by the EU. At December 31, 2010, 2009 and 2008, there were no unendorsed standards effective as of and for the years ended December 31, 2010, 2009 and 2008, respectively, that affected our consolidated financial statements, and there was no difference between EU-IFRS and IFRS as issued by the IASB as applied by Portugal Telecom. Accordingly, our financial statements as of and for the years ended December 31, 2010, 2009 and 2008 are prepared in accordance with IFRS as issued by the IASB. IFRS comprise the accounting standards issued by the IASB and its predecessor body and interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") and its predecessor body.

We publish our financial statements in Euro, the single EU currency adopted by certain participating member countries of the European Union, including Portugal, as of January 1, 1999. Unless otherwise specified, references to "Euros," "EUR" or "€" are to the Euro. References herein to "U.S. dollars," "$" or "US$" are to United States dollars. References to "Real," "Reais" or "R$" are to Brazilian Reais. The Federal Reserve Bank of New York's noon buying rate in the City of New York for Euros was €0.6764 = US$1.00 on April 28, 2011, and the noon buying rate on that date for Reais was R$1.5870= US$1.00. We are not representing that the Euro, US$ or R$ amounts shown herein could have been or could be converted at any particular rate or at all. See "*Item 3 Key Information Exchange Rates*" for further information regarding the rates of exchange between Euros and U.S. dollars and between Reais and U.S. dollars.

We provided mobile telecommunications services in Brazil through Vivo Participações S.A. ("Vivo") through September 2010. We held our participation in Vivo through our 50% interest in Brasilcel N.V., a joint venture with Telefónica, S.A. On July 28, 2010, we reached an agreement with Telefónica for them to buy from us our 50% interest in Brasilcel N.V. We closed the transaction on September 27, 2010. Our consolidated statements of income and cash flows present Vivo under the caption "Discontinued Operations" for all periods presented, and our consolidated balance sheet as of December 31, 2010 no longer includes the assets and liabilities related to Vivo.

Table of Contents

FORWARD-LOOKING STATEMENTS

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

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

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

- material adverse changes in economic conditions in Portugal, Brazil or the other countries in which we have operations and investments;
- risks and uncertainties related to national and supranational regulation;
- increased competition resulting from further liberalization of the telecommunications sector in Portugal and Brazil;
- the development and marketing of new products and services and market acceptance of such products and services; and
- the adverse determination of disputes under litigation.

Table of Contents

PART I

ITEM 1 IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

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

ITEM 2 OFFER STATISTICS AND EXPECTED TIMETABLE

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

ITEM 3 KEY INFORMATION

Selected Consolidated Financial Data

The selected consolidated statement of financial position data as of January 1, 2009 and December 31, 2009 and 2010 and the selected consolidated statement of income and cash flow data for each of the years ended December 31, 2008, 2009 and 2010 have been derived from our audited consolidated financial statements included herein prepared in accordance with IFRS. The selected consolidated statement of financial position data as of December 31, 2006 and 2007 and the selected consolidated statement of income and cash flow data for the years then ended have been derived from our consolidated financial statements prepared in accordance with IFRS included in our Annual Report for the year ended December 31, 2008. The selected consolidated statement of financial position data as of December 31, 2008 and 2009 and the consolidated statement of income and cash flow data for the years ended December 31, 2006, 2007, 2008 and 2009 have been restated from that presented in the 2009 20-F in order to (i) present Vivo as a discontinued operation following the sale of that investment during 2010 (See Note 20 to our audited consolidated financial statements) and pursuant to the provisions of IFRS 5, *Non-current Assets Held for Sale and Discontinued Operactions*, and (ii) retrospectively reflects the adoption of IFRIC 12, *Service Concession Arrangements*, which became effective as of January 1, 2010, following its approval by the European Commission on March 25, 2009.

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

Given the sale on September 27, 2010 of our interest in Vivo to Telefónica, the selected consolidated statement of income for Vivo is presented under the caption "Discontinued Operations" for all periods through the completion of the sale, and the selected consolidated statement of financial

Table of Contents

position as of December 31, 2010 no longer includes the assets and liabilities related to Vivo, following the completion of the sale on September 27, 2010.

	Year Ended December 31,				
	2006	**2007**	**2008**	**2009**	**2010**
			(EUR Millions)		
Statement of Income Data(1):					
Continuing operations					
Revenues:					
Services rendered	3,498.6	3,530.0	3,503.4	3,492.0	3,516.0
Sales	174.5	187.7	217.7	197.2	165.6
Other revenues	33.0	32.8	40.1	44.3	60.6
Total revenues	**3,706.1**	**3,750.5**	**3,761.2**	**3,733.4**	**3,742.3**
Costs, expenses losses and income:					
Wages and salaries	531.9	523.7	489.4	546.7	637.1
Direct costs	476.0	478.9	520.8	522.4	547.6
Costs of products sold	195.5	206.7	244.8	207.3	179.9
Marketing and publicity	74.5	81.3	87.9	78.6	81.1
Supplies and external services	672.7	695.1	695.6	733.3	724.5
Indirect taxes	49.0	50.4	45.9	57.8	45.4
Provisions and adjustments	37.8	19.1	29.0	30.5	35.0
Depreciation and amortization	624.9	600.0	647.5	716.9	758.6
Net post retirement benefit costs (gains)	(72.1)	(65.1)	44.8	89.6	38.2
Curtailment and settlement costs	19.0	275.6	100.0	14.8	145.5
Gains on disposals of fixed assets, net	(2.7)	(8.5)	(18.3)	(2.0)	(5.5)
Other costs, net	58.9	42.7	22.6	45.6	141.2
Income before financial results and taxes	**1,040.8**	**850.6**	**851.3**	**691.9**	**413.8**
Minus: Financial costs (gains), net	(1.2)	(202.8)	32.4	(200.7)	81.6
Income before taxes	**1,042.0**	**1,053.3**	**818.9**	**892.6**	**332.2**
Minus: Income taxes	135.5	243.6	204.8	185.9	77.5
Net income from continuing operations	**906.4**	**809.8**	**614.1**	**706.7**	**254.6**
Discontinued operations					
Net income from discontinued operations	47.7	24.0	81.7	82.5	5,565.4
Net income	**954.1**	**833.8**	**695.8**	**789.2**	**5,820.1**
Attributable to non-controlling interests	87.4	92.8	119.7	104.5	147.9
Attributable to equity holders of the parent	**866.8**	**740.9**	**576.1**	**684.7**	**5,672.2**
Income before financial results and taxes per ordinary share, A share and ADS(2)	0.92	0.83	0.95	0.77	0.46
Earnings per share, A share and ADS:					
Basic(3)	0.78	0.71	0.64	0.78	6.48
Diluted(4)	0.73	0.67	0.62	0.76	6.06
Earnings per share, A share and ADS from continuing operations, net of non-controlling interests:					
Basic(3)	0.80	0.72	0.60	0.74	0.19
Diluted(4)	0.74	0.69	0.59	0.72	0.19
Cash dividends per ordinary share, A share and ADS(5)	0.475	0.575	0.575	0.575	2.30
Share capital	395.1	30.8	26.9	26.9	26.9

(1) As explained in Note 4 to our consolidated financial statements, we applied retropectively, from January 1, 2009, the interpretation IFRIC 12, *Service Concession Arrangements*, which became effective as from January 1, 2010, following its approval by the European Commission as at March 25, 2009. Consequently, our previously reported consolidated balance sheet data as of

Table of Contents

December 31, 2009 and consolidated income statement data for the year ended December 31, 2009 were restated in order to reflect the impact of the adoption of this interpretation.

(2)

Based on 1,128,856,500 ordinary and A shares issued as of December 31, 2006, 1,025,800,000 ordinary and A shares issued as of December 31, 2007 and 896,512,500 ordinary and A shares issued as of December 31, 2008, 2009 and 2010.

(3)

The weighted average number of shares for purposes of calculating basic earnings per share is computed based on the average ordinary and A shares issued and the average number of shares held by Portugal Telecom.

(4)

The weighted average number of shares for purposes of calculating diluted earnings per share is computed based on the average ordinary and A shares issued and the average number of shares held by Portugal Telecom adjusted by the number of shares from the exchangeable bonds issued on August 28, 2007 and from the exchangeable bonds issued on December 6, 2001 to December 6, 2006, when those bonds were repaid, in each case assuming the conversion of the bonds into ordinary shares.

(5)

Cash dividends per ordinary share, A share and ADS for the years ended December 31, 2006, 2007, 2008, 2009 and 2010 were €0.475, €0.575, €0.575, €0.575 and €2.30, respectively. Cash dividends per ordinary share, A share and ADS for the years ended December 31, 2006, 2007, 2008 and 2009 were US$0.64, US$0.90, US$0.78 and US$0.78, respectively. As mentioned in Note 22 to our audit consolidated financial statements, cash dividends for the year ended December 31, 2010 included (1) an extraordinary dividend per share of €1.65, of which €1.00 was paid in December 2010 and the remaining €0.65 will be paid in 2011 subject to approval at our Annual Shareholders' Meeting scheduled for May 6, 2011 and (2) an ordinary cash dividend of €0.65 per share, also subject to Annual Shareholders' Meeting approval.

	Year Ended December 31,				
	2006	**2007**	**2008**	**2009**	**2010**
			(EUR Millions)		
Cash Flow Data:					
Cash flows from operating activities	1,821.7	1,859.2	1,828.9	1,927.5	1,506.9
Cash flows from investing activities	1,136.7	235.9	(108.7)	(597.8)	4,072.4
Cash flows from financing activities	(3,015.4)	(1,953.6)	(1,283.8)	(997.3)	(1,929.1)

Table of Contents

	As of December 31,				
	2006	2007	2008	2009	2010
			(EUR Millions)		
Statement of Financial Position Data(1):					
Current assets	3,998.7	3,816.3	3,317.0	3,699.1	8,855.4
Investments in group companies	499.1	538.1	613.2	597.2	361.5
Other investments	132.4	27.2	21.1	16.9	17.7
Tangible assets	3,942.0	3,585.4	4,621.5	4,843.9	3,874.6
Intangible assets	3,490.9	3,383.1	3,486.2	4,074.3	1,111.7
Post retirement benefits	134.1	134.1	1.6	67.6	1.9
Deferred tax assets	1,166.0	992.2	1,032.7	1,019.5	653.1
Other non-current assets	807.1	645.1	628.0	522.1	294.0
Total assets	**14,170.2**	**13,121.5**	**13,721.2**	**14,840.5**	**15,169.9**
Current liabilities	3,884.6	3,862.2	5,153.6	3,398.4	2,683.7
Medium and long term debt	4,467.5	4,960.7	4,441.2	6,551.5	6,254.4
Accrued post retirement liability	1,807.6	1,463.9	1,836.9	1,558.3	968.8
Deferred tax liabilities	90.4	84.9	462.2	483.1	311.6
Other non-current liabilities	811.3	666.2	631.1	461.7	342.3
Total liabilities	**11,061.4**	**11,037.9**	**12,525.0**	**12,453.0**	**10,560.8**
Equity excluding non-controlling interests	2,258.0	1,340.1	232.0	1,318.3	4,392.4
Non-controlling interests	850.8	743.6	964.2	1,069.1	216.7
Total equity	**3,108.8**	**2,083.6**	**1,196.2**	**2,387.4**	**4,609.1**
Total liabilities and shareholders' equity	**14,170.2**	**13,121.5**	**13,721.2**	**14,840.5**	**15,169.9**
Number of ordinary shares	1,128.9	1,025.8	896.5	896.5	896.5
Share capital(2)	395.1	30.8	26.9	26.9	26.9

(1) As explained in Note 4 to our consolidated financial statements, we retrospectively applied IFRIC 12, *Service Concession Arrangements*, which became effective as from January 1, 2010, following its approval by the European Commission on March 25, 2009. Consequently, our previously reported consolidated statement of financial position data as of December 31, 2008 and 2009 and consolidated income statement data for the year ended December 31, 2009 were restated in order to reflect the impact of the adoption of this interpretation.

(2) As of the dates indicated, we did not have any redeemable preferred stock.

Exchange Rates

Euro

The majority of our revenues, assets, liabilities and expenses are denominated in Euros. We have published our audited consolidated financial statements in Euros, and our shares trade in Euros on the regulated market Euronext Lisbon. Our financial results could be affected by exchange rate fluctuations in the Brazilian Real. See "*Item 5 Operating and Financial Review and Prospects Exchange Rate Exposure to the Brazilian Real*."

Our dividends, when paid in cash, are denominated in Euros. As a result, exchange rate fluctuations have affected and will affect the U.S. dollar amounts received by holders of ADSs on conversion of such dividends by The Bank of New York, as the ADS depositary. The Bank of

New York converts dividends it receives in foreign currency into U.S. dollars upon receipt, by sale or such other manner as it has determined and distributes such U.S. dollars to holders of ADSs, net of The

Table of Contents

Bank of New York's expenses of conversion, any applicable taxes and other governmental charges. Exchange rate fluctuations may also affect the U.S. dollar price of the ADSs on the New York Stock Exchange.

The following tables show, for the period and dates indicated, certain information regarding the U.S. dollar/Euro exchange rate. The information is based on the noon buying rate in the City of New York for cable transfers in Euro. On April 28, 2011, the Euro/U.S. dollar exchange rate was €0.6764 per US$1.00.

Year ended December 31,	Average Rate(1)
	(EUR per US$1.00)
2006	0.7898
2007	0.7248
2008	0.6805
2009	0.7166
2010	0.7567

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

Period	High	Low
	(EUR per US$1.00)	
October 2010	0.7306	0.7109
November 2010	0.7671	0.7030
December 2010	0.7640	0.7465
January 2011	0.7726	0.7291
February 2011	0.7422	0.7250
March 2011	0.7240	0.7036
April 2011 (through April 28, 2011)	0.7037	0.6745

None of the 27 member countries of the European Union has imposed any exchange controls on the Euro.

Brazilian Real

Although as of December 31, 2010, the majority of our revenues, assets and expenses are denominated in Euros, on January 26, 2011, we announced that we had entered into a strategic partnership with Telemar Participações S.A. and its subsidiaries (collectively, "Oi"), the Brazilian telecommunications company. On March 28, 2011, we completed the acquisition of an economic interest of 25.6% in Telemar Participações S.A. and 25.3% in Telemar Norte Leste S.A. We will have a role in the management of Oi and, as a result, will proportionally consolidate the results of operations of Oi in our results of operations. Oi records its financial position and results of operations in Brazilian Reais. In addition, our other Brazilian investments are Brazilian companies that similarly record their financial position and results of operations in Brazilian Reais. Consequently, exchange rate fluctuations between the Euro and the Brazilian Real will affect our revenues in future periods.

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

The following tables show, for the periods and date indicated, certain information regarding the Real/U.S. dollar exchange rate. On April 28, 2011, the Real/U.S. dollar exchange rate was R$1.5870 per US$1.00. The information is based on the noon buying rate in the City of New York for cable transfers

Table of Contents

in Brazilian Reais as certified for United States customs purposes by the Federal Reserve Bank of New York.

Year ended December 31,	**Average Rate(1)**
	(R$ per US$1.00)
2006	2.164
2007	1.929
2008	1.831
2009	1.987
2010	1.757

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

Period	**High**	**Low**
	(R$ per US$1.00)	
October 2010	1.716	1.657
November 2010	1.738	1.679
December 2010	1.718	1.663
January 2011	1.692	1.645
February 2011	1.678	1.660
March 2011	1.673	1.627
April 2011 (through April 28, 2011)	1.616	1.564

Risk Factors

General Risks Relating to Our Company

The current economic and financial crisis has affected, and will likely continue to affect, demand for our products and services, our revenues and our profitability

The global economic and financial crisis, and the current economic recession in Portugal, have had, and are likely to continue to have, an adverse effect on the demand for our products and services and on our revenues and profitability. Recent economic rescue packages for Greece and Ireland, Portugal's recent request for an economic rescue package, and continuing concerns regarding the possibility of sovereign debt defaults by other European Union member countries, affected access to funding by certain European governments, corporations and the financial sector, and dampened investor confidence. These concerns and concerns about continuing budget deficits in Portugal have required the Portuguese government to implement severe budget-cutting measures that could delay emergence from the recession and may weaken consumer demand.

Against this backdrop, the Fitch credit rating agency downgraded Portugal's sovereing debt from A+ to A-, and Standard & Poor's downgraded it from A- to BBB. Standard & Poor's further downgraded Portugal's sovereign debt from BBB to BBB-. On April 1, 2011, Fitch further downgraded Portugal's sovereign debt from A- to BBB- and Moody's Investors Service, Inc. downgraded Portugal's sovereign debt from A3 to Baa1.

On April 6, 2011, Portugal announced that it would seek an economic rescue package from the European Union. Since that date, Portugal has formally requested an economic rescue package from the European Union and the International Monetary Fund and has begun negotiating the terms of that package.

As one of Portugal's largest companies and one of its largest employers, Portugal Telecom's financial condition, revenues and profitability are closely linked to circumstances in the Portuguese economy. The recession in Portugal has had a direct effect on demand for our products and services, contributing to a decline in our mobile revenues and, to a lesser degree, our wireline revenues, in 2010.

We must maintain liquidity to fund our working capital, service our outstanding indebtedness and finance investment opportunities. Without sufficient liquidity, we could be forced to curtail our investments, or we may not be able to pursue new business opportunities. The principal sources of our liquidity are cash generated from our operations and equity and debt financing. Cash generated from operations is driven by our revenues and net income, which could be adversely affected by the economic crisis.

Also, notwithstanding our recent debt issuances that took place in 2011, we may be unable to access the equity or debt markets to obtain additional financing or to refinance existing indebtedness. We discuss our liquidity and sources of funding in "*Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources*."

In these and other ways, the global economic and financial crisis and its effect on the European and Portuguese economies has significantly affected, and could continue to significantly affect, our business, liquidity and financial performance.

Financial market conditions may adversely affect our ability to obtain financing, significantly increase our cost of debt and negatively impact the fair value of our assets and liabilities

Beginning in 2008, events in the global and European financial markets have increased the uncertainty and volatility of the financial markets, leading to a significant increase in execution and price risks in financing activities. Global financial markets and economic conditions were severely disrupted and volatile in 2008 and 2009 and remain subject to significant vulnerabilities, such as the

Table of Contents

deterioration of fiscal balances and the rapid accumulation of public debt, continued deleveraging in the banking sector and limited supply of credit. Credit markets and the debt and equity capital markets were exceedingly distressed in 2008 and 2009 and remained challenged in 2010. In 2010, the financial markets grew increasingly concerned about the ability of certain European countries, particularly Greece, Ireland and Portugal, but also others such as Spain and Italy, to finance their deficits and service growing debt burdens amidst difficult economic conditions. This loss of confidence has led to rescue measures for Greece, Ireland and now Portugal by the European Union and the International Monetary Fund. These issues, along with the re-pricing of credit risk and the difficulties currently experienced by financial institutions have made it difficult, and will likely continue to make it difficult, for companies to obtain financing.

As a result of the disruptions in the credit markets, many lenders have increased interest rates, enacted tighter lending standards, required more restrictive terms (including higher collateral ratios for advances, shorter maturities and smaller loan amounts) or refused to refinance existing debt at all or on terms similar to pre-crisis conditions. Changes in interest rates and exchange rates may also adversely affect the fair value of our assets and liabilities. If there is a negative impact on the fair values of our assets and liabilities, we could be required to record impairment charges.

Notwithstanding our international exposure and diversification, the recent downgrades of Portugal's sovereign debt described in the preceding risk factor may have a significant effect on our costs of financing, particularly given the size and prominence of our company within the Portuguese economy. The recent events in Portugal and the other factors described above could adversely affect our ability to obtain future financing to fund our operations and capital needs and adversely impact the pricing terms that we are able to obtain in any new bank financing or issuance of debt securities and thereby negatively impact our liquidity.

Any future ratings downgrades may impair our ability to obtain financing and may significantly increase our cost of debt

The effects of the economic and financial crisis described above, or any adverse developments in our business, could lead to downgrades in our credit ratings. Any such downgrades are likely to adversely affect our ability to obtain future financing to fund our operations and capital needs. Any downgrade of our ratings could have even more significant effects on our ability to obtain financing and therefore on our liquidity. For example, the pricing conditions applicable to our commercial paper programs could be revised in the event our credit rating is changed. In addition, certain of our loan agreements, totaling €183 million as of December 31, 2010, contain provisions that require us to provide certain guarantees if our ratings decline below specified levels. Any failure to provide those guarantees could enable the lender to accelerate the loans. For further information on these covenants, please refer to "*Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources Indebtedness Covenants*."

We may not be able to pay our announced dividends

In connection with the sale of our interest in Vivo in September 2010, we announced an extraordinary dividend to our shareholders of €1.65 per share, of which we paid €1.00 per share on December 28, 2010. Subject to the approval of our next General Shareholders' Meeting, we expect to pay the remaining €0.65 per share of this dividend, as well as an ordinary dividend of €0.65 per share with respect to the years ended December 31, 2010 and 2011, following the respective General Shareholders' Meetings. In addition, in November 2010, we announced that our Board of Directors intends to propose to the General Shareholders' Meeting that we adopt a progressive dividend policy with the objective of raising the dividend per share every year between 3% and 5% for the period between 2012 and 2014. Furthermore, for fiscal year 2011 onwards, the Board of Directors has its intention to approve the payment of an interim ordinary dividend based on the financial performance of our company, in order to allow for a smoother cash return to our shareholders throughout the year. The exceptional cash dividend and the remuneration package proposal are subject to market conditions, our financial condition, applicable law regarding the distribution of net income, including additional shareholder approvals, and other factors considered relevant by our Board of Directors at the time.

The payment of future dividends will depend on our ability to continue to generate cash flow in our businesses, which is dependent not only on our revenue stream but also on our ability to further streamline our operations and reduce our costs. In addition, significant volatility in the Real/Euro exchange rate may impair our ability to pay dividends. The Real has fluctuated significantly in relation to the Euro in recent years and has worked in our favor, but we cannot guarantee that this trend will continue going forward.

If any of the conditions described above proves not to be the case or if any other circumstances (including any risks described in this "Risk Factors" section) impede our ability to generate cash and distributable reserves, shareholders may not receive the full remuneration we have announced, and the price of our ordinary shares and ADSs could be negatively affected.

Unfunded post retirement benefit obligations may put us at a disadvantage to our competitors and could adversely affect our financial performance

We have unfunded post retirement benefit obligations that may limit our future use and availability of capital and adversely affect our financial and operating results. Although in December 2010, we transferred to the Portuguese Government the post retirement benefits obligations relating to regulated pensions of Caixa Geral de Aposentações and Marconi, we retained all other obligations, including (1) salaries to suspended and pre-retired employees amounting to €924.3 million as of December 31, 2010, which we must pay monthly directly to the beneficiaries until their retirement age and (2) €472.4 million in obligations related to pension supplements and healthcare as of December 31, 2010, which are backed by plan assets with a market value of €448.1 million, resulting in unfunded obligations of €24.3 million.

Any decrease in the market value of our plan assets relating to our pension supplements and healthcare obligations could increase our unfunded position. Although there is in place an investment policy with capital preservation targets, in the current economic and financial crisis, in particular, the market value of our plan assets is volatile and poses a risk. In addition, our obligations to pay salaries to suspended and pre-retired employees are unfunded. The value of the obligations referred to above, namely the ones related to pension supplements and healthcare, may also fluctuate, depending on demographic and financial factors that are beyond our control. Any significant increase in our unfunded obligations could adversely affect our ability to raise capital, require us to use cash flows that we would otherwise use for capital investments, implementing our strategy or other purposes and adversely affect perceptions of our overall financial strength, which could negatively affect the price of our ordinary shares and ADRs.

See "*Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources Post Retirement Obligations*" for a description of our transfer of pension obligations to the Portuguese Government.

Table of Contents

The Portuguese Government holds all of our A shares, which afford it special approval rights

All of our 500 A shares are held by the Portuguese Government. Under our articles of association, the holders of our A shares, voting as a class, may veto a number of actions of our shareholders, including the following:

- election of the chairman of the Audit Committee and the statutory auditor (See "*Item 10 Additional Information Corporate Governance New Corporate Governance Model*"), as well as the members of the board of the General Meeting of Shareholders;
- authorization for a dividend exceeding 40% of our distributable net income per year;
- capital increases and other amendments to our articles of association, as well as the limitation or suppression of pre-emptive rights;
- issuance of bonds and other securities;
- authorization of a shareholder that performs an activity competing with us to hold more than 10% of our ordinary shares;
- approval of the general goals and fundamental principles of our policies; and
- definition of our investment policies, including any requirements for the authorization of acquisitions and transfers of shareholdings.

Additionally, the election of one-third of the Directors, including the Chairman of the Board of Directors, must be approved by the Portuguese Government, as the holder of all the A shares.

Our articles of association state that, among the members of the Executive Committee appointed by the Board of Directors, at least one or two appointed directors out of the Executive Committee of five or seven members must be elected pursuant to the election rule described in the preceding paragraph.

On July 8, 2010, the European Court of Justice ruled that the Portuguese Government's ownership of our A shares is illegal under European law. See "*Item 8 Financial Information Legal Proceedings Regulatory Proceedings*."

Risks Relating to Our Portuguese Operations

Intense competition has significantly affected, and is expected to continue to significantly affect, our revenues and our results of operations

Competition from mobile telephony and from other wireline operators has reduced our wireline revenues and could continue to adversely affect our revenues. During 2010, approximately 47.2% of our consolidated revenues were derived from services provided by our wireline services in Portugal, as compared to 48.1% in 2009. 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, we have experienced, and may continue to experience, erosion of market share of both access lines and of outgoing domestic and international traffic. The number of active mobile telephone cards in Portugal has overtaken the number of wireline main lines. Some of our wireline customers are using mobile services as an alternative to wireline telephone services. Mobile operators can bypass our international wireline network by interconnecting directly with wireline and mobile networks either in our domestic network or abroad. Competition is also forcing down the prices of our wireline telephone services for long distance and international calls. Lowering our international call prices has caused a decline in our revenues from international wireline telephone services. The decrease in wireline traffic and lower tariffs resulting from competition has significantly affected our overall revenues, and we expect these

factors to continue to negatively affect our revenues. See "*Item 4 Information on the Company Competition Competition Facing our Wireline Business*."

Increased competition in the Portuguese mobile markets may result in decreased tariffs and loss of market share. We operate in the highly competitive Portuguese mobile telecommunications market. We believe that our existing mobile competitors, Vodafone and Optimus will continue to market their services aggressively. After we launched our low-cost brand "Uzo," for example, Vodafone and Optimus quickly responded with similar products of their own. As another example, in 2010, we launched a tribal plan as a reaction to similar plans launched by our competitors, and that plan provides for lower revenue per user than many of our other plans.

In 2007, CTT, the Portuguese postal company, launched a mobile virtual network operator, or "MVNO," operation supported by TMN's network. MVNOs do not have their own network infrastructure and thus do not have the fixed cost burdens facing our current GSM (Global System for Mobile Communications) and UMTS (Universal Mobile Telecommunications System) services. In 2008, ZON Multimedia ("ZON") launched an MVNO under the brand "ZON Mobile" after signing an agreement with Vodafone Portugal to operate using its mobile network.

We expect competition from VoIP-based operators also to place increasing price pressure on voice tariffs and lead to reductions in mobile voice traffic. Competition from companies providing wireless local-area network, or "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 prospect of LTE (Long Term Evolution) services may cause a disruption in the mobile data and voice markets, posing additional threats to and impairing TMN's current competitive position. See "*Item 4 Information on the Company Competition Competition Facing TMN*."

The broadband market in Portugal is highly competitive and may become more competitive in the future. Our competitors have been improving their commercial offers in broadband Internet, with most of them offering triple-play bundled packages (voice telephony, broadband Internet and Pay-TV subscription). We believe that with competition in Internet broadband access intensifying, and with the development of existing technologies such as broadband wireless access, mobile broadband through UMTS, and high speed broadband supported by the deployment of a fiber optic network, we may face additional pricing pressure on our services, which could result in the loss of revenues.

Increased competition in the Portuguese Pay-TV market may result in a decrease in our revenues. In 2008, we launched a nationwide Pay-TV service under the *Meo* brand, primarily using our fixed network (IPTV over ADSL2+ and fiber-to-the-home ("FTTH") and DTH satellite technology). This service required us to make significant investments in our network in order to increase the bandwidth and offer a better service quality than our competitors. The main competitors in the market are ZON, Cabovisão, Optimus and Vodafone. Notwithstanding the increase in our revenues from Pay-TV services in recent years, we have experienced pressure from our competitors to reduce monthly subscription fees. In addition, our efforts to build scale to enable us to negotiate better programming costs with our content suppliers, especially certain premium content owned by one of our competitors, may not prove successful. Our wireline revenues and financial position could be significantly affected if we are not successful in the Pay-TV business, which is becoming increasingly important as a retention tool of our fixed-line and broadband customers.

An adverse regulatory environment may negatively affect our profitability

Reduced interconnection rates have negatively affected our revenues for our mobile and wireline businesses and will continue to do so in 2011. In recent years, ANACOM has imposed price controls on interconnection rates for the termination of calls on mobile networks. These reductions have had a

Table of Contents

significant impact on interconnection revenues of our mobile subsidiary, TMN Telecomunicações Móveis Nacionais, S.A. ("TMN"), and consequently its earnings.

In January 2010, ANACOM issued a draft decision regarding fees for the termination of calls on mobile networks, proposing to reduce them to €0.035 by April 1, 2011. In May 2010, ANACOM imposed a new glide path that would reduce mobile termination rates by €0.005 per quarter, to reach €0.035 in August 2011. These new rates will have a negative effect on our cash flows.

In 2008, the European Commission started a public consultation process for its draft recommendation on voice calls termination rates (both in mobile and fixed networks), which are intended to harmonize regulation and drive down termination rates even further across all EU countries starting in 2012. This recommendation was published in 2009 and is expected to have a negative effect on our future revenues. ANACOM is currently consulting on the definition of a bottom-up long-run incremental cost (LRIC) cost model to regulate mobile termination rates. The expectation is that mobile termination rates will fall into the interval between 1.5 and 3.0 eurocents by the end of 2012.

In addition, in August 2008, ANACOM published a "reasoning" regarding mobile rates for originating calls, aimed at driving mobile operators to reducing their prices by the end of September 2008 to a level equal or close to the level of mobile termination rates. In the second half of 2008, the three mobile operators reduced their rates for originating calls but not to the extent desired by ANACOM. In February 2010, ANACOM chose to take the matter to the Portuguese national competition authority ("Autoridade da Concorrência"). Although we cannot predict the outcome of this process, ANACOM's actions could negatively impact our revenues and results of operations.

ANACOM's price controls on fixed-to-mobile interconnection may also negatively affect our wireline retail revenues because we are required to reflect the reduction in these interconnection charges in our retail prices for calls from our fixed line network. We expect that the reduction in interconnection charges will continue to have an impact on our wireline retail revenues.

In addition, the lower interconnection rates have reduced revenues for our wholesale wireline business, which records revenue from incoming calls transiting through our network that terminate on the networks of mobile operators. The prices we charge to international operators (and hence our revenues) also depend on the interconnection fees charged by mobile operators for international incoming calls terminating on their networks, and these fees have been decreasing. We expect that lower interconnection rates will continue to have a negative impact on our wholesale wireline revenues.

ANACOM also issued a decision in 2006 requiring our wireline business to offer capacity-based interconnection rates (a flat-rate interconnection tariff), which had a negative effect on our wholesale wireline revenues in 2007 and 2008.

The European Commission's review of roaming charges may lead to a reduction in mobile revenues. The European Commission has determined that roaming prices in Europe should be reduced and has published new regulations that have been effective since 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 €0.26 per minute currently applies. In the retail market, maximum roaming charges of €0.19 per minute (for received calls) and €0.43 per minute (for outgoing calls) currently apply.

In 2008, the European Commission launched a new consultation on roaming, proposing to carry over Regulation (EC) No. 717/2007, on roaming on mobile communications networks within the community (the "Roaming Regulation"), beyond 2010 and to extend it to data and Short Messaging Services ("SMS"), or text messaging. In 2009, Regulation (EC) No. 544/2009, amending the Roaming Regulation (the "New Roaming Regulation") went into effect, limiting roaming charges. The European

Commission expects the New Roaming Regulation to reduce roaming charges by up to 60%. The European Commission also requested clarification from operators with respect to price differences between data services while roaming compared to prices in the domestic market.

Under the New Roaming Regulation, voice roaming rates in the retail market continue to be subject to a glide path (prices excluding VAT): from July 1, 2010, maximum rates of €0.39 per minute for outgoing and €0.15 per minute for incoming roaming calls; and from July 1, 2011, maximum rates of €0.35 per minute for outgoing and €0.11 per minute for incoming roaming calls. In the wholesale market, maximum rates are €0.22 and €0.18 as of July 1, 2010 and July 1, 2011, respectively. For SMS services, caps of €0.11 in the retail and of €0.04 in the wholesale came into force on July 1, 2009. For data services, maximum wholesale rates of €0.80 and €0.50 apply from July 1, 2010 and July 1, 2011, respectively.

These regulations have had, and will continue to have, an adverse effect on the revenues of our mobile business and on our company as a whole.

Burdensome regulation in an open market may put us at a disadvantage to our competitors and could adversely affect our business. The Portuguese electronic communications sector is fully open to competition. However, many regulatory restrictions and obligations are still imposed on us. In the previous round of market analysis, carried out in 2004-2006, the Portugal Telecom group was found by ANACOM to have significant market power in all but one of the 16 markets analyzed 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. Pursuant to the European Relevant Markets recommendation that significantly reduced the number of markets subject to regulation, ANACOM determined the regulatory obligations that should be imposed on operators with significant market power in the provision of wholesale (physical) network infrastructure access and wholesale broadband access. In the case of wholesale broadband access, ANACOM alleviated regulatory obligations in 184 areas considered to be competitive, which represented 61% of broadband accesses. During 2011, ANACOM intends to revise markets numbers 4 and 5 to integrate the changes due to the development of Next Generation Networks. There is a risk that ANACOM may reduce the number of areas where it had alleviated regulatory obligations and impose additional regulatory obligations on our fiber network. The substantial resources we must commit to fulfill the remaining obligations could adversely affect our ability to compete. See "*Item 4 Information on the Company Regulation Portugal*."

The Portuguese government could terminate or fail to renew our wireline concession, our licenses and our authorization for data and mobile services. We provide a significant number of services under a concession granted to us by the Portuguese government and under licenses and authorizations granted to us by ANACOM. See "*Item 4 Information on the Company Regulation Portugal*." The concession runs until 2025, but the Portuguese government can revoke the concession if it considers the revocation to be in the public interest. It can also terminate our concession at any time if we fail to comply with our obligations under the concession. Even if the concession remains in force, its terms and conditions could be materially affected by the outcome of a public consultation process by the Portuguese government relating to the provision of universal service, which is expected to begin during 2011. A tender for the designation of the Universal Service Provider(s) is also expected during 2011. The Portuguese government can also terminate our licenses under certain circumstances. Through TMN, we hold a renewable, non-exclusive license to provide GSM digital mobile telephone services throughout Portugal, valid until 2022 and a renewable, non-exclusive license to provide UMTS mobile telephone services throughout Portugal, valid until 2016. If the Portuguese government took such actions, we would not be able to conduct the activities authorized by the concession or the relevant licenses. This loss would eliminate an important source of our revenues.

Table of Contents

In July 2010, ANACOM decided, within the context of the 900/1800 MHz spectrum "refarming" process (a change to the conditions of use of that frequency range), to unify into a single title the conditions applicable to the rights of use of frequencies allocated to TMN for the provision of the land mobile service, in accordance with GSM 900/1800 and UMTS technologies. The authorization is valid until July 8, 2025.

During 2011, ANACOM intends to launch an auction for allocation of rights of use of frequencies in the 450, 800, 900, 1800 MHz and 2.1 and 2.6 GHz bands. These frequencies allow the provision of electronic communications services and could be used to implement 4G mobile solutions. However, we may face the risk of not being granted rights of use in those frequency bands. This loss would have negative impact on our ability to implement new mobile technologies, the existing mobile infrastructures, provide innovative services and develop new sources of revenue.

Regulatory investigations and litigation may lead to fines or other penalties

We are regularly involved in litigation, regulatory inquiries and investigations involving our operations. ANACOM, the European Commission and the Autoridade da Concorrência (the Portuguese national competition authority) can make inquiries and conduct investigations concerning our compliance with applicable laws and regulations. Current inquiries and investigations include several complaints before the Autoridade da Concorrência related to alleged anti-competitive practices in our wireline business. These inquiries and investigations are described in "*Item 8 Financial Information Legal Proceedings*."

On January 19, 2011, the European Commission opened an investigation into an agreement between Telefónica and Portugal Telecom allegedly not to compete in the Iberian telecommunications markets. Portugal Telecom has developed various strategic partnerships with Telefónica in recent years. Although we do not believe the existence of these partnerships has impeded competition and ordinary activities of our company and Telefónica, our relationship with Telefónica is now subject to investigation. The European Commission has stated that the initiation of proceedings does not imply that the Commission has conclusive proof of an infringement but that the Commission will deal with the case as a matter of priority. We cannot predict whether this investigation may lead to fines or other sanctions or whether it may have an adverse effect on our business.

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

Risks Related to Our International Operations

Although Telefónica S.A. acquired our interest in Vivo, the Brazilian telecommunications company, on September 27, 2010, we announced on July 28, 2010 that we intended to enter into a strategic partnership with Telemar Participações S.A. ("TmarPart") and its subsidiaries (collectively, "Oi"), the Brazilian telecommunications company. On January 26, 2011, we announced that we had signed definitive documents relating to the transaction, and on March 28, 2011, we completed the acquisition of a 25.6% economic interest in TmarPart and of a 25.3% economic interest in Telemar Norte Leste S.A. We will have a role in the management of Oi and, as a result, will proportionally consolidate the results of operations of Oi in our results of operations. Consequently, the risks described below relating to the Brazil and the Brazilian telecommunications markets will continue to be relevant to our business. Additional risk factors that are specific to Oi are set forth below under " Risks Related to our Strategic Partnership with Oi."

Table of Contents

We are exposed to exchange rate and interest rate fluctuations

We are exposed to exchange rate fluctuation risks, mainly due to our significant investments in Brazil. On March 28, 2011, we completed the acquisition of an economic interest of 25.3% in Oi (through a 25.6% economic interest in TmarPart and a 25.3% interest in Telemar Norte Leste S.A.), Brazil's largest telecommunications group. We do not expect to hedge our economic exposure against exchange rate fluctuations. We are required to make adjustments to our equity on our balance sheet in response to fluctuations in the value of foreign currencies in which we have made investments. Devaluation of the Brazilian Real in the future could result in negative adjustments to our balance sheet, which could limit our ability to generate distributable reserves.

We are also exposed to interest rate fluctuation risks. We have entered into financial instruments to reduce the impact on our earnings of an increase in market interest rates, but these financial instruments may not prevent unexpected and material fluctuations of interest rates from having any material adverse effect on our earnings.

The Brazilian Central Bank's Monetary Policy Committee (*Comitê de Política Monetária do Banco Central COPOM*) establishes the basic interest rate target for the Brazilian financial system by referring to the level of economic growth of the Brazilian economy, the level of inflation and other economic indicators. As of December 31, 2006, 2007, 2008, 2009 and 2010, the basic interest rate was 13.3%, 11.3%, 13.8%, 8.8% and 10.8%, respectively. Increases in interest rates may have a material adverse effect on Oi by increasing its interest expense on floating rate debt and increasing its financing costs.

Macroeconomic factors in Brazil could reduce expected returns on our Brazilian investments

A material portion of our business, prospects, financial condition and results of operations has been, and will continue to be, dependent on general economic conditions in Brazil. In particular, our growth 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 our 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 utilized salary and price controls, currency devaluation, capital controls and limits on imports, among other things as tools in its previous attempts to stabilize the Brazilian economy and control inflation. Changes in the Brazilian government's exchange control policy, or in general economic conditions in Brazil, could have a material adverse effect on the results of our operations in Brazil. Deterioration in economic and market conditions in other countries (mainly in other Latin American and emerging market countries) may adversely affect the Brazilian economy and our business.

Past political crises in Brazil have affected the confidence of investors and the public in general, as well as the development of the economy. Future political crises could have an adverse impact on the Brazilian economy and Oi's business, financial condition and results of operations.

Fluctuations in the Real and increases in interest rates. The Brazilian currency has historically experienced frequent fluctuations relative to the Euro and other currencies. In 2007, 2009 and 2010, the Real appreciated against the Euro by 8.3%, 29.2% and 13.2%, respectively, and in 2008 depreciated against the Euro by 20.0%. 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 our operations and our ability to distribute reserves. It would also increase costs associated with financing our operations in Brazil. In addition, a devaluation of the Real relative to the U.S. dollar may increase the costs of imported products and equipment. Our operations in Brazil rely on imported equipment, and, as a result of such devaluation, such equipment would be more expensive to purchase.

In response to the global economic and financial crisis, the Brazilian government increased the SELIC basic interest rate to 13.75% as of December 31, 2008. In 2009 Brazilian Central Bank reduced the SELIC up to 8.75% as of December 31, 2009 and in 2010 increased it up to 10.75% as of December 31, 2010. An increase in interest rates could negatively affect our profitability and results of operations and would increase the costs associated with financing our operations in Brazil.

Inflation in Brazil. Brazil has historically experienced 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. Inflationary pressures persist, and actions taken in an effort to curb inflation, coupled with public speculation about possible future governmental actions, have in the past contributed to economic uncertainty in Brazil and heightened volatility in the Brazilian securities market. According to the Broad Consumer Price Index (*Índice Nacional de Preços ao Consumidor Amplo*), or "IPCA", published by the Brazilian Institute for Geography and Statistics (*Instituto Brasileiro de Geografia e Estatística*), or "IBGE", the Brazilian consumer price inflation rates were 3.1% in 2006, 4.5% in 2007, 5.9% in 2008, 4.3% in 2009 and 5.9% in 2010.

Since 2006, Oi's telephone rates have been indexed to the Telecommunications Service Index (*Índice de Serviços de Telecomunicações*, or "IST"), which is a basket of national indexes that reflect the Brazilian telecommunications sector's operating costs. However, Brazilian monetary policy continues to use the IPCA as an inflation targeting system. The inflation target for 2011 is 4.5%. If inflation increases beyond this official 2011 target, basic interest rates may rise, causing direct effects on Oi's cost of debt and indirect effects on the demand for telecommunications goods and services.

The market value of securities issued by Brazilian companies is influenced by the perception of risk in Brazil and other emerging market countries, which may have a negative effect on the value of our investment in Oi and may restrict Oi's access to international capital markets.

Economic and market conditions in other emerging market countries, especially those in Latin America, may influence the market for securities issued by Brazilian companies. Investors' reactions to developments in these other countries may have an adverse effect on the market value of securities of Brazilian issuers. Adverse economic conditions in other emerging market countries have at times resulted in significant outflows of funds from Brazil. In 2008, certain Brazilian and Mexican companies announced significant losses in connection with currency derivatives as a result of the depreciation of the *real* and the Mexican peso against the U.S. dollar, respectively. As a result, a number of these companies suffered financial distress and sought protection under various bankruptcy regimes. In addition, in October 2008, the Argentine government nationalized the Argentine private pension funds. Crises in other emerging countries or the economic policies of other countries, in particular the United States, may adversely affect investors' demand for securities issued by Brazilian companies, including Oi's preferred shares and ADSs. Any of these factors could adversely affect the market price of Oi's preferred shares and ADSs and impede its ability to access the international capital markets and finance its operations in the future on terms acceptable to it or at all.

Substantial competition exists in the Brazilian telecommunications market.

Competition is expected to continue to intensify for telecommunication operators in Brazil 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. An operator'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 an operator 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 it could suffer a decline in its revenue. Competition from other Brazilian fixed-line service providers, Personal Mobile Service (*Serviço Móvel Pessoal*, or "SMP") providers and data transmission service providers has affected, and may continue to affect, Oi's financial results by causing, among other things, a decrease in its customer growth rate, decreases in prices and increases in selling expenses.

Oi's competitors may be able to offer lower prices than it does and develop and deploy new or improved technologies, services and products more rapidly. Oi's response to competition may require it to lower rates, extend higher subsidies to its customers, and/or increase marketing expenses, thereby adversely affecting its margins.

In addition, market participants in other areas of Brazil may also seek to operate in Oi's area, most likely through acquisitions. Recently, there has been consolidation in the Brazilian telecommunications market, and we believe this trend may continue.

Consolidation may result in increased competitive pressures within our market. Oi may be unable to respond adequately to pricing pressures resulting from consolidation, which would adversely affect its business, financial condition and results of operations. Oi could be negatively affected by antitrust limitations imposed by the Brazilian National Telecommunications Agency (*Agência Nacional de Telecomunicações*, or "ANATEL") and the Brazilian Administrative Council for Economic Defense (*Conselho Administrativo de Defesa Econômica*, or "CADE"). Consolidation of other players in the Brazilian telecommunications market will increase the competitive pressure on Oi due to an increase in their economies of scale and a reduction in their operating costs.

Regulation may have a material adverse effect on Oi's results

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

Brazil's telecommunications regulatory framework is continuously evolving. The interpretation and enforcement of regulations, the assessment of compliance with regulations and the flexibility of regulatory authorities are all marked by uncertainty. Oi operates its fixed-line and personal mobile services under concession agreements and authorizations from the Brazilian government, and its ability to retain these authorizations is a precondition to its success. However, in light of the regulatory framework, ANATEL could modify the terms of the concession agreements and authorizations adversely. Furthermore, according to the terms of concession agreements and operating authorizations, Oi is obligated to meet certain requirements and to maintain minimum network expansion, quality, coverage and service standards. Failure to comply with these requirements may result in the imposition of fines or other government actions, including the early termination of operating authorizations. Any partial or total revocation of any operating authorizations would have a material adverse effect on Oi's business, financial condition, revenues, results of operations and prospects.

In recent years, ANATEL has also been reviewing and introducing changes in applicable regulation, especially regarding the interconnection fees among telecommunications service providers in

Brazil. Interconnection fees, which are fees charged by telecommunications service providers to each other to interconnect to each others' networks, are an important part of Oi's revenue base. To the extent that changes to the rules governing interconnection fees reduce the amount of interconnection fees Oi is able to collect, businesses, financial conditions, revenues, results of operations and prospects could be adversely affected.

Certain legislative bills seeking to terminate monthly subscription fees charged by local fixed-line service providers have been submitted to the Brazilian Congress and remain pending. In March 2008, a special committee was formed in the Brazilian House of Representatives to discuss the various proposed bills on this issue. As of the date of this annual report, no action had been taken by the committee. In 2010, monthly subscription fees represented 24.0% of Oi's gross operating revenue. The enactment of legislation terminating the monthly subscription fees would have a material adverse effect on its results of operations.

Our other international investments are subject to political, economic, regulatory and legal risk in those countries, which could adversely affect the value of our investments and our results of operations

In accordance with our strategy, we continue to proactively manage our international businesses in selected markets and regions where we have a clear competitive advantage. This strategy may be pursued either by investing alone or by developing partnerships and by acquiring existing companies or by investing in new projects.

These investments are exposed to political and economic risks that include, but are not limited to, exchange rate and interest rate fluctuations, inflation and restrictive economic policies and regulatory risks that include, but are not limited to, the process for the renewal of licenses and the evolution of regulated retail and wholesale tariffs. In addition, our ventures in international markets face risks associated with increasing competition, including due to the possible entrance of new competitors and the rapid development of new technologies.

The development of partnerships in these markets raises risks related to the ability of the partners to jointly operate the assets. Any inability of us and our partners to operate these assets may have a negative impact on our strategy and on our results of operations.

All these risks may have material adverse effects on our results of operations.

Adverse political, economic and legal conditions in the countries where we have investments may hinder our ability to receive dividends from our international subsidiaries

The governments of many of the countries where we have investments have historically exercised, and continue to exercise, significant influence over their respective economies and legal systems. Countries where we have investments may enact legal or regulatory measures that restrict the ability of our subsidiaries to make dividend payments to us. Similarly, adverse political or economic conditions in these countries may hinder our ability to receive dividends from our subsidiaries. We receive significant amounts in dividends each year from our international investments, particularly in Africa, and a limitation on our ability to receive a material portion of those dividends could adversely affect our cash flows and liquidity.

Table of Contents

Risks Related to Our Strategic Partnership with Oi

Our strategy of enhancing our operations in Brazil through our strategic partnership with Oi may not be successful, and we do not have free access to cash flows from Oi

The successful implementation of our strategy for our mobile operations in Brazil depends on the development of our strategic partnership with Oi. On January 26, 2011, we announced that we had entered into agreements with Oi to acquire a significant economic stake of that company, and on March 28, 2011, we completed the acquisition of a 25.6% economic interest in TmarPart and a 25.3% economic interest in Telemar Norte Leste S.A.

As in any strategic partnership, it is possible that we and Oi will not agree on its strategy, operations or other matters. Any inability of Oi and us to operate Oi jointly could have a negative impact on Oi's operations, which could have a negative impact on our strategy in Brazil and could have a material adverse effect on our results of operations. In addition, we cannot be sure that Oi 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 strategic partnership will be realized.

As part of our strategic alliance with Oi, we plan to merge Dedic S.A. ("Dedic") and GPTI Tecnologia da Informação S.A. ("GPTI"), our contact center operations in Brazil, with Contax S.A. ("Contax") and increase our economic stake in CTX, Contax's indirect controlling shareholder, from 42.0% to 44.4%. This merger is still subject to approval by our board of directors and shareholders and other conditions that are beyond our control.

In addition, because we hold joint control of Oi, we may not have free access to its cash flows. It will be necessary for us and other controlling shareholders of Oi to agree to approve any distributions from Oi. See "*Item 4 Information on the Company Our Businesses Strategic Alliances Strategic Partnership with Oi*."

Oi has a substantial amount of existing debt, which could restrict its financing and operating flexibility and have other adverse consequences.

At December 31, 2010, Oi had total consolidated debt of R$29,136 million. Oi is subject to certain financial covenants that limit its ability to incur additional debt. Its existing level of indebtedness and the requirements and limitations imposed by its debt instruments could adversely affect its financial condition or results of operations. In particular, the terms of some of these debt instruments restrict our ability, and the ability of our subsidiaries, to:

- incur additional debt;
- grant liens;
- pledge assets;
- sell or dispose of assets; and
- make certain acquisitions, mergers and consolidations.

Furthermore, some of Oi's debt instruments include financial covenants that require it and some of its subsidiaries to maintain certain specified financial ratios. Additionally, the instruments governing a substantial portion of its indebtedness contain cross-default or cross-acceleration clauses, and the occurrence of an event of default under one of these instruments could trigger an event of default under other indebtedness or enable the creditors under other indebtedness to accelerate that indebtedness.

If Oi is unable to incur additional debt, it may be unable to invest in its business and make necessary or advisable capital expenditures, which could reduce future net operating revenue and

adversely affect its profitability. In addition, cash required to serve its existing indebtedness reduces the amount available to it to make capital expenditures.

If Oi's growth in net operating revenue slows or declines in a significant manner, for any reason, it may not be able to continue servicing its debt. If it is unable to meet its debt service obligations or comply with our debt covenants, it could be forced to renegotiate or refinance its indebtedness, seek additional equity capital or sell assets. It may be unable to obtain financing or sell assets on satisfactory terms, or at all.

Oi is subject to numerous legal and administrative proceedings, which could adversely affect its business, results of operations and financial condition.

Oi is subject to numerous legal and administrative proceedings. It is difficult to quantify the potential impact of these legal and administrative proceedings. It classifies its risk of loss from legal and administrative proceedings as "probable," "possible" or "remote." It makes provisions for probable losses but does not make provisions for possible and remote losses. At December 31, 2010, Oi had recorded provisions of R$6,793 million for probable losses relating to various tax, labor and civil legal and administrative proceedings against it.

At December 31, 2010, Oi had claims against it of R$15,305 million in tax proceedings, R$2,547 million in labor proceedings and R$1,372 million in civil proceedings with a risk of loss classified as "possible" or "remote" and for which it had made no provisions.

If Oi is subject to unfavorable decisions in any legal or administrative proceedings and the losses in those proceedings significantly exceed the amount for which it has provisioned or involve proceedings for which it has made no provision, its results of operations and financial condition may be materially adversely affected.

Oi is subject to delinquencies of its accounts receivables. If it is unable to limit payment delinquencies by its customers, or if delinquent payments by its customers increase, its financial condition and results of operations could be adversely affected.

Oi's business significantly depends on its customers' ability to pay their bills and comply with their obligations to it. In 2010, Oi recorded provisions for doubtful accounts in the amount of R$979 million, primarily due to subscribers' delinquencies. As a percentage of Oi's gross operating revenue, its provision for doubtful accounts was 2.1% at December 31, 2010.

ANATEL regulations prevent Oi from implementing certain policies that could have the effect of reducing delinquency, such as service restrictions or limitations on the types of services provided based on a subscriber's credit record. If Oi is unable successfully to implement policies to limit subscriber delinquencies or otherwise select its customers based on their credit records, persistent subscriber delinquencies and bad debt will continue to adversely affect Oi's operating and financial results.

In addition, if the Brazilian economy declines due to, among other factors, a reduction in the level of economic activity, depreciation of the Brazilian Real, an increase in inflation or an increase in domestic interest rates, a greater portion of Oi's customers may not be able to pay their bills on a timely basis, which would increase its provision for doubtful accounts and adversely affect its financial condition and results of operations.

Tele Norte Leste Participações S.A., a subsidiary of Telemar Participações S.A., whose ADRs are listed on the New York Stock Exchange, files its own Annual Reports on Form 20-F with the Securities and Exchange Commission. It filed its most recent Annual Report on Form 20-F on May 4, 2011, and that report contains additional information regarding the business, financial position, results of operations and risks relating to Oi. However, Annual Report on Form 20-F of Tele Norte Leste Participações S.A. is not incorporated by reference into our Annual Report on this Form 20-F.

Risks Relating to Our ADSs and Ordinary Shares

An ADS holder may face disadvantages compared to an ordinary shareholder when attempting to exercise voting rights

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

If you are a U.S. tax resident, you will not be eligible for the reduced rates of Portuguese withholding tax on dividends under the U.S.-Portugal income tax treaty unless you fill out a form required by the Portuguese tax authorities and get it certified by the U.S. Internal Revenue Service

If you are a U.S. tax resident, you will not be eligible for the reduced rates of Portuguese withholding tax on dividends under the U.S.-Portugal income tax treaty unless you fill out a form required by the Portuguese tax authorities and have it certified by the U.S. Internal Revenue Service.

Under Portuguese law, dividends paid by Portuguese companies are subject to withholding tax at a 21.5% rate. Dividends placed in bank omnibus accounts (except where the identity of the effective beneficiary is disclosed), are subject to withholding tax at a rate of 30%.

However, under the U.S.-Portugal income tax treaty, the withholding tax rate on dividends distributed to U.S. tax residents may be reduced, as a general rule, to 15%. In order to apply the reduced treaty rate, confirmation that each shareholder is eligible for the benefits of the treaty is required. A specific form (Form 21-RFI of the Directorate-General of Taxes (*Direcção Geral de Impostos* DGCI) of the Portuguese Ministry of Finance), duly certified by the U.S. Internal Revenue Service, must be received by Banco Espírito Santo, the custodian for the depositary, if you are a holder of ADSs, or your financial intermediary, if you are a holder of Portugal Telecom ordinary shares, prior to the date the dividends are made available to shareholders.

If this form is not available as of the relevant date, Portuguese withholding tax will be levied at the 21.5% rate. If you are able to submit the form to the custodian for the depositary, if you are a holder of ADSs, or to your financial intermediary, if you are a holder of ordinary shares, no later than the 20th day of the month following the payment of the dividend, we believe that the custodian or the financial intermediary, as the case may be, should release the 6.5% excess Portuguese withholding tax to you. However, we cannot guarantee that the custodian or the financial intermediary will do so.

In addition, the 6.5% excess Portuguese withholding tax may be subsequently reimbursed by the Portuguese tax authorities pursuant to specific claims of individual shareholders on Form 22-RFI of the

Table of Contents

Directorate-General of Taxes of the Portuguese Ministry of Finance, duly certified by the U.S. Internal Revenue Service and presented to the Portuguese tax authorities within two years following the last day of the year in which the dividends were made available. See "*Item 10 Additional Information Taxation Dividends*."

If you are an investment fund, pension fund or trust holding ADSs or ordinary shares, you should be aware that, under a guidance note issued by the Portuguese tax authorities, in order to benefit from the Treaty provisions, you must comply with certain additional requirements that are described in "*Item 10 Additional Information Taxation Dividends*." Although this is not demanded by the Treaty, the Portuguese tax authorities take the position that the compliance with the applicable requirements should be certified by the U.S. Internal Revenue Service, using a form or other mean specifically permitted for this purpose. If you are an investment fund, pension fund or trust, you should contact your tax advisor for more information regarding the requirements of the Portuguese tax authorities.

You should know that receiving certification of a Form 21-RFI or Form 22-RFI from the U.S. Internal Revenue Service can be a lengthy process. In addition, although Portuguese law states that the excess withholding tax should be reimbursed within one year from the date the claim was submitted, we cannot guarantee if or when you will receive any reimbursement of the 6.5% excess Portuguese withholding tax even if you fill out Form 22-RFI and are eligible to receive reimbursement as described above. You should contact your tax advisor if you wish to fill out Form 21-RFI or Form 22-RFI to claim eligibility for the benefits of the Treaty.

ITEM 4 INFORMATION ON THE COMPANY

Overview

Our legal and commercial name is Portugal Telecom, SGPS, S.A. We are a limited liability holding company, organized as a *Sociedade Gestora de Participações Sociais* under the laws of the Portuguese Republic. The company was originally incorporated as Portugal Telecom, S.A., a *sociedade anónima* in June 1994. Our principal offices are located at Avenida Fontes Pereira de Melo, 40, 1069-300 Lisboa, Portugal. Our telephone number is +351 21 500 1701, and our facsimile number is +351 21 500 0800. Our agent for service of process in the United States is Puglisi & Associates at 850 Library Avenue, Suite 204, Newark, Delaware 19711. Our home page is located at *www.telecom.pt*. The information on our website is not part of this report. The website address is included as an indicative textual reference only.

We provide telecommunications services mainly in Portugal (our "Portuguese operations") and through our significant strategic partnerships and investments in Brazil, certain countries in sub-Saharan Africa and Asia (our "international operations"). In Portugal, we provide services to the following customer categories:

- *Residential services*, which provides integrated networks inside the customer's home, enabling the simultaneous connection of multiple devices, including fixed line telephone, TV (including Internet Protocol Television and direct-to-home satellite Pay-TV services), game consoles, PCs, laptops, tablets and smartphones. We provide these services through our subsidiaries, in particular PT Comunicações, S.A. ("PT Comunicações");

- *Personal services*, which provides mobile telecommunications services, such as voice, data and Internet-related multi-media services, in particular mobile phones, smartphones, tablets and laptops, through our subsidiary TMN Telecomunicações Móveis Nacionais, S.A. ("TMN");

- *Enterprise services, including Corporate and SME/SoHo services*, which provide our corporate and medium and small business customers with data and business solutions, as well as IT/IS and business process outsourcing (BPO) services.

Table of Contents

- *Wholesale services*, which includes leased lines, interconnection services, unbundled access to our local loops, broadband ADSL services, wholesale line rental, access to ducts, transmission of television and radio signals and international carrier services.

- *Other services,* which primarily includes our directories business and portal services that are provided in Portugal as part of our comprehensive service offering.

Since the closing of our transaction with Oi on March 28, 2011, we also hold a 25.3% economic stake in Oi, which provides mobile, wireline, broadband and Pay-TV services in Brazil. As part of the same transaction, we acquired a 16.2% economic stake in CTX Participações S.A. ("CTX"), the parent company of Contax Participações S.A. ("Contax Participações") and Contax, which provides contact center services in Brazil. We also agreed to merge Dedic and GPTI, our subsidiaries that provide contact center and IS/IT services in Brazil, with Contax, subject to approval by our board of directors and shareholders and other conditions.

In addition, we have significant interests in telecommunications companies in Angola, Cape Verde, Namibia and São Tomé and Principe in Africa and in Macau and East Timor in Asia.

In Portugal, we are the leading provider of all of these services, except for IPTV and DTH services, according to data provided by ANACOM, the Portuguese telecommunications regulator. The provision of residential and enterprise services through our wireline business in Portugal continues to account for a large proportion of our revenues (47.2% during 2010) as compared to revenues derived from any other line of business.

Strategy

We remain committed to discipline in our strategy, cost, operations and financial performance, and we aim to focus our resources on our core businesses and core regions, namely Portugal, Brazil and sub-Saharan Africa. Our strategy continues to be guided by the five medium-term strategic objectives:

- grow our customer base to 100 million customers;

- increase our exposure to international businesses up to two-thirds of our revenues;

- seek and reinforce leadership in all domestic market sectors;

- achieve performance in the top quartile of European companies in shareholder return and operating and financial results; and

- become a reference company in sustainability efforts.

Our success in achieving these goals is subject to a number of uncertainties, including the factors described in "*Item 3 Key Information Risk Factors*."

Some of our specific strategies to achieve these goals include the following:

Portuguese Operations

- reinforce leadership in all market sectors where we operate and aim at offering broad and convergent products and services;

continue to enhance our customer service;

continue to engage in innovations using a structural approach and benefiting from our estabhished strategic partnerships; and

continue to invest in technologically advanced fixed, mobile and integrated networks;

Table of Contents

International Operations

- maximize the strategic value of our international assets and reinforce our focus on Brazil and sub-Saharian Africa; and

- focus on operational and commercial efficiency of all assets and promote the sharing of best practices among all businesses.

Corporate Structure

Our market is characterized by increasing competition and rapid technological change. Our subsidiaries are held directly and indirectly by Portugal Telecom in its role as holding company. We have integrated certain functions across the company, in particular information systems (PT Sistemas de Informação), research and development capabilities (PT Inovação), back office activities (PT Pro), central purchasing capabilities (PT Compras) and call center operations (PT Contact). The diagram below presents our different businesses as of the date of filing of this Annual Report on Form 20-F.

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(1) Providing wireline services in Portugal, including our fixed telephone service, Internet access services, wholesale services, data and business solutions services, portal and e-commerce solutions, and IPTV and DTH services.

(2) Various companies providing services to Portugal Telecom group companies, including PT Sistemas de Informação (information systems), PT Inovação (research and development), PT Pro (shared services), PT Compras (central purchasing) and PT Contact (call centers).

(3) The acquisition of this investment was completed in March 2011, as explained in more detail below.

(4) Includes our investment in Contax, which is explained in " *Recent Developments Strategic Partnership with Oi*" below, our investments in global telecommunications operators in the Cape Verde Islands, São Tomé and Principe Islands and Macau, mobile operators in Namibia and Angola, and other investments.

For additional information on our significant subsidiaries, see Exhibit 8.1, which is incorporated herein by reference.

Table of Contents

The following table sets forth the operating revenues of each of our major business lines, on a standalone basis, for the years ended December 31, 2008, 2009 and 2010:

	Year Ended December 31,		
	2008	2009	2010
	(EUR millions)		
Wireline services (Residential, Enterprise Services and Wholesale Services):			
Retail	953.5	971.0	969.2
Wholesale	488.5	495.4	491.3
Data and corporate	286.5	300.7	287.7
Other	203.0	180.6	180.8
Total	1,931.5	1,947.8	1,929.0
Mobile services (Personal Services):			
Services:			
Customers	1167.3	1173.4	1099.0
Interconnection	231.2	161.0	141.9
Roamers	26.4	25.5	23.7
Total services	1,424.9	1,360.0	1,264.7
Sales	159.4	144.1	112.4
Other	9.3	13.7	10.4
Total	1,593.6	1,517.8	1,387.5
Other Operations	794.7	873.9	1088.3
Eliminations in consolidation	(558.4)	(606.0)	(662.5)
Total consolidated operating revenues	3761.2	3,733.4	3,742.3

For information about the effects of seasonality on our business, see "*Item 5 Operating and Financial Review and Prospects Overview Business Drivers and Measures Seasonality*."

Recent Developments

Acquisition of Vivo by Telefónica

On July 28, 2010, we signed an agreement with Telefónica for the acquisition by Telefónica of the 50% of the capital stock of Brasilcel N.V. we owned. Brasilcel owned approximately 60% of the total share capital of Vivo Participações, S.A. ("Vivo"). The acquisition price of that capital stock was €7,500 million, €4,500 million of which was paid at the closing of the transaction on September 27, 2010 and €1,000 million of which was paid on December 30, 2010, with the remaining €2,000 million due on October 31, 2011 (though we may request that this final payment be made on July 29, 2011, in which case such final payment, and correspondingly, the total price of the acquisition, would be reduced by €25 million). The agreement also provided for certain other commercial arrangements between Telefónica and Portugal Telecom that were subsequently rendered inapplicable. Upon closing of the transaction, the respective subscription and shareholders agreements entered into by Telefónica and Portugal Telecom in 2002 relating to Vivo were terminated.

Strategic Partnership with Oi

On January 26, 2011, we announced that we had entered into a series of agreements with Oi, Brazil's largest telecommunications group, to acquire a significant stake in that company. In connection with our agreements to establish a strategic partnership with Oi, we also agreed to merge Dedic and GPTI, our subsidiaries that provide call center and IS/IT services in Brazil, with Contax, one of the leading corporate services company and the leader in contact center services in Brazil. Contax is currently controlled by the controlling shareholders of Oi, through CTX and Contax Participações. The Oi transaction closed on March 28, 2011. We also completed the acquisition of a 16.2% stake in CTX but have not yet completed the merger of Dedic and Contax, which is subject to the approval of our board of directors and shareholders and other conditions. Following the closing of the transaction, we hold a 25.3% econominc stake in Oi, and we expect to hold a 44% economic stake in CTX (42.0% prior to the merger of Dedic and Contax).

For more information about the transaction, see "*Item 4 Information on the Company Our Businesses Strategic Alliances Strategic Partnership with Oi*."

Sale of Interest in Universo Online S.A.

On December 29, 2010, we reached an agreement for the sale of our 28.78% of stake in Universo Online S.A. ("UOL"), a Brazilian internet provider to a Brazilian businessman. The total consideration for the sale was R$356 million (€161 million as of December 31, 2010). The transaction closed on January 27, 2011.

Our Businesses

Portuguese Operations

Our Portuguese operations are managed alongside two segments: wireline and mobile (TMN). Within each of the wireline and mobile segments, we provide services to five key customer categories:

- *Residential services*, which provide integrated networks inside the customer's home enabling the simultaneous connection of multiple devices, including fixed line telephones, TVs (including Internet Protocol Television and direct-to-home satellite Pay-TV services), game consoles, PCs, laptops, tablets and smartphones. Profits and losses related to services provided to residential customers are recorded under the wireline segment;

- *Personal services*, which provide mobile telecommunications services, such as voice, data and Internet-related multi-media services across several access devices, such as mobile phones, smartphones and tablets, as well as wireless datacards and dongles for internet access. Profits and losses related to services provided to personal customers are recorded under the mobile segment;

- *Enterprise services, including Corporate and SME/SOHO services*, which provide our corporate as well as media and small business customers with data and business solutions, as well as IT/IS and business process outsourcing (BPO) services:

  - *Corporate services,* which targets large companies and provides data, Internet, video and voice communications, services, fixed mobile convergence solutions and selected information technology services, network managing and outsourcing; and

  - *SME/SOHO services*, which targets (1) small and medium enterprises ("SMEs"), providing vertical data and business solutions that are similar to our corporate services and (2) small office/home office ("SOHO") customers and provides cost-effective data and business solutions for those working in small businesses or at home;

  Profits and losses related to services provided to Enterprise customers are recorded under both the wireline and mobile segments;

Wholesale services, which includes leased lines, interconnection services, unbundled access to our local loops, broadband ADSL services, wholesale line rental, access to ducts, transmission of television and radio signals and international carrier services. Profits and losses related to services provided to Wholesale customers are recorded under the wireline segment; and

Table of Contents

Other services, which primarily includes our directories business and portal services that are provided in Portugal as part of our comprehensive service offering.

Residential Services (Included in our Wireline Business)

Our residential customer category provides fixed line telephone services, Pay-TV (IPTV and DTH satellite TV) services and Internet access services to residential customers. The table below sets forth the total number of retail lines (or accesses), net retail additions and other information as of the dates indicated. The wireline business, as reported, includes not only the services and products provided to our residential customers but also fixed telecommunications services provided to corporate and SME/SOHO customers. A relevant part of our retail business is to residential customers, but retail services provided to business customers (described under " Enterprise Services" below) are also reflected in the table below.

	As of December 31,		
	2008	**2009**	**2010**
Retail accesses (thousands):			
PSTN/ISDN(1):			
Traffic-generating lines	2668	2,612	2,600
Carrier pre-selection	174	134	95
Total PSTN/ISDN lines	2843	2,746	2,695
Fixed broadband retail	710	862	1,001
TV customers	312	581	830
Total retail accesses	3865	4,189	4,527
Net additions (thousands):			
PSTN/ISDN:			
Traffic-generating lines	(110)	(56)	(12)
Carrier pre-selection	(63)	(40)	(39)
Fixed broadband retail	73	152	139
TV customers	291	269	249
Total retail accesses	191	325	337
Retail RGU per PSTN/ISDN line(2)	1.53	1.53	1.68
ARPU (Euros)	29.2	30.1	30.1
Retail traffic (millions of minutes)	4,990	4,713	4,581

(1) The public switched telephone network ("PSTN") is the traditional telephone system that runs through copper lines. The integrated digital services network ("ISDN") is the digital telecommunications network that allows simultaneous voice and data transmission over an access line.

(2) Revenue generating units ("RGUs") are individual subscribers of our services.

(3) The average revenue per user ("ARPU") is the monthly average service revenues per average number of users in the period.

Fixed Line Network

We had approximately 4.9 million telephone and asymmetric digital subscriber line ("ADSL") access lines in service at December 31, 2010, excluding external supplementary lines, direct extensions and active multiple numbers. We break our fixed line network down into retail accesses and wholesale accesses. Within retail accesses, we report:

traffic-generating lines held by subscribing customers;

Table of Contents

carrier pre-selection lines, which are lines of competitors for which those customers have elected to use our services;

fixed broadband retail lines; and

Internet protocol television ("IPTV") customers.

The number of active mobile cards (the mobile equivalent of main lines) exceeds the number of fixed line main lines in Portugal, and traffic that once was transmitted in whole or in part on our fixed line network is now carried on our mobile network or on the network of other mobile operators. We are addressing this trend by encouraging increased use of our fixed line network for bundled services, including not only fixed telephone services but also broadband internet access and Pay-TV services, primarily offered as triple-play packages.

All of our local switches in Portugal have been digital since 1999. Digital technology is used on all long distance and trunk connections. This level of digitalization of our fixed line network permits us to market and provide network-based value-added services, such as call waiting, call forwarding and voice mail, resulting in increased line usage. Moreover, in May 2009, we announced our objective to cover one million homes with Fiber-to-the-Home ("FTTH"), which we achieved by the end of 2010. Our FTTH network, which is developed in urban areas, is a strategic investment to improve our competitiveness in the market not only in residential services, where we can offer distinctive Pay-TV and bundled offers, but also for our enterprise services, where trends like cloud services, outsourcing of infrastructure and software applications are emerging rapidly.

We measure volume on our network in terms of traffic, which is the number of minutes that our retail and wholesale accesses are used. Total traffic on the network has been decreasing since 2002, primarily because consumers have increasingly used mobile services instead of fixed line services and because of the migration of dial-up Internet users to ADSL. However, in the fourth quarter of 2010, positive net additions of fixed lines were achieved for the first time in seven years, primarily due to strong performance of *Meo* double-play and triple-play offers.

We are required to provide carrier selection to our customers for all kinds of traffic. See " *Regulation-Portugal Number Portability and Carrier Selection*." Carrier selection has been an additional factor that has contributed to the reduction in traffic on our network.

Except for customer pre-selection and Internet traffic, we account for traffic originating on our network as fixed line telephone services, described below, and we allocate the revenue billed to customers to those services. Traffic originating on other networks but terminating on our network, and the related revenue, is allocated to our wholesale services described under " Wholesale Services" below.

Fixed Line Telephone Services

We provide public fixed line telephone services in Portugal to retail customers. This business area provided €969.2 million and €971.0 million during 2010 and 2009, respectively.

Table of Contents

We distinguish between two principal sources of revenue in the provision of fixed telephone services:

Fixed charges, including network access charges based on a monthly line rental and an initial installation fee, as well as, in most cases, a monthly fee from pricing packages, which can include broadband and Pay-TV; and

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

In recent years, fixed line traffic has continued to decrease, primarily due to the trend toward the use of mobile services instead of fixed line services and strong competition from fixed and cable operators, though partially offset by the strong performance of our *Meo* double-play and triple-play offers.

Pay-TV Services

IPTV Services. In 2008, we announced the launch of our nationwide Pay-TV offer, which includes DTH (satellite) and IPTV offers. Our television strategy is based on a multiplatform concept that aims to provide similar content and user experiences across television, PCs and mobile phones. *Meo* is our TV brand across the various platforms, namely at home (through IPTV and satellite), through mobile handsets (through *Meo Mobile*) or through personal computers. *Meo* provides access to a comprehensive content offering, with more than 120 TV channels and over 2,500 video-on-demand titles. We offer tiered packages of channels, as well as on-demand availability that can be subscribed for directly through the TV set in real time. *Meo* also provides access to advanced features, such as digital recording and pause live-TV. The set-top boxes in the *Meo* service are all HD-compliant, using MPEG4. We were the first operator in Portugal to introduce HDTV and have the most extensive video-on-demand offer in the market.

In 2008, *Meo* launched a "quintuple-play" offer, including Pay-TV, fixed broadband, voice, video-on-demand and mobile broadband.

In 2009, *Meo* further reinforced its position in the Portuguese market by launching several features to differentiate its offer, including (1) real video-on-demand (VoD) with DVD-like features and a catalog of more than 2,500 movies, including high definition ("HD"), (2) catch-up TV, (3) an electronic programming guide accessible remotely through the Internet and the mobile phone, (4) TV channel recording, which can be remotely programmed through the Internet or through the mobile phone, (5) gaming, karaoke and several interactive content and service areas, (6) access to personal photo folders and (7) customized offers for kids. In addition, we launched Meo@PC, allowing customers to have online access to *Meo*'s Pay-TV service through their personal computers, strengthening the mobility and convergence attributes of *Meo*.

Meo's VoD offer, which includes movies from five Hollywood studios, is a key differentiating feature of the service, as more than 55% of *Meo*'s IPTV customers have already used VoD on a paid basis, consuming on average 2.3 movies per month.

In 2010 and early 2011, we continued to add to the channels and features available on *Meo*, including (1) several new channels, including FoxLife, Channel Q, Food Network HD, Mezzo Live HD and Travel Channel HD, (2) channel interactivity, including TVI Secret Story Interactivo, an exclusive interactive channel developed in partnership with TVI, a free-to-air broadcast channel, (3) Meo Online, which gives access to *Meo*'s VoD catalogs through PCs, (4) Meo Jogos, which offers games from leading game developers, (5) Music Box, an integrated service for mobile phones, PCs and TV; and (6) Meo Remote, an application allowing *Meo* customers to install a Meu remote control on their smartphones and tablets.

Table of Contents

As of December 31, 2010, we had 830 thousand TV customers.

DTT Services. In 2008, we were notified of the final decision of ANACOM endorsing the Draft Final Decision of the Portuguese Committee of Evaluation to allocate to us the frequency usage rights for Digital Terrestrial Television ("DTT") associated with the system for combining more than one information stream into a single stream for transmission ("Multiplex" or "Mux"), namely Mux A (transport of free-to-air signal) and Muxes B to F (Pay-TV service). In 2009, the Portuguese Media Regulatory Entity (*Entidade Reguladora para a Comunicação Social*, or "ERC"), an independent regulatory authority for the Portuguese media, notified us of its final decision to grant us a license to act as a TV distribution operator.

We launched DTT (with DVB-T) in 2009, initially covering 29 municipalities and over 40% of the population. By the end of 2009, this figure reached 80% of the population. The switch-off of analog television is foreseen for April 2012, although this may happen sooner given that by the end of 2010, coverage reached 100% of the population.

On December 22, 2010, ANACOM approved a draft decision regarding the alteration of the operating channel Mux A of the DTT, assigned to PT Comunicações. In addition, on December 22, 2010, ANACOM approved the final decision on the identification of re-transmitters and respective dates of termination of broadcasts of the pilot phase provided in the detailed plan for the cessation of analog terrestrial television broadcasts (*i.e.*, switch-off plan). On December 27, 2010, invoking reasons of public interest, ANACOM initiated a process to change the radio channels assigned to PT Comunicações with the goal of improving efficient spectrum management and harmonizing the conditions of use of frequencies in the 800 MHz band.

We requested that ANACOM revoke frequency usage rights associated with Muxes B to F and requested that ERC revoke the license to act as a TV distribution operator. ANACOM issued a draft decision on January 29, 2010, pursuant to which ANACOM stated that it intended to revoke the action granting PT Comunicações the right to use the frequencies associated with Muxes B to F, retroactive to January 29, 2010. This draft decision was submitted to a public consultation. On July 12, 2010, ANACOM made a final decision to revoke the granting of rights of use of the frequencies associated with Muxes B to F and, consequently, the five titles that document the rights assigned to PT Comunicações. The revocation decision was retroactive to the date of the draft decision issued by ANACOM on January 29, 2010. As a result, we continue to use the Mux A (transport of free-to-air signal) for our DTT services but do not provide Pay-TV channels through our DTT services. We provide our Pay-TV channels instead using FTTH, ADSL and DTH technologies.

As to the request submitted to ERC, this authority issued a draft decision, under which it stated that reasons of public interest prevented revoking the license granted to PT Comunicações to operate as a TV distribution operator using the frequencies allocated by ANACOM for that purpose. This draft decision was also submitted to a public consultation. The final decision, issued on March 17, 2010, maintained ERC's draft position. The decision process of the ERC is independent from that of ANACOM.

Fixed Broadband Retail Services

We offer Internet access through the lines of our fixed line network. As of December 31, 2010, we had approximately 1.0 million fixed broadband retail customers, which represented an overall increase of 16% over the previous year. The majority of these customers use our ADSL services. However, we also offer dial-up paid and free Internet access services.

Table of Contents

How We Report Residential Services in Our Financial Statements

We report our entire residential services customer category revenues within the wireline business in our financial statements.

Personal Services (Included in our Mobile Business)

We provide telecommunications and data mobility services for a variety of personal devices, including traditional cell phones, smartphones, tablets and laptops through our mobile business. We conduct our mobile business in Portugal through our 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 €1,387.5 million in 2010 compared to €1,517.8 million in 2009. At December 31, 2010, there were approximately 159.9 active mobile telephone cards per 100 Portuguese inhabitants according to ANACOM. The table below provides statistical information relating to TMN.

	As of December 31,		
	2008	**2009**	**2010**
Number of subscribers (thousands)(1)	6,933	7,252	7,419
Subscriber growth per annum(%)	11	5	2
Number of subscribers per 100 inhabitants (including competitors' subscribers)(2)	140.4	149.9	159.9
Estimated market share by number of subscribers(%)(3)	46.6	45.5	45
Number of employees	1,082	1,004	1,029

(1) Including mobile virtual network operators, or "MVNO," customers.

(2) Source: ANACOM.

(3) Sources: ANACOM and TMN; calculated as TMN's total number of subscribers divided by the mobile market in terms of subscribers, as disclosed by ANACOM.

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's strategy has been to use GSM 1800 services to offer an increased number of channels in high traffic density areas without compromising the quality of the network. Dual-band handsets, which select available channels from each frequency band, enable users to benefit from the wider range of available channels.

At the end of 2010, TMN's UMTS population coverage was approximately 93%, and its geographic coverage was about 68%, or 4,194 municipalities out of a total of 4252 in Portugal, including every municipality with over five thousand inhabitants.

TMN paid spectrum fees in 2010 and 2009 of €21 million and €24 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 in our financial statements.

Table of Contents

During 2010, TMN introduced the following new services in Portugal:

- an internet tablet service offering allowing mobile data access from tablet personal devices;
- "tribal plans," which are pricing plans targeted at youth customers;
- new unlimited mobile broad band tariff plans to increase penetration;
- new "TMN unlimited" and "all net unlimited" postpaid pricing plans aimed at the high value customers;
- a new "e nunca mais acaba" prepaid pricing plan aimed at the mass market, including free and unlimited communications with TMN customers;
- "Music Box," a new cross-platform music service for mobile phones, computers and TVs, with sharable playlists across all devices;
- a new handset application store and a Facebook store; and
- "Car Control," a new location-based security service for cars.

During 2010, in order to support our innovative service offering and distinguish it from the market, TMN launched the following new products in Portugal:

- the Samsung Galaxy-S, an advanced smartphone based on the Android operating system;
- the Samsung Galaxy Tab, a tablet PC based on the Android operating system;
- an exclusive arrangement to market the Samsung Omnia 7, the first mobile phone in Portugal to integrate the Windows 7 operating system;
- the i-Phone 4; and
- the Sapo a5, a low-cost smartphone using the Android operating system.

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. 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, corporate solutions and mobile payment services. TMN also offers a m-payment service called Telemultibanco that allows the payment of utility bills by mobile phone.

TMN also offers a variety of services for access to e-mail or Internet through Wi-Fi, GPRS and UMTS. GPRS is a mobile data service standard for GSM handsets. Currently, TMN offers speeds up to 21.6 Mbps. TMN also provides internet access through more than 1,600 hot spots.

In 2010, TMN contined to strengthen its mobile broadband offerings, increasing the speed and download capacity to its customers. As part of its efforts to maintain its strong market position in innovative products, TMN performed a long-term evolution ("LTE") technical trial. TMN has been investing significantly in new services, such as (1) Music Box, an integrated service for mobile phones, PCs and TV that provides access to a catalog of millions of music tracks, with immediate access to unlimited streaming from the main global music companies; (2) TMN's application store making available sports, news, entertainment, games, books and utility apps, which leverages on the wide experience and presence of PT's portal Sapo in the online world and partnerships with third parties; (3) *Meo* Mobile, which makes available 40 TV channels, in various areas such as information, sports, entertainment, children and other, on the mobile phone, and (4) Pond, an aggregation service that enables the access to multiple personal accounts and aggregation of social network accounts. This service and applications offering is complemented with the internetnotelemóvel service, which offers internet access on mobile phones in any place at any time and also access to TMN's innovative mobile portal.

As part of its innovation strategy, TMN recently launched its internet Pad service offering, a new mobile data access offer specifically designed for tablet PC's, aimed at establishing a leading position in this high-growth market. The internet Pad offer was recently further reinforced with the integration of the Samsung Galaxy Tab, based on the Android operating system.

TMN offers data services specifically focused on the corporate customer category, 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 Localizz, which is a location-based service that allows mobile management and localization of a company's resources (such as handsets, cars, machines and containers) through an Internet website.

TMN has 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. Uzo focuses primarily on selling SIM cards and low-cost 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, according to ANACOM. At December 31, 2010, TMN had approximately 7,419 million subscribers, representing an increase of 2.3% from December 31, 2009. At December 31, 2010, TMN's subscribers represented 45% of the total mobile subscribers in Portugal. During 2010, TMN's share of new mobile subscribers (net additions) was 39.5% according to ANACOM.

In addition to the increase in the number of subscribers, mobile usage grew during 2010. TMN's voice traffic in terms of minutes grew by 7.1% to 10.54 billion minutes in 2010, compared to 9.84 billion minutes in 2009. Average monthly usage per subscriber increased by 3.0% to 121 minutes in 2010, compared to 117 minutes in 2009, primarily because a greater proportion of subscriber growth was in the lower sections of the market.

Prices and Revenue Breakdown

We believe that mobile services in Portugal are priced lower than the European average and are among the lowest in Europe. Mobile telephone charges are not regulated. Traffic charges, sales of handsets and connection and subscription fees represented approximately 91.4%, 8.1% and 0.5%, respectively, of TMN's revenues in 2010 and approximately 90.1%, 9.5% and 0.4%, respectively, of TMN's revenues in 2009.

Fixed-to-mobile and mobile-to-mobile interconnection charges are regulated by ANACOM and have a significant impact on TMN's business. Since 2005, when 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. Interconnection rates have been reduced steadily since then. These reductions have had, and are expected to continue to have, a significant impact on TMN's interconnection revenues and consequently its earnings. In 2010, termination rates followed the new glide path defined by ANACOM on May 21, 2010. Pursuant to this decision, the maximum wholesale prices to be applied by mobile operators with significant market position in the termination of voice calls in individual mobile networks (market 16) are as follows: (1) €0.06 as of May 24, 2010; (2) €0.055 as of August 24, 2010; (3) €0.05 as of November 24, 2010; (4) €0.045 as of February 24, 2011; (5) €0.04 as of May 24, 2011 and (6) €0.035 as of August 24, 2011.

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. We estimate that at the end of 2010, approximately 69% of its subscribers were using TMN's prepaid products. TMN has been expanding its subscriber base through increased advertising and the use of its own distribution network. In recent years, TMN has focused on encouraging the use of mobile services by young people through SMS incentive packages.

TMN markets its services through more than 2,573 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 2010, TMN's digital network had 4,706 GSM base stations, including 72 base stations added during 2010, and 3,678 UMTS B nodes, including 160 B nodes added during 2010. As of December 31, 2010, these GSM base stations covered more than 98% of continental Portugal and 99% of the Portuguese population, and the UMTS B nodes covered approximately 68% of continental Portugal and 93% of the Portuguese population.

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 2010, TMN had entered into GSM roaming agreements with a total of 461 operators (in 219 countries), 301 GPRS roaming agreements (in 173 countries) and 170 3G roaming agreements (in 94 countries).

Equipment Sales

TMN sells mobile phones and related equipment in Portugal. Equipment sales contributed €112.4 million, €144.1 million, and €159.4 million to TMN's operating revenues in 2010, 2009 and 2008, respectively.

TMN's Commitment to the Portuguese Information Society

Under the terms of its UMTS license, TMN committed to invest in the development of the Portuguese information society. TMN's outstanding commitments were determined in May 2007 to be approximately €355 million. As part of these commitments, TMN was required to co-invest with the Portuguese Government in providing laptop computers with wireless broadband connectivity, at a discount, to teachers, students and certain other individuals through 2015. In 2007, we recorded an intangible asset and a corresponding liability on our balance sheet in the amount of €233 million, equivalent to the present value of the contributions related to those information society initiatives that are not in the ordinary course of TMN's business. In addition, in 2007 TMN assumed the payment of one-third of the commitment of Oniway, a mobile operator that withdrew from the market, in the amount of €8 million and in 2009 TMN was required to co-invest with the Portuguese Government in providing laptop computers to young students, in the amount of €11.5 million. As of December 31, 2010, our expenses relating to the liabilities recorded in 2007 and 2009 had been fully reflected in our financial statements, and the only liabilities on our balance sheet relating to our commitments under the terms of TMN's license were liabilities in the ordinary course of our business.

How We Report Personal Services in Our Financial Statements

We report our entire personal services customer category revenues within the mobile business in our financial statements.

Enterprise Services (Included in Both Our Wireline and Mobile Businesses)

We provide enterprise services to corporate and SME/SOHO customers that need diversified telecommunications solutions and integration with IT services. These services include:

- *Network services*, namely fixed voice services, fixed and mobile convergence services, broadband data, Ethernet services, digital leased lines and VSAT services, business high band Internet accesses and applications, and global services for multinational customers;

- *IT services*, namely data center services (housing and hosting), storage, application servers, private virtual servers and systems administration, desktop management services, security managed services based on a Security Operations Center, business continuity services and disaster recovery, IT infrastructure outsourcing and IT and security consultancy; and

- *Business solutions and applications*, namely unified communications, IP Centrex and voice servers, digital signage Corporate TV, business videocommunications and telepresence solutions, business process outsourcing (BPO), vertical solutions for special business market customer categories (health care, the public sector), special bundling services for small and medium-size enterprises, using the "Office Box" brand name, and outsourcing.

In addition to the service offerings described above, we provide our customers with sector-specific solutions, especially in the health, education and public sectors. We are maintaining our focus on the developing convergent offers for SMEs for specific sectors, such as "Office Box Cafés e Restaurantes" (for coffee shops and restaurants) and "Office Box Médicos e Clínicas" (for physicians and medical practices).

Services

We have developed a full range of telecommunications services for businesses, and we integrate these services (together with other services we offer, such as fixed line services and mobile services) to provide our customers with service packages. By combining our communications capabilities with our software-based integrated systems and applications, we offer integrated voice, data and image solutions, virtual private networks, convergence solutions, consultancy and outsourcing. We believe we are the primary service provider in Portugal capable of offering customers a full range of integrated and customized services.

We offer services in partnership with leading operators and service providers such as Telefónica, British Telecom, Orange and BT Infonet. We use systems and networks in partnership with Siemens, Alcatel, Cisco Systems, Motorola, Nortel Networks, Critical Software and Matra/EADS Telecom.

We lease lines and broadband capacity to large businesses for data communications and other private uses and provide related services. We also provide integrated voice and data services to corporate customers. We offer 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, Ethernet broadband services, security/firewall services and VSAT satellite communications services. In addition, we offer a new range of data, voice and Internet services, such as Intranet, Extranet and managed services, including VoIP and ToIP. 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. We use IP-based solutions to improve interconnections between companies and their employees and between customers and commercial partners through remote access. We provide a range of Ethernet broadband solutions to corporate customers. The type of solution depends on the type of service (voice, data or image), volume, priority level, and stability of information flow required by our customers.

We also provide reporting services targeted to special customers to control service level agreements and the overall performance of the network. In addition, we provide outsourced corporate network services for our customers. For example, we operate and manage the SIBS network, as well as the corporate networks of our strategic partners Caixa Geral de Depósitos, Banco Espírito Santo and CATT.

In 2010, we launched several vertical offers targeting corporate services customer category, including (1) Menu Box, an integrated multi-media service targeted at the food and beverage sector, leveraging a combination of leading software tools and hardware bundles, (2) Lex Box, a solution oriented for customers in legal services integrating fixed, mobile voice and broadband services with specialized software which enables access to legal content and (3) Corporate Fiber, a television service for customers in the health and hotel sectors with customized corporate channel, content and remote control of channel selection.

In September 2010, we announced that we had entered into a partnership with Cisco towards the development, implementation and launch of new services of cloud computing, which include virtual services and unified communications, intended to help companies adopt more efficient business models by reducing costs related to information technology.

In December 2010, we signed a collaboration agreement with SingTel, the Singapore telecommunications company. This agreement provides for: (1) sharing best practices and benchmarks in operational and commercial areas related to fiber and IPTV, (2) cooperation in research and development, including the joint creation of multiplatform applications and solutions, (3) development of innovative applications for fixed and mobile high speed networks, (4) leveraging economies of scale through joint procurement and (5) promotion of internship programs allowing the employees of both companies to share best practices and experiences.

Networks

We provide services over the largest IP/MPLS backbone in Portugal. We have points of presence in all major cities throughout Portugal, and we link our network to our customers' premises through switches and access points that we own. 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. We also provide high speed Internet access through ADSL and Ethernet.

When we receive revenues from services offered through lines leased by our subsidiary PT Prime from PT Comunicações, we typically divide the revenues between PT Prime's own direct billings to its 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.

Data Centers and Systems Integration Services

We offer an integrated range of telecommunications and information technology services to the business market. Our goal is to service all of our customers' telecommunications needs and to leverage the traditional offering of products and services from Portugal Telecom.

We have a strong and competitive position in the development of information technology solutions where communications are an integral part of the services provided. To reinforce our position as a leader in this area, we are 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, we have opened Data Centers in Lisbon and Oporto as well as in Funchal and Ponta Delgada, in the Madeira and Azores islands, respectively. These facilities allow us to provide services, such as co-location, sophisticated web hosting, ISP services, data storage, disaster recovery and ASP services.

In February 2011, we announced the construction of a new Data Center in Covilhã, Portugal, which will be a 45,000-square meter facility with installation capacity for over 50,000 servers. The Data Center has been designed to be energy efficient, including a wind park with an expected 28 towers. The Data Center will be supported by a fiber network to connect it to major global communications networks and is expected to focus on providing data storage capacity to customers outside Portugal and cloud computing services. We expect that the Data Center will become operational in 2012.

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

Marketing and Customer Care

We focus significant resources on marketing and customer care. Account managers are given clear incentives to meet and exceed sales targets. We seek to compete in Portugal on the basis of the quality of our services as well as our position as the leading supplier of integrated telecommunications and IT services. We price our various service offerings on the basis of volume, the duration of service agreements and the scope of the services offered to each customer.

We offer our corporate customers services available from other companies in the Portugal Telecom group. Our subsidiary PT.com, for example, provides significant support for product development and the marketing of Internet and ADSL access.

How We Report Enterprise Services in Our Financial Statements

We report revenues from fixed telecommunications services, including fixed line, data and corporate services, provided to corporate and SME/SOHO customers within our wireline business. We report mobile services provided to corporate and SME/SOHO customers within our mobile business.

Wholesale Services (Included in Our Wireline Business)

Wholesale services provided €491.3 million and €495.4 million to our wireline operating revenues in 2010 and 2009, respectively. The table below sets forth the total number of wholesale lines (or accesses), net wholesale additions and other information as of the dates indicated.

	As of December 31,		
	2008	**2009**	**2010**
Wholesale accesses (thousands):			
Unbundled local loops	305	281	242
Wholesale line rental	76	63	62
Fixed broadband wholesale	53	54	52
Total wholesale accesses	434	398	356
Net additions (thousands):			
Unbundled local loops	14	(25)	(38)
Wholesale line rental	(65)	(12)	(2)
Fixed broadband wholesale	(8)	1	(2)
Total wholesale accesses	(59)	(36)	(42)
Wholesale traffic (millions of minutes)	6,898	6,512	6,286

Our wholesale services consist of:

- domestic and international interconnection telephone services (including capacity-based domestic interconnection) that we provide to other telecommunications service providers in Portugal;
- provision of carrier pre-selection and number portability;
- leasing of domestic and international lines to other telecommunications service providers and Portuguese cable television operators;
- provision of ADSL (including "naked" DSL) on a wholesale basis to other ISPs;
- provision of unbundled access (including shared access) to metallic loops and sub-loops to provide broadband and voice services to other telecommunications operators in Portugal;
- provision of wholesale line rental to other telecommunications service providers in Portugal;
- provision of co-location services and access to ducts, poles and associated facilities to other telecommunications operators in Portugal;
- transmission of television and radio signals for major broadcast television companies in Portugal;
- narrowband Internet access origination services, which we provide to ISPs;
- international carrier services (transport, transit and/or termination) for international switched traffic; and
- other services provided to telecommunications service providers and operators, such as IP international connectivity.

Interconnection Traffic

Interconnection traffic comprised about 42% of our wholesale business in terms of revenues in 2010. The service providers who purchase interconnection services include fixed and mobile network operators, voice and data communications service providers, ISPs, value-added service providers and service providers whose international calls are terminated on or carried by our network. Providing interconnection services means allowing third parties to connect their networks to our network, and vice versa. We have interconnection rates namely for call termination, call origination, transits and international interconnection.

Wholesale traffic is generated by the interconnection portion of our wholesale business and increased by 1.6% in 2010 compared to 2009 and decreased by 5.0% in 2009 compared with 2008. This increase in 2010 was primarily due to increases in national terminated traffic and in wholesale operators' outgoing traffic.

Prices

Domestic interconnection revenue per minute for calls terminated on our network declined by 6% in nominal terms in 2010 compared to 2009 and by 7% in 2009 compared with 2008. International interconnection revenue per minute for wholesale operators' outgoing traffic decreased 13% in nominal terms in 2010 compared with 2009, and by 5% in 2009 compared with 2008. In accordance with EU and Portuguese regulations, our national interconnection prices are cost-oriented (with costs audited by ANACOM) plus a margin.

Table of Contents

Leased Lines

We lease lines to other telecommunications providers for fixed, mobile and data communications services, including our own subsidiaries and competitors. Leased line services involve making a permanent point-to-point connection with dedicated and transparent capacity between two geographically separate points. We offer both national terminating segments and trunk segments at the wholesale level. We also lease international circuits to national and international operators to allow them to complete their circuits (often circuits that pass through Portugal linking other countries), and we sell segments of international circuits to international operators.

The three current mobile telephone operators in Portugal, which include our subsidiary TMN, Vodafone Portugal and Optimus, are among our wireline business's largest leased line customers.

How We Report Wholesale Services in Our Financial Statements

We report substantially all of our revenues from wholesale services in the "wholesale" line item within the wireline business in our financial statements.

Other Services

We also generate revenues from our telephone directories business and from sales of telecommunications equipment.

Directories

Operating revenues from our directories business amounted to €66.2 million and €80.1 million in 2010 and 2009, respectively. We subcontract to Páginas Amarelas (an affiliated company 25% owned by us) for the publication and distribution of telephone directories throughout Portugal in return for an annual payment of approximately 72% of its gross revenues from the sale of advertising space.

Sales of Telecommunications Equipment

Revenues from sales of telecommunications equipment amounted to €46.6 million and €43.2 million in 2010 and 2009, respectively, including the sale of handsets, modems and other telecommunications equipment.

Other

We also record revenue from advertising on sapo.pt, our Internet portal, contractual penalties imposed on customers and rentals of equipment and other infrastructure.

How We Report Other Services in Our Financial Statements

We report revenues from our other services within the wireline business in our financial statements. In "*Item 5 Operating and Financial Review and Prospects Results of Operations*," we report our directories business as a separate line item within our wireline business, we report our revenues from sales of telecommunications equipment as the "Sales" line item within our wireline business and we report the remaining revenues as "Other."

Marketing

We have increased our marketing efforts aimed at customer loyalty and promoting increased use of our wireline telephone services. We aggressively promote the sale of products and services targeted to specific customers through, among other things, the rollout of flat-rate pricing plans.

Table of Contents

We use market research programs to evaluate customer satisfaction and service quality and to help develop new products. We focus our marketing on different sections of the residential and business market. We have an advanced billing and customer information system and a marketing information database that combines usage and other relevant data.

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

We have developed a distribution network through our retail service centers and agents such as supermarkets and other retail outlets. Our customer support system allows us to develop and implement strategies to sell new and expanded services to our customers. We often use telemarketing to both the residential and small and medium-sized enterprise market categories to develop closer relationships with our customers.

We have continued to pursue our strategy of market segmentation, namely our residential and business market customer categories, and established partnerships between our subsidiaries to offer integrated telecommunications solutions to corporate customers, including simpler voice services and integrated website solutions. We have also executed agreements with corporate associations to benefit small businesses.

We continue to aggressively market *Meo*, our Pay-TV service. *Meo* is an integrated offer of voice, internet and Pay-TV services and is a key component of our strategy, strengthening and differentiating our offer to residential customers. We have continued to launch innovative features to encourage subscriptions to *Meo*, including: (1) real video on demand, with DVD-like functionalities and a catalog of more than 2,500 movies, (2) catch-up TV, (3) an electronic programming guide accessible through the Internet and the mobile phone, (4) TV channel recording, which can be remotely programmed through the Internet or through the mobile phone, (5) gaming, karaoke and several interactive content and service areas, (6) access to personal photo folders and (7) customized offers for kids. We continue to add channels, features and functionalities to *Meo*. See " *Residential Services Pay-TV Services*" above.

International Operations

Brazil

Sale of Interest in Vivo

On July 28, 2010, we reached an agreement with Telefónica to sell our 50% interest in Brasilcel N.V., a joint venture that held our interest in Vivo, to Telefónica. The sale was concluded on September 27, 2010. We reflect Vivo in our statements of income and cash flows for periods prior to September 27, 2010 as a discontinued operation. As of December 31, 2010, none of the assets or liabilities of Vivo are reflected on our balance sheet.

Our audited consolidated financial statements included in this Annual Report on Form 20-F include the results of operations and cash flows of Vivo as a "Discontinued Operation" for the period prior to our sale of our interest in Vivo to Téléfonica S.A. on September 27, 2010. Vivo provides mobile telecommunications services throughout Brazil.

Oi Transaction

On January 26, 2011, we announced that we had entered into a series of agreements with Oi, Brazil's largest telecommunications group, to acquire a significant stake in that company. In connection

Table of Contents

with our agreements to establish a strategic partnership with Oi, we also agreed to merge Dedic and GPTI, our subsidiaries that provide call center and IS/IT services in Brazil, with Contax, one of the leading corporate services company and the leader in contact center services in Brazil. Contax is currently controlled by the controlling shareholders of Oi, through CTX and Contax Participações. The Oi transaction closed on March 28, 2011. We also completed the acquisition of a 16.2% stake in CTX but have not yet completed the merger of Dedic and Contax, which is subject to the approval of our board of directors and shareholders and other conditions. Following the closing of the transaction, we hold a 25.3% economic stake in Oi, and we expect to hold a 44% economic stake in CTX (42.0% prior to the merger of Dedic and Contax). See " *Strategic Alliances Strategic Partnership with Oi*" below for more information about this strategic partnership.

Other Brazilian Investments

Dedic/GPTI. Our subsidiaries Dedic and GPTI provide call center and IS/IT services in Brazil. Dedic's operating revenues were R$479.4 million in 2010 (€205.6 million), R$402.3 million in 2009 (€145.2 million) and R$307.8 million in 2008 (€115.1 million); GPTI's operating revenues were R$133 million in 2010 (€56.9 million). As of December 31, 2010, our participation in Dedic was 87.5%, and Dedic had 100% ownership of GPTI. As described above, we have agreed to merge Dedic and GPTI with Contax, subject to the approval of our board of directors and shareholders and other conditions.

UOL. On December 29, 2010, we reached an agreement for the sale of our 28.78% stake in Universo Online S.A., Brazil's largest internet provider by revenue, to a Brazilian businessman, for R$356 million. UOL's total operating revenues were R$816.7 million in 2010 (€350.5 million), R$726.4 million in 2009 (€262.2 million) and R$577.2 million in 2008 (€216.2 million).

Africa and Asia

Our subsidiary Portugal Telecom Investimentos Internacionais Consultoria Internacional, S.A. manages all of our international businesses other than our investment in Oi described above.

Operations in Africa

We have several investments in Africa, including investments in Angola, Cape Verde Islands and Namibia. In 2007, we established a strategic partnership with Helios Investors LP ("Helios"), a private equity firm operating in sub-Saharan Africa. Under the terms of the agreement, Helios acquired a 22% stake in Africatel, the holding company formed to hold all of our interests in sub-Saharan Africa and whose main assets are Unitel, Cabo Verde Telecom, MTC and CST. In 2008, Helios increased its stake in Africatel to 25%. Our interest in the individual companies described below reflects the percentage of capital of those companies owned by Africatel.

Unitel in Angola. In 2000, we acquired 25% of the share capital of Unitel, a GSM mobile operator in Angola. Unitel's other shareholders are Sonangol, which holds 25%, and other local partners, which hold the remaining 50%. Unitel began operations in Luanda in 2001. As of December 31, 2010, Unitel had 6,128 thousand subscribers, of which 99% were prepaid cards.

Unitel's total gross operating revenues were US$1,502.0 million in 2010 (€1,133.8 million), US$1,562.1 million in 2009 (€1119.9 million) and US$1269.4 million in 2008 (€863.1 million).

Cabo Verde Telecom. Africatel owns 40% of the share capital of Cabo Verde Telecom. Cabo Verde Telecom provides fixed, mobile and data services in the Cabo Verde Islands.

At December 31, 2010, Cabo Verde Telecom had 72 thousand fixed lines in service, which represents approximately 13.9 fixed main lines per 100 inhabitants. Cabo Verde Telecom had

308 thousand active mobile telephone cards at December 31, 2010, of which 99% were prepaid customers.

Cabo Verde Telecom's total gross operating revenues were €84.0 million in 2010, €76.9 million in 2009 and €73.1 million in 2008.

MTC in Namibia. In 2006, we acquired 34% of the capital of MTC, the Namibian mobile operator. In connection with this transaction, we entered into an agreement with the other shareholders of MTC that allows us to set and control the financial and operating policies of this company. As of December 31, 2010, MTC had 1,666 thousand customers, of which 94% were customers under prepaid plans. MTC's revenues were 1,444.0 million Namibian dollars (€148.9 million) in 2010, 1,443.8 million Namibian dollars (€123.7 million) in 2009 and 1,277.0 million Namibian dollars (€105.9 million) in 2008.

CST in São Tomé and Principe. Africatel owns 51.0% of the share capital of CST Companhia Santomense de Telecomunicações, S.A.R.L. ("CST"), which provides fixed, mobile and data services in São Tomé and Principe. As of December 31, 2010, CST had 102.7 thousand mobile customers. CST's revenues were €12.7 million in 2010, €11.9 million in 2009 and €9.1 million in 2008.

Operations in Asia

We have investments in Asia in CTM and in Timor Telecom.

CTM. We have a 28% interest in Companhia de Telecomunicações de Macau ("CTM"), a provider of fixed and mobile telephone services in Macau. Macau, situated near Hong Kong on the coast of Guangzhou Province, China, was a territory administered by the Portuguese government until December 1999, when it was transferred to the People's Republic of China. The other shareholders of CTM are Cable & Wireless plc and CITIC 1616.

At December 31, 2010, CTM had 178 thousand fixed main lines in service. This figure represents approximately 32.2 fixed main lines per 100 inhabitants. CTM's mobile telephone services were 515 thousand customers at December 31, 2010.

CTM's total gross operating revenues were 2,760.2 million Patacas (€260.1 million) in 2010, 2,439.2 million Patacas (€ 219.2 million) in 2009 and 2,442.0 million Patacas (€ 206.9 million) in 2008.

Timor Telecom. We also have a 41.12% interest in Timor Telecom, S.A. ("Timor Telecom"), a telecommunications provider for fixed and mobile services in East Timor. As of December 31, 2010, Timor Telecom had a total mobile customer base of 473 thousand and 3 thousand fixed lines. Timor Telecom's revenues were US$57.2 million in 2010 (€43.2 million), US$48.6 million in 2009 (€34.9 million) and US$38.5 million in 2008 (€ 26.2 million).

Shared Services Companies

PT SI. PT SI is the group unit responsible for data centers, information systems and information technology activities of our business units in Portugal. PT SI provides integrated information systems and information technology services to our business units in Portugal, as well as to our existing and new customers. We hold 100% of the share capital of PT SI.

PT Inovação. PT Inovação is our unit responsible for research and development activities. Our research and development programs focus on intelligent networks, network management systems, advanced services and systems and network integration and have led to the introduction of innovative products and services. PT Inovação's activities have been a driving force behind the development of new products and services, telecommunications infrastructure and information systems.

Table of Contents

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 our call center operations.

PT Pro. PT Pro aggregates all our back-office activities in Portugal. PT Pro takes advantage of economies of scale and process alignments throughout our group to reduce costs in back-office activities. The creation of PT Pro has also allowed for a reduction of the execution risk of our financial reporting function through standardization of processes and implementation of best practices.

PT Compras. PT Compras optimizes our purchasing function on an integrated basis, taking advantage of scale and specialization.

For a list of our significant subsidiaries, see Exhibit 8.1 to this Annual Report on Form 20-F, which exhibit is incorporated herein by reference. For further details on our percentage interest in our subsidiaries and their business activities, see the exhibits to our audited consolidated financial statements.

Strategic Alliances

Strategic Partnership with Oi

On January 26, 2011, we announced that we had entered into a series of agreements with Oi, Brazil's largest telecommunications group, aimed at acquiring a minimum 22.38% direct and indirect economic stake in Telemar Norte Leste S.A., the main operating company of Oi. In connection with our agreements to establish a strategic partnership with Oi, we also agreed to merge Dedic and GPTI, our subsidiaries that provide call center and IS/IT services in Brazil, with Contax, one of the leading corporate services company and the leader in contact center services in Brazil. Contax is currently controlled by the controlling shareholders of Oi through CTX and Contax Participações. The Oi transaction closed on March 28, 2011, except for the merger of Dedic and Contax. Following the closing of the transaction, we currently hold a 25.3% direct and indirect econominc stake in Oi and we expect to hold a 44% economic stake in CTX (42.0% prior to the merger of Dedic and Contax).

Background and History

We use the term "Oi" to refer, collectively, to Telemar Participações S.A. ("TmarPart"), its subsidiary Tele Norte Leste Participações S.A., a Brazilian company whose ADRs are listed on the New York Stock Exchange ("TNLP"), and TNLP's subsidiaries, including Telemar Norte Leste S.A. ("Telemar"), mentioned above, a Brazilian company with shares traded on the São Paulo Stock Exchange (*BM&FBOVESPA S.A. Bolsa de Valores, Mercadorias e Futuros*, or "BM&FBOVESPA"). TNLP and its subsidiaries provide telecommunications services in Brazil using the brand name "Oi", including:

- fixed-line telecommunications business in Regions I and II of Brazil, which include local and long-distance services, network usage services (interconnection) and public telephones;

- mobile telecommunications services throughout Brazil (Regions I, II and III); and

- other miscellaneous services, which include operating a fiber optic cable system that connects the United States, Bermuda, Brazil and Venezuela; an internet portal under the brand name "iG"; subscription television services and broadband internet access to the residential, commercial and corporate market categories in the cities of Belo Horizonte, Poços de Caldas, Uberlândia and Barbacena in the State of Minas Gerais through its subsidiary WAY TV Belo Horizonte S.A.; and subscription television services using DTH satellite technology in the States of Minas Gerais, Paraná, Rio Grande do Sul, Rio de Janeiro and Santa Catarina.

Table of Contents

On July 28, 2010, AG Telecom Participações S.A., or "AG Telecom," and LF Tel S.A., or "LF Tel," companies that are part of the controlling group of TNLP, and with TmarPart, TNLP and Telemar as intervening parties, entered into a letter of intent with Portugal Telecom to establish the main terms that would serve as a framework for the negotiation of our strategic partnership with Oi. On January 25, 2011, Portugal Telecom and our subsidiary Bratel Brasil S.A. ("Bratel") entered into agreements with TmarPart, AG Telecom, Luxemburgo Participações S.A. (a subsidiary of AG Telecom, hereinafter referred as "Luxemburgo" and, together with AG Telecom, "AG"), LF Tel, BNDES Participações S.A., or "BNDESPar," Fundação Atlântico de Seguridade Social, or "FASS," Caixa de Previdência dos Funcionários do Banco do Brasil PREVI, or "PREVI," Fundação Petrobrás de Seguridade Social PETROS, or "PETROS," and Fundação dos Economiários Federais FUNCEF, or "FUNCEF," to implement our strategic partnership with Oi. Under these agreements, the transactions described below have been completed.

On March 28, 2011:

- Bratel acquired from BNDESPar, PREVI, PETROS and FUNCEF an aggregate of 261,631,051 common shares issued by TmarPart, representing 9.6% of TmarPart's total outstanding common shares;

- Bratel acquired from Andrade Gutierrez Telecomunicações Ltda. and La Fonte Telecom S.A. a 35% stake in each of Pasa Participações S.A. and EDSP75 Participações S.A., respectively, holding companies that own 100% of the share capital of AG Telecom and LF Tel.

- TmarPart increased its share capital through the issuance of 186,664,449 common shares, in which transaction (1) Bratel subscribed for an aggregate of 91,225,537 common shares issued by TmarPart, representing 3.1% of TmarPart's total outstanding common shares, (2) AG Telecom and its subsidiary Luxemburgo subscribed for an aggregate of 36,784,491 common shares issued by TmarPart, representing 1.3% of TmarPart's total outstanding common shares, (3) LF Tel subscribed for an aggregate of 36,784,491 common shares issued by TmarPart, representing 1.3% of TmarPart's total outstanding common shares, and (4) FASS acquired an aggregate of 21,869,930 common shares issued by TmarPart, representing 0.7% of TmarPart's total outstanding common shares;

- TNLP increased its share capital through the issuance of 56,417,086 common shares at an issue price of R$38.5462 per share and of 28,409,175 preferred shares at an issue price of R$28.2634 per share. The aggregate proceeds received by TNLP from this capital increase amounted to R$2,978 million. In this capital increase, TmarPart and its wholly-owned subsidiary Valverde Participações S.A. subscribed for 35,309,502 common shares issued by TNLP, and Bratel acquired an aggregate of 20,752,270 common shares and 28,298,549 preferred shares issued by TNLP. Following this capital increase, TmarPart owned, and owns as of the date hereof, 22.4% of TNLP's total share capital, including 50.5% of its voting share capital, and Bratel owned, and owns as of the date hereof, an aggregate 10.5% of TNLP's total share capital, or 11.3% of its voting share capital;

- Telemar increased its share capital through the issuance of 46,969,121 common shares at an issue price of R$63.7038 per share and 58,696,856 class A preferred shares at an issue price of R$50.7010 per share. The aggregate proceeds received by Telemar from such capital increase amounted to R$5,969 million, of which R$4,624 million represented the purchase price for the shares issued by Telemar subscribed for by TNLP. In this capital increase, TNLP acquired 46,743,149 common shares issued by Telemar, and Bratel acquired an aggregate of 32,475,534 class A preferred shares issued by Telemar. Following this capital increase, TNLP owned, and owns as of the date hereof, 70.4% of Telemar's total share capital, including 98.0% of its voting share capital, and Bratel owned, and owns as of the date hereof, an aggregate of 9.4% of Telemar's total share capital.

Table of Contents

In light of the transactions mentioned above, we currently hold a 25.3% economic stake in Telemar on a consolidated basis. We hold this stake through (1) an indirect 35% stake in AG Telecom, (2) an indirect 35% stake in LF Tel, (3) a 12.1% direct stake in TmarPart, (4) a 10.5% direct stake in TNLP and (5) a direct 9.4% stake in Telemar. Given our economic stake and our rights to participate in the management of Oi as described below, we will proportionally consolidate 25.6% of TmarPart in our consolidated financial statements, which fully consolidates TNLP and Telemar.

We set forth below a simplified corporate chart showing our investment in Oi.

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(1) Includes holding companies, namely Luxemburgo Participações S.A. (controlled 100% by AG Telecom) and Pasa Participações S.A. (controls 100% of AG Telecom).

(2) Includes EDSP75 Participações S.A. (controls 100% of LF Tel).

(3) Reflects the direct and indirect stakes included in this chart and also stakes held directly by AG Telecom and LF Tel in Tele Norte Leste Participações S.A. (2.4% each) and in Telemar Norte Leste S.A. (3.3% each) and by Telemar Participações S.A. directly in Telemar Norte Leste S.A. (3.8%).

The purpose of our strategic partnership with Oi is to develop a global telecommunications platform that will allow for cooperation in diverse areas, with a view to, among other things, sharing best practices, achieving economies of scale, implementing research and development initiatives, developing new technologies, expanding internationally, particularly in Latin America and Africa, diversifying the services provided to our customers, maximizing synergies and reducing costs, and seeking to offer constant high quality services to our corporate and individual customers, while creating and adding value for our shareholders.

In this context, it is envisaged for example that, amongst other purposes, Oi will use part of the proceeds received from share capital increases to acquire up to 10% of the outstanding shares of Portugal Telecom. As of April 28, 2011, Oi had purchased 62,755,860 shares of Portugal Telecom, representing 7.0% of our outstanding shares through broker transactions.

Regulatory and Antitrust Matters

In October 2010, ANATEL approved our strategic partnership with Oi without imposing any conditions other than a requirement that Oi pay all pending administrative taxes assessed until that

Table of Contents

moment, in the amount of R$218 million approximately, and, accordingly, that Oi waive all rights it was pleading in certain administrative proceedings instituted with a view to contesting such administrative taxes. Oi sought, and has been granted, injunctive relief that has allowed it to make judicial deposits of the amounts of such taxes while preserving its rights to continue litigating the amounts assessed by ANATEL. ANATEL has appealed the injunctions benefitting Oi, but such appeals have not yet been heard as of the date hereof and thus remain pending decision.

In addition, in accordance with Brazilian antitrust laws, Portugal Telecom and Oi have jointly submitted the formation of our strategic relationship to the CADE for final approval, which remains pending, and subject to review by the CADE of to submissions by regulatory agencies relating to the strategic partnership: (1) one applicable to regulated markets, submitted by ANATEL, and (2) another applicable to non-regulated markets, submitted by the Secretariat for Economic Defense of the Brazilian Ministry of Justice (*Secretariado de Defesa Econômica*, or "SDE"). Brazilian law allowed Oi and us to complete our strategic partnership prior to receiving final approval from the CADE. In its review of the agency submissions, the CADE will determine whether or not the partnership formed with Oi has an adverse impact on the underlying competitive conditions in the markets in which Oi operates or whether or not the partnership adversely affects consumers in the markets in which Oi operates.

Corporate Governance

In connection with the formation of our strategic partnership with Oi, we have entered into various shareholders' agreements with Oi's current shareholders in order to regulate corporate governance practices within Oi, establish the rules, procedures and quorums for the approval of certain matters by Oi's board of directors, board of executive officers and within Oi's shareholder structure, rights of first offer or first refusal in the sale of Oi's shares by its shareholders, tag-along rights and other provisions, and these rights allow us to play an active role in Oi's corporate governance. For example, our shareholders' agreements contemplate, among other things, (1) a lock-up period of five years with respect to AG Telecom, LF Tel and TmarPart, a right of first refusal over a non-control sale of AG Telecom and LF Tel and over any sale of TmarPart, and a right of first offer and tag-along rights in case of a control sale of AG Telecom and LF Tel and (2) the need for our approval on certain corporate governance matters, including: (i) amendments to bylaws, (ii) mergers and acquisitions and shareholders agreements, (iii) dissolution, (iv) capital increases or reductions, (v) issuances of debt securities above a specified ratio and (vi) the annual budget and investments. We will also participate in several management committees in place or to be created at the material subsidiaries within Oi's corporate structure, including committees dedicated to finance, human resources, risks and contingencies, and will appoint the President of the Committee of Engineering & Network, Technology & Innovation and Product Offering that will be created as part of the framework agreement.

On April 28, 2011, at TNLP's annual general shareholders' meeting, Zeinal Bava, our Chief Executive Officer, and Shakhaf Wine, an executive board member, both nominated by us, were elected as members of the board of directors of TNLP, as we had announced on April 6, 2011. In addition, Messrs. Bava and Wine were appointed members of the board of directors of TmarPart. Mr. Bava will also be designated to head Oi's Committee of Engineering & Network, Technology & Innovation and Product Offering, which will be created. On April 6, 2011, we also announced that Otávio Marques de Azevedo and Pedro Jereissati, who are respectively, Chairman and Chief Executive Officer of TmarPart, were appointed to complete the 2009-2011 term office as non-executive members of our board of directors.

Described below are some specific aspects of the shareholders' agreements we have entered into in the context of the formation of our strategic partnership with Oi.

Table of Contents

TmarPart Shareholders' Agreements

On April 25, 2008, TmarPart's shareholders entered into two shareholders' agreements. The shareholders' agreement among AG Telecom, LF Tel, Asseca Participações S.A., or "Asseca," BNDESPar, Fiago and FASS as parties, having TmarPart, PREVI, PETROS, FUNCEF and Andrade Gutierrez Investimentos em Telecomunicações S.A. as intervening parties, is referred as the "Global Shareholders' Agreement". The shareholders' agreement among AG Telecom, LF Tel, Asseca and FASS as parties, having TmarPart and Andrade Gutierrez Investimentos em Telecomunicações S.A. as intervening parties, is referred as the "Control Group Shareholders' Agreement".

On June 20, 2008, Asseca assigned the TmarPart shares it held to LF Tel and Andrade Gutierrez Investimentos em Telecomunicações S.A. (currently Luxemburgo Participações S.A.). As a result, Asseca ceased to be a TmarPart shareholder and to have any rights under the Global Shareholders' Agreement or the Control Group Shareholders' Agreement.

In July 2009, Fiago assigned TmarPart shares it held to PREVI, PETROS, FUNCEF and FASS. As a result of such transaction, Fiago ceased to be a TmarPart shareholder and to have any rights under the Global Shareholders' Agreement.

On January 25, 2011, TmarPart's shareholders amended the Global Shareholders' Agreement and the Control Group Shareholders' Agreement, both effective as of March 28, 2011, to reflect our acquisition, through Bratel, of voting shares of TmarPart and to modify certain clauses of the Global Shareholders' Agreement and the Control Group Shareholders' Agreement. AG Telecom, Luxemburgo, BNDESPar, PREVI, FASS, FUNCEF, PETROS, LF Tel and Bratel are parties to the amendment to the Global Shareholders' Agreement, while TmarPart and Portugal Telecom executed the amendment as intervening parties. AG Telecom, Luxemburgo, LF Tel and FASS are parties to the amendment to the Control Group Shareholders' Agreement, while TmarPart executed such an amendment as intervening party.

Global Shareholders' Agreement

The initial term of the Global Shareholders' Agreement expires on the later of April 25, 2048 or the expiration date of the last to expire of the concessions or authorizations held by TmarPart or its subsidiaries (including any renewals thereto). The term of the Global Shareholders' Agreement may be extended for successive periods of 10 years with the consent of each of the parties thereto.

The parties to the Global Shareholders' Agreement have agreed to the following provisions with respect to elections of members of the boards of directors and executive officers, and the voting of their shares of TmarPart, TNLP, Telemar, Brasil Telecom and each of TmarPart's, TNLP's or Telemar's material subsidiaries (*i.e.*, subsidiaries having annual net operating revenues equal to or in excess of R$100 million):

- AG, LF Tel, and FASS will together have the right to designate a majority of the members of the board of directors of TmarPart and of each of the material subsidiaries;

- each increment of 7% of the voting share capital of TmarPart held by party to the Global Shareholders' Agreement entitles that party to designate one member of the board of directors of TmarPart and each of the material subsidiaries and his or her alternate;

- so long as we hold at least 7% of the voting share capital of TmarPart, we will be entitled to designate one member and the respective alternate of the board of directors of TmarPart and two members and the respective alternates of the board of directors of TNLP, such appointees to be designated from among the directors and executive officers of Bratel;

- PREVI, PETROS, FUNCEF and BNDESPar are entitled to aggregate their shares to determine their eligibility to exercise the rights described above;

- Bratel, PREVI, PETROS, FUNCEF and BNDESPar each have the right to designate one member of the board of directors of any other subsidiary, provided that AG, LF Tel and FASS have designated members of such board of directors;

- AG, LF Tel, BNDESPar, FASS, PREVI, PETROS, FUNCEF and we, through Bratel, will jointly select the chief executive officers of each of the material subsidiaries pursuant to the rules outlined in the Global Shareholders' Agreement;

- the chief executive officer of TNLP will select the members of TNLP's board of executive officers;

- the chief executive officer of TNLP, together with the chief executive officer of each of the other material subsidiaries, will select the other members of the board of executive officers of such material subsidiary;

- BNDESPar, PREVI, PETROS and FUNCEF, jointly, have the right to designate one member to the fiscal council of each of the material subsidiaries;

- AG, Luxemburgo, LF Tel, BNDESPar, FASS, PREVI, FUNCEF, PETROS and we, through Bratel, will hold pre-meetings prior to shareholders' and board of directors meetings of the material subsidiaries and will vote our TmarPart shares and instruct our representatives on the boards of directors of the material subsidiaries to vote in accordance with the decisions made at pre-meetings; and

- that approval of certain matters be subject to the supermajority vote of the shareholders (for instance, among other things, approval of changes to the bylaws of TmarPart or to the bylaws of any of its material subsidiaries, approval of donation policies, approval of investments of any kind not specifically foreseen in the budgets in excess of R$50 million and certain other matters are subject to a 75% majority; approval of, and amendments to, the annual budget of TmarPart and its material subsidiaries, capital reduction or increases, the issue of securities, proposals to pay or distribute dividends or interest on shareholders' equity in amounts below 25% of the net income, selection of auditors and certain other matters are subject to a 77% majority; sale or creation of any liens on the shares issued by the material subsidiaries, or the issue of convertible securities, the adoption of any procedure that would cause TmarPart to lose control of the material subsidiaries, any merger or spin-off transaction involving TmarPart or any of its material subsidiaries and certain other matters are subject to a 87.4% majority).

Under the Global Shareholders' Agreement, each of the shareholders party to it has agreed:

- not to enter into other shareholders' agreements with respect to its TmarPart shares, other than (1) the Global Shareholders' Agreement, (2) the Control Group Shareholders' Agreement and (3) the shareholders' agreement entered into among Bratel, Andrade Gutierrez Telecomunicações Ltda. and La Fonte Telecom S.A.;

- not to amend the Global Shareholders' Agreement, the Control Group Shareholders' Agreement or the shareholders' agreement entered into among Bratel, Andrade Gutierrez Telecomunicações Ltda. and La Fonte Telecom S.A. without the consent of all parties to the Global Shareholders' Agreement;

- to grant a right of first refusal and tag-along rights to the other parties to the Global Shareholders' Agreement with respect to any sale of its TmarPart shares, except that FASS must grant the right of first refusal for its TmarPart shares to AG and LF Tel, (ii) any sale of TmarPart shares among PREVI, PETROS and FUNCEP is not subject to the right of first refusal and (iii) PREVI, PETROS and FUNCEF must grant the right of first refusal for their TmarPart shares to BNDESPar;

Table of Contents

- that the other parties to the Global Shareholders'Agreement have the right to sell, and Bratel has the obligation to buy, up to all of the other parties' shares of TmarPart in the event that Bratel acquires control of TmarPart;

- to offer its TmarPart shares to the other parties to the Global Shareholders' Agreement in the event of a transfer of control of such shareholder, including, without limitation, in the event that Bratel acquires control of AG or LF Tel;

- that the other shareholders have the right to purchase all of Bratel's TmarPart shares in the event of a change of control of Portugal Telecom; and

- Oi will use part of the proceeds received from our investment in Oi to acquire up to 10% of the outstanding shares of Portugal Telecom. As of April 28, 2011, Oi had purchased 62,755,860 shares of Portugal Telecom, representing 7.0% of our outstanding shares through broker transactions.

Control Group Shareholders' Agreement

The initial term of the Control Group Shareholders' Agreement expires on April 25, 2048 and may be extended for successive periods of 10 years with the consent of each of the parties thereto.

Under the Control Group Shareholders' Agreement, each of the parties has agreed:

- to hold pre-meetings between themselves prior to the pre-meetings to be held pursuant to the Global Shareholders' Agreement and to vote their TmarPart shares in accordance with the decisions made at such pre-meetings;

- that any TmarPart shares sold by a party to the Control Group Shareholders' Agreement to any other party to this agreement will remain subject to this agreement; and

- that if a party to the Control Group Shareholders' Agreement sells all or part of its TmarPart shares to another party or to a third party, the purchaser(s) and the selling party, as the case may be, will be considered one voting bloc for the purposes of the Control Group Shareholders' Agreement (even if the purchaser(s) is/are already a party to the agreement) and that such voting bloc will hold pre-meetings prior to the meetings of the parties to the Control Group Shareholders' Agreement.

PASA Participações S.A. and EDSP75 Participações S.A. Shareholders' Agreements

We currently hold a 25.3% economic stake in Telemar on a consolidated basis. Part of the structure we used in order to obtain such an interest in Oi was to acquire an indirect 35% stake in AG Telecom and in LF Tel, through a direct investment in PASA Participações S.A. and EDSP75 Participações S.A., respectively. We have a 35% direct economic stake in PASA Participações S.A., and the remaining 65% economic interest in the company is held by Andrade Gutierrez Telecomunicações Ltda. Likewise, we have a 35% direct economic stake in EDSP75 Participações S.A., and the remaining 65% economic interest in the company is held by La Fonte Telecom S.A. AG Telecom is wholly owned by PASA Participações S.A., and LF Tel is wholly owned by EDSP75 Participações S.A.

In connection with our investments in PASA Participações S.A. and EDSP75 Participações S.A., on January 25, 2011, we entered into two shareholders' agreements, one with Andrade Gutierrez Telecomunicações Ltda. (in relation to PASA Participações S.A.) and another with La Fonte Telecom S.A. (in relation to EDSP75 Participações S.A.). The initial terms of these shareholders' agreements expire on April 25, 2048 but may be extended for successive periods of 10 years with the consent of each of the parties.

Table of Contents

These shareholders' agreements serve the purpose of regulating corporate governance within PASA Participações S.A. and EDSP75 Participações S.A. and streamlining decision-making process between us, Andrade Gutierrez Telecomunicações Ltda. and La Fonte Telecom S.A. in connection with our investments in Oi. For instance, under these shareholders' agreements:

- pre-meetings are to be held between the shareholders to decide in advance the matters to be analyzed during pre-meetings to be held under the Global Shareholders' Agreement and the Control Group Shareholders' Agreement; and

- approval of certain matters are subject supermajority vote of the shareholders (*e.g*, approval of, and amendments to, the annual budget of PASA Participações S.A., EDSP75 Participações S.A., AG and LF Tel are subject to an 83% majority; the entering by PASA Participações S.A., EDSP75 Participações S.A., AG or LF Tel of any loan agreements in excess of R$50 million, or the entering of any agreement imposing a pecuniary obligation on PASA Participações S.A., EDSP75 Participações S.A., AG or LF Tel in excess of R$50 million, or the granting of any guarantees by PASA Participações S.A., EDSP75 Participações S.A., AG or LF Tel in excess of R$50 million, are subject to a 90% majority; and any amendments to the Global Shareholders' Agreement or the issuance of preferred shares by PASA Participações S.A., EDSP75 Participações S.A., AG or LF Tel, the approval of any decision subject to supermajority vote under the Global Shareholders' Agreement (defined as a "material decision" under the PASA Participações S.A. and EDSP75 Participações S.A. shareholders' agreements), among other matters, are subject to the unanimous vote of the shareholders).

In addition, as long as we hold at least 17% of the voting and total share capital of each of PASA Participações S.A. and EDSP75 Participações S.A., we have the right to appoint one member to the board of executive officers of each of these companies. On the other hand, reduction in our interest in PASA Participações S.A. or EDSP75 Participações S.A. may change some of our rights under these agreements and in connection with the Global Shareholders' Agreement. For example, should our interest in PASA Participações S.A. or EDSP75 Participações S.A. be reduced to less than 20.5% of the voting share capital of either of these companies, approval of certain "material decisions," as defined in the preceding paragraph, subject to a 75% majority vote under the Global Shareholders' Agreement (for instance, approval of changes to the bylaws of TmarPart) would no longer require our consent.

These shareholders' agreements also contemplate:

- rights of first offer to the shareholders with respect to the transfer of the shares issued by PASA Participações S.A. and EDSP75 Participações S.A.;

- tag-along rights for our benefit in case of the sale of PASA Participações S.A. and EDSP75 Participações S.A. shares by Andrade Gutierrez Telecomunicações Ltda. or La Fonte Telecom S.A., as the case may be;

- a general restriction on the sale of the shares issued by PASA Participações S.A. and EDSP75 Participações S.A. by Andrade Gutierrez Telecomunicações Ltda. or La Fonte Telecom S.A, as the case may be, to our competitors; and

- a general right to PREVI, PETROS, FUNCEF and BNDESPAR, while they remain shareholders of TmarPart, or to any third parties which may acquire the shares held by these companies in TmarPart, to substitute Andrade Gutierrez Telecomunicações Ltda. or La Fonte Telecom S.A. in the exercise of their preemptive rights under the PASA Participações S.A. and EDSP75 Participações S.A. shareholders' agreements in case we decide to sell our shares in PASA Participações S.A. and/or EDSP75 Participações S.A.

Table of Contents

BNDESPar, PREVI, PETROS and FUNCEF Shareholders' Agreement

On January 25, 2011, PREVI, PETROS, FUNCEF, BNDESPAR, Andrade Gutierrez Telecomunicações Ltda. and La Fonte Telecom S.A. entered into a voting bloc shareholders' agreement. The purpose of this shareholders' agreement is to regulate the exercise of voting rights with respect to, and general governance in connection with, PASA Participações S.A. and/or EDSP75 Participações S.A. in case of the sale of our interest in PASA Participações S.A. and/or EDSP75 Participações S.A. and the acquisition of such interest by any of PREVI, PETROS, FUNCEF or BNDESPAR, in which circumstance the purchaser, or purchasers, of our interest in PASA Participações S.A. and/or EDSP75 Participações S.A. will be deemed to be a single bloc and will succeed us in all our rights and obligations. We are not party to this shareholders' agreement, and no obligation or right is imposed or conferred upon us.

Acquisition of the Interest in Contax in Connection with the Implementation of our Partnership with Oi

AG and LF Tel, two of the significant shareholders of TmarPart, are also the controlling shareholders of Contax Participações S.A. In connection with the Oi transaction, we agreed to merge Mobitel S.A. ("Dedic") and its subsidiary GPTI Tecnologia da Informação S.A. ("GPTI") with Contax S.A. ("Contax"), in return for common and preferred shares of Contax. In this transaction, we acquired a 16.2% stake of CTX Participações S.A. ("CTX"), the parent company of Contax Participações S.A. and Contax, for consideration of R$116 million. To complete the transaction, we expect to raise our stake in CTX to 19.9% through the contribution of a portion of the Contax preferred shares we will receive following the merger of Dedic and GPTI with Contax. Also in connection with this transaction, we will receive net cash of approximately R$162 million from the reimbursement by Contax of shareholder loans we had made to Dedic and GPTI and from the sale to CTX of a portion of the Contax common and preferred shares we will receive in the merger of Dedic and GPTI with Contax.

Following the completion of the entire Contax transaction, including the merger of Dedic and GPTI with Contax, we will hold a 19.5% economic stake in Contax through a 19.9% direct stake in CTX, which will hold a 34.2% of Contax, and a 4.3% direct economic stake in Contax. Our direct economic stake in Contax consists of 7.0% of Contax's outstanding common and preferred shares, which we are free to sell at any time.

In connection with this transaction, on January 25, 2011, we entered into a shareholders' agreement with the other CTX shareholders, that is, AG Telecom, Luxemburgo, LF Tel and FASS through our subsidiary Portugal Telecom Brasil S.A., effective as of March 28, 2011 (the "Contax Shareholders' Agreement"). AG Telecom, Luxemburgo, LF Tel, FASS and Portugal Telecom Brasil S.A. are parties to the Contax Shareholders' Agreement, while CTX, Portugal Telecom, Andrade Gutierrez Telecomunicações Ltda., PASA Participações S.A., La Fonte Telecom S.A. and EDSP75 Participações S.A. are intervening parties in the Contax Shareholders' Agreement.

Under the Contax Shareholders' Agreement, we have similar rights to those contained in the Global Shareholders' Agreement and the other shareholders' agreements described above, and, accordingly:

- pre-meetings are to be held among the shareholders to decide in advance the matters to be voted during any shareholders' or board of directors' meetings and the decisions taken during such pre-meetings shall be binding upon the shareholders and their representatives; and

- approval of certain matters are subject to a supermajority vote of the shareholders (for instance, approval of amendments to CTX's bylaws, of the execution of any agreements with Telemar and certain other matters are subject to a 66.67% majority; approval of CTX's annual budget and the investment plans of CTX and its subsidiaries, among other matters, are subject to a 70%

majority; approval of the sale of the shares issued by CTX's subsidiaries and of any merger, spin-off, or initial public offering involving CTX, among other matters, are subject to an 84% majority).

In addition, (i) as long as we hold at least 10% of CTX's voting share capital, we have the right to appoint two members to the board of directors of both CTX and Contax Participações; (ii) as long as we hold at least 5% of CTX's voting share capital, we have the right to appoint one member to the board of directors of both CTX and Contax Participações; (iii) as long as we hold at least 11% of CTX's voting share capital, we have the right to appoint one member to the board of executive officers of CTX. Also, under the Contax Shareholders' Agreement, we have the right to veto one among three of the nominees appointed by AG Telecom, Luxemburgo, LF Tel and FASS to the position of chief executive officer of Contax.

The Contax Shareholders' Agreement also contemplates preemptive rights to the shareholders with respect to the transfer of CTX's shares and tag-along rights in case of the sale of CTX's shares by its shareholders. More importantly, however, (i) the corporate control in any of CTX's shareholders may not be transferred without such shareholder first offering its CTX's shares to the other CTX shareholders in accordance with the procedures contained in the Contax Shareholders' Agreement concerning the rights of first offer; and (ii) should we cease to be a TmarPart shareholder, our interest in CTX may be redeemed or exchanged in accordance with the procedures established in the Contax Shareholders' Agreement.

The Contax Shareholders' Agreement was executed on January 25, 2011, and its first term expires on April 25, 2048. The term of the Contax Shareholders' Agreement may be extended for successive periods of 10 years with the consent of each of the parties thereto.

Properties

Our principal properties consist of buildings and telecommunications installations. These include various sizes of exchanges, transmission equipment, cable networks, base stations for mobile networks, equipment for radio communications and a nationwide network of ducts. They are located throughout Portugal and internationally.

Following the transfer to the Portuguese Government of the pension funds described in "*Item 5 Operating and Financial Review and Prospects Liquidity and Capital Resources Post Retirement Benefits*," Portugal Telecom acquired several buildings previously owned by those funds. Portugal Telecom and its subsidiaries own several office buildings in Portugal. Our main proprietary office space is located at the following addresses:

- R. General Humberto Delgado, 342/368, Coimbra, Portugal (13,321 square meters);
- Largo do Carmo, Faro, Portugal (11,452 square meters);
- R. Postiguinho Valadares, 12, Castelo Branco, Portugal (9,464 square meters);
- Av. Carvalho Araújo, 629, Vila Real, Portugal (9,030 square meters);
- Av. Doutor João Martins Azevedo, 21, Torres Novas, Portugal (7,112 square meters);
- Av. de Zarco, Funchal, Portugal (7,025 square meters);
- Rua 9 de Julho, Beja, Portugal (5,331 square meters);
- R. D. Estefânia 78/82, Lisboa, Portugal (4,441 square meters);

Praceta Nuno Rodrigues dos Santos, 9, Lisboa, Portugal (5,735 square meters);

R. Maria Veleda, 1, Lisboa, Portugal (4,333 square meters);

Rua Passos Manuel, 2, Lisboa, Portugal (1,395 square meters).

R. José Ferreira Pinto Basto, Aveiro, Portugal (36,030 square meters);

R. Tenente Valadim, 431/453, Porto, Portugal (21,400 square meters);

R. Afonso Costa, 4, Lisboa, Portugal (13,266 square meters);

R. Andrade Corvo, 10/14, Lisboa, Portugal (10,300 square meters).

Av. Fontes Pereira de Melo, 38/40, Lisboa, Portugal (61,534 square meters).

We have registered our important trademarks, such as "Portugal Telecom," "PT Comunicações," "PT Prime," "Telepac," "Sapo," "Meo," "TMN" and their related logos, in Portugal. We have also applied for a European Community trademark for "Portugal Telecom" and our logo. We do not own any registered patents or copyrights which are material to our business as a whole.

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

Competition

We face substantial and increasing competition. The Portuguese telecommunications' sector has been fully open to competition since January 1, 2000. The competitive conditions of each of our business segments are described below.

Competition Facing Our Portuguese Operations

Fixed Market

PT faces heavy competition from various telecommunications operators. Our primary competitors in the wireline voice market include ZON (with financial institutions as the main shareholders, as well as Kento Holding Limited with a qualified participation of 10% and Telefónica with 5.5%), Sonaecom (which is 53.2% owned by Sonae, SGPS, S.A. and 20% owned by France Telecom), Vodafone Portugal (a Vodafone Group subsidiary), Oni Telecom InfoComunicações, S.A. (60.9% owned by Riverside Europe Telecom LLC fund and 34.6% owned by Gestmin SGPS), Cabovisão (100% owned by Cogeco Cable, the fourth Canadian cable operator), AR Telecom and Colt.

Due to their shareholder structures, Vodafone Portugal and Optimus have access to substantial resources, cost synergies (*e.g.*, network and equipment costs) and best practices (*e.g.*, product development processes). In addition, by strengthening their position in the mobile business, these assets enable them to compete more directly and aggressively in the fixed-line services.

ZON, the newest telecommunications operator, was born in November 2007, after the failure of Sonaecom's attempt to take over Portugal Telecom and our subsequent spin-off of PT Multimedia. ZON is the leader of the Pay-TV business in Portugal. Nevertheless, and due to increasing competition in its core business, ZON has been aggessive in expanding into new business areas, including the fixed voice and Internet businesses.

The competitive environment has been becoming more challenging for several reasons, such as the expansion of mobile operators that entered in the fixed market, as well as the diversification of existing fixed operators that previously were more focused on one service, through the launch of bundle offers with strong focus on 3P (triple play) commercial configurations. This strategy has been followed by several players, namely *Meo* (our own brand), ZON, Cabovisão, Vodafone and Sonaecom. Among these players, Both PT and ZON have a strong 3P customer base (PT with 440k customers in 2010, a growth of 58% vis-à-vis 2009 and ZON with 642k customers, 33% up from 2009), with PT having 27% of its

56

Table of Contents

historically large fixed-line customers already with 3P, and ZON carrying 55% of its cable TV customers with 3P, according to its press release. We compete with respect to content, as well as with respect to price through the launch of bundle offers. Due to this competitive environment, our domestic consumer market has been, and will likely continue to be, very challenging.

Fixed Voice

Our wireline business faces increasingly strong competition from fixed line operators as well as from mobile players, including our own mobile service provider, TMN. By December 2010, the number of mobile subscribers in Portugal was almost four times the number of fixed lines.

Currently, all mobile network operators have commercial offers that are a direct alternative to our wireline telephone services, competing for the same customers. Residential services supported by mobile networks are offered by TMN, Optimus and Vodafone Portugal through their "Casa t fixo," "Optimus Home" and "Vodafone Casa" products, respectively.

In addition, the low-cost brands launched by TMN (Uzo), Optimus (Rede 4) and Vodafone Portugal (Directo) are designed to reach the lower-end segment of the mobile market and have also had an effect on our fixed line retail service, exacerbating the trend among consumers toward switching from fixed line to mobile service.

According to ANACOM figures, as of December 31, 2010, PT Comunicações, which provides retail services as part of our wireline business, had an estimated 60.4% market share of access lines (63.4% in 2009 and 68.5% in 2008). Using the same source and our own estimates, PT Comunicações had an estimated 59.5% market share of total outgoing traffic in 2010, a decrease of 2.6 percentage points when compared to 2009.

Measures such as call-by-call selection (introduced in January 2000) and carrier pre-selection (introduced in October 2000), as well as number portability (introduced in July 1, 2001), make it easier for our competitors to attract our customers to their services. As of December 31, 2010, according to ANACOM data, there were approximately 117 thousand lines in pre-selection, the lowest figures since 2001. This has resulted from operators being more focused on direct access commercial offers and putting strong efforts on customer migration from pre-selection configurations.

We are losing revenues from our international telephone services because large telecommunications users lease lines through which they connect to networks outside Portugal. In addition, mobile operators establish direct international interconnections with mobile or fixed-line networks outside of Portugal, enabling them to offer international telephone services without using our network. We also face indirect competition in international fixed line telephone services from calling cards and rerouting of calls by other international operators. Furthermore, VoIP increasingly enables cheaper communications than traditional public switched telephone networks. Together with falling international call prices worldwide, these factors put significant pressure on us to reduce international fixed line telephone prices. According to ANACOM data and our estimates, PT Comunicações had a 62.0% market share of international traffic in 2010, a decrease of 5.5 percentage points when compared to 2009.

The overall effect of full competition partly depends on the prices that other mobile and wireline network operators pay us to terminate communications in our network. Our termination rates are subject to regulatory review. See "*Regulation Portugal Interconnection*."

Pay-TV

Pay-TV has been at the core of the 3P bundles launched by the fixed telecom operators in the Portuguese market.

Table of Contents

According to ANACOM, the Pay-TV market has a total of 2,775 thousand customers, representing a 48.5% penetration on homes. ZON is the current market leader with a 57.9% market share, representing a 6.5% decrease from 2009. Our *Meo* brand has been steadily gaining market share, reaching 29.9% in less than three years after its launch, representing a 6.9% increase from 2009. Cabovisão has struggled to maintain its market share, with 9.4% in 2010, a 0.8% drecrease from 2009, while the remaining players have not been able to rise above their insignificant positions.

We have committed to an ambitious FTTH roll-out strategy in the past few years, reaching more than 1 million homes by the end of 2010. Zon and Cabovisão have leveraged on their coaxial cable networks to upgrade to the DOCSIS 3.0 standard. Sonaecom and Vodafone have based their offers mainly on IPTV, relying on lines leased from PT and their own FTTH network, which is being rolled out. Recently, the two joined forces to share their fiber-based networks, which they expect to reach around 400 thousand homes passed.

Fixed Broadband Interrnet

By the end of 2010, fixed broadband Internet surpassed two million customers in Portugal, with market penetration at 19.5 per 100 inhabitants, which still shows a significant upside potential.

According to ANACOM figures, we are the market leader in this service, with 46.8%, an increase of 2.3% from 2009. ZON is the second player with 33.0% of market share, up 0.8% from 2009.

Data and Corporate

We face significant competition from several operators, namely ZON, Vodafone Portugal, Sonaecom, Oni Telecom, AR Telecom and Colt. These companies compete with us in providing data communications, voice services and internet services to business customers. Customers tend to have large volumes of traffic and complex virtual private network services with data, voice and video integration.

Our competitors may use satellite-based networks, public network operators' infrastructure, leased lines and their own infrastructure to provide telecommunications services to customers. These are all alternatives to our leased lines offer. As a result of competition, we have reduced our prices for leased lines and are focusing on value-added solutions based on Internet Protocol Virtual Private Networks ("IP VPN").

Our strong investment in our FTTH network, as well as our commitment to the investment in a top-European level Data Center, allow us to take advantage of the cloud services business opportunity. Cloud services are considered to be an attractive growth point in the telecommunications industry and we intend to position ourself ahead of the competition to provide such services that will be an additional source of revenue as well as a retention and loyalty tool in our data and corporate customer category.

Wholesale

Fixed and 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 our network. This is decreasing our wholesale revenues generated from connecting mobile operators in Portugal to operators abroad.

Our interconnection business faces more direct competition now that operators are focuses on install and operate their own public wireline telephone networks, pushing more for direct access offers.

Table of Contents

Some international operators are now providing wholesale services in Portugal, including international telephone services, network interconnection, data services, and broadband access to Portuguese ISPs.

Mobile Market

TMN competes with Vodafone Portugal and Optimus, the two other mobile network operators licensed to provide mobile telephone services in Portugal. In 2005, Optimus introduced the low-cost brand "Rede 4" in response to our brand "Uzo". Vodafone Portugal also launched a similar product called Directo in 2005 targeting the same market as Uzo and Rede 4. The second wave of low cost offers emerged when virtual operators entered the Portuguese market, namely Phone-ix and ZON Mobile in 2007 and 2008, respectively.

In 2007, CTT, the Portuguese postal company, launched "Phone-ix," an MVNO (Mobile Virtual Network Operator) supported by TMN's network. In 2008, ZON launched an equivalent structure under the brand "ZON Mobile," a mobile virtual operation hosted by Vodafone Portugal's network.

In 2008, the Portuguese mobile market experienced an important development, the launch of aggressive on-net differentiated pricing plans. According to ANACOM data, on-net traffic increased 23.2% and 17.5% in 2009 and 2010, respectively. This trend is partially explained by the success of the attractive tribal plans led by Optimus (with "Tag") and followed by TMN ("Moche") and Vodafone Portugal ("Extreme" and "Extravaganza"). In addition to the tribal plans, some on-net oriented bundles of "voice+internet" were launched by the three major mobile operators, namely TMN (tmn unlimited), Optimus (Smart) and Vodafone (Best). The focus on on-net oriented flat rate plans and bundles of "voice+internet", where operators explore the concept of unlimited on-net voice calls, led to an increase of minutes of usage and an erosion of Average Revenue per Minute.

According to figures from ANACOM, at the end of 2010, TMN had a 44.1% market share in terms of mobile stations in the Portuguese market. Market share leadership is and will continue to be TMN's priority. We believe that our main mobile competitors, Vodafone Portugal and Optimus, will continue to market their services aggressively. As described above, Vodafone Portugal and Optimus each have major shareholders that provide them with substantial resources, cost synergies and best practices to compete aggressively against us in the Portuguese mobile telephone market.

By the end of 2010, there were approximately 155 active mobile cards per 100 inhabitants in Portugal, making it one of the European countries with the highest adoption rate of mobile services. This performance derives from an extremely dynamic market, where operators are devoted to providing an extended product portfolio in order to address all communication needs of all customers.

Mobile operators also undertake aggressive marketing efforts. These initiatives often offer a subscription fee that allows the access to cheaper communications during a certain period. These actions aim to increase usage in the medium term, while usually having a negative impact on retail revenues in the short term. Aggressive pricing structures and campaigns contributed to a 14.4% decrease in retail voice revenue per minute between 2009 and 2010. Additionally, voice revenues have also been threatened by changes in mobile termination rates, which declined approximately 55% (from 11 eurocents to 5 eurocents) between December 2007 and December 2010. Further reductions are expected in the near future.

Given the voice service framework, mobile operators are focused on alternative revenue streams, particularly broadband services, which have been the main engine of growth in recent years. According to ANACOM data, mobile broadband customers using dongles/modems reached 1,279 thousand by the end of 2010. This movement is largely explained by e-initiative programs launched by operators under the "information society" commitments they undertook in connection with the award of UMTS licenses. The operators' efforts to strengthen data services have resulted in growing data revenues as a percentage of service revenues, which have already reached 25% on average.

Competition Facing Oi in Brazil

Since the closing of the Oi transaction on March 28, 2011, we hold a 25.3% economic stake in Oi. Now that Telefónica has acquired Vivo from us, Vivo will be the largest competitor of our Brazilian mobile business. Vivo is now controlled by Téléfonica, a large Spanish telecommunications company with significant resources. The other principal competitors of Oi are Claro, which is controlled by a consortium led by Telecom Américas Ltd. (controlled by América Móvil S.A. de C.V., a large Mexican telecommunications company), and TIM, which is controlled by Telecom Italia, a large Italian telecommunications company.

Oi faces intense competition in all the areas in which it operates from other mobile service and fixed-line operators. Many of these competitors are part of large, national or multinational groups and 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.

Local Fixed-Line Services

In the local fixed-line telecommunication services market, competition is focused on corporate customers. In addition, competition from other telecommunication services has been increasing, particularly from mobile telecommunication services, which has led to traffic migration from fixed-line traffic to mobile traffic and the substitution of mobile services in place of fixed-line services, encouraged by offers of aggressively priced packages from some mobile telecommunication service providers. Finally, the decrease in interconnection rates has discouraged the construction of new fixed-line networks and has led to decreases in market prices for telecommunication services by enabling telecommunication service providers that use the local fixed-line networks of incumbent fixed-line providers to offer lower prices to their customers.

Oi is the leading provider of local fixed-line services in Regions I and II. As of December 31, 2010, it had 12.8 million fixed lines in service and an estimated market share of 77.5% in Region I and 7.2 million fixed lines in service and an estimated market share of 78.0% in Region II, based on information available from ANATEL. Oi's principal competitor in Region I for fixed-line services are (1) Embratel (an affiliate of Telecom Americas Group, which is a subsidiary of América Móvil, an affiliate of Telmex), which had an estimated market share of 17.8% in Region I and 6.7% in Region II, and (2) GVT (an affiliate of Vivendi S.A.), which had an estimated market share of 3.2% in Region I and 15.3% in Region II, in each case, based on information available from ANATEL.

Oi also expects competition from Embratel and GVT to increase in certain cities, such as Rio de Janeiro, Belo Horizonte and Salvador, where they continue to expand their respective local fixed-line network.

Oi expects to continue to face competition from mobile services providers, which represent the main source of competition in the local fixed-line service market. The increase in the number of mobile users, in addition to reduced mobile services rates, is expected to continue to adversely affect the number of fixed-line subscribers and the volume of local fixed-line traffic. In addition, because mobile providers offer promotions and service plans that permit subscribers to make calls within the mobile provider's network at rates that are less than those charged for calls from a fixed-line telephone to a mobile telephone, Oi believes that it may be vulnerable to traffic migration as customers with both fixed-line and mobile telephones use their mobile devices to make calls to other mobile subscribers.

Table of Contents

We believe that major technological innovations, such as instant messaging services and VoIP, may impact local fixed-line traffic in the future. In Brazil, those services have been increasing in popularity, which could put further pressure on the local fixed-line telecommunications market.

Long-Distance Services

The long-distance services market is highly competitive. For the year ended December 31, 2010, based on information available from ANATEL, of the total number of long-distance minutes originated in Region I, Oi had a market share of 15.0%, ranking behind TIM with 65.1% and Embratel with 15.4%, of the total number of long-distance minutes originated in Region II, Oi had a market share of 28.1%, ranking behind TIM with 47.1% and ahead of Embratel with 15.9%, and of the total number of long-distance minutes originated in Region III, Oi had a market share of 12.7%, ranking behind TIM with 32.3%, Telesp with 29.7% and Embratel with 19.4%.

Oi's principal competitor for long-distance services is TIM, which in 2010 began aggressively promoting its long-distance services with significant discounts. Historically, Oi's principal competitor for long-distance services has been Embratel.

New technologies that serve as an alternative to traditional long-distance telephone calls, such as VoIP, may start to capture part of Brazil's long-distance traffic.

Mobile Services

The mobile telecommunication services market in Brazil is characterized by intense competition among providers of mobile telecommunication services. Oi competes primarily with the following mobile services providers, each of which provides services throughout Brazil: (1) Vivo; (2) TIM, which is a subsidiary of Telecom Italia S.p.A. and markets its services under the brand name "TIM"; and (3) Telecom Americas Group, which markets its services under the brand name "Claro." In December 2010, Nextel Brazil acquired licenses to provide 3G services throughout Brazil. Nextel has announced that it expects to launch commercial services on its 3G network in certain markets between December 2011 and June 2012. Oi expects that Nextel's entrance in the market will increase competition for mobile services.

Competitive efforts in the Brazilian mobile telecommunication services market generally take the form of handset subsidies in the post-paid market and traffic subsidies in both the pre-paid and post-paid market. The aggressiveness of promotions is generally driven by the desire of the provider offering the promotion to increase market share; however, these promotions generally are for a short duration as the pricing terms offered are not sustainable over the long-term.

As of December 31, 2010, based on information available from ANATEL, Oi had a market share of 24.1% of the total number of subscribers in Region I, followed by Vivo with 26.9%, TIM with 26.2% and Claro with 22.2%, and Oi captured 4.8% of all net additions of mobile subscribers in Region I (calculated based on the number of mobile subscribers at the end of a period less the number of mobile subscribers at the beginning of that period) during 2010. In Region II, Oi had a market share of 15.1%, ranking behind Vivo with 30.9%, Claro with 28.7% and TIM with 25.0%, and Oi captured 9.3% of all net additions of mobile subscribers in Region II during 2010. In October 2008, Oi launched its mobile services in Region III, which represents a new competitive environment for it. As of December 31, 2010, Oi had a market share of 14.2% of the total number of subscribers in Region III, ranking behind Vivo with 34.1%, Claro with 28.5% and TIM with 23.1%. Based on information available from ANATEL, Oi captured 29.8% of all net additions of mobile subscribers in Region III during 2010.

Table of Contents

Data Transmission Services

Cable television providers that offer broadband services, particularly Net, represent Oi's principal competition in the broadband market. Oi faces competition from these providers that offer integrated packages, consisting of subscription television, broadband and voice telephone services to cable television subscribers who, in general, have more purchasing power than other consumers.

Oi's principal competitors in the commercial data transmission services market are Embratel, GVT and Intelig. Because the commercial data transmission services market is significantly less regulated than the fixed-line, long-distance and mobile services markets and, therefore, presents fewer barriers to entry, this market is subject to competition from a large number of competitors, including fixed-line telecommunication service providers and specialized services companies competing in this high-growth market and focused on large- and medium-sized business customers. Along with growth in traffic volume and increasing demand for broadband capacity, Oi expects significant price reductions in data transmission services as competitors expand their networks. Oi also anticipates a shift in competition towards value-added services provided over IP platforms.

DTH Services

In Brazil, the high quality programming of television broadcasters has resulted in aggregate ratings for these broadcasters of approximately 90% of viewers and has limited the perceived value of subscription television. As a result, the subscription television market in Brazil has a low penetration compared to developed countries and even to other South American countries such as Argentina, Chile and Mexico. Penetration rates by subscription television have grown from 8.0% of Brazilian households in 2005 to 16.7% in 2010. According to information available from ANATEL, the Brazilian subscription television market grew by more than 30.7% in 2010.

The primary providers of subscription television services in Regions I and II in Brazil are Embratel, which provides DTH service under the "Via Embratel" brand, SKY, which provides DTH services, and NET, which provides subscription television services using coaxial cable. Oi commenced offering DTH subscription television services to the low-income residential market in the State of Rio de Janeiro in July 2009, in the State of Minas Gerais in August 2009, in the State of Rio Grande do Sul in October 2009 and in the States of Paraná and Santa Catarina in November 2009. In 2010, Oi expanded this service to the Distrito Federal and the states of Bahia, Sergipe, Pernambuco, Ceará, Paraíba, Rio Grande do Norte, Alagoas and Goiás. In 2011, Oi expects to offer this service to all states of Regions I and II.

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 "*Item 8 Financial Information Legal Proceedings*."

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 privatized 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 January 1, 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.

Table of Contents

Portugal

In the competitive Portuguese telecommunications market, the regulatory measures which most affect our operations, our revenues and our costs relate to:

- restrictions on the products we offer and the prices it charges in its wireline retail business;
- restrictions on our broadband retail products through the application of retail-minus rules in those areas considered non-competitive;
- price controls on our wholesale reference offers, such as local loop unbundling, wholesale line rental, interconnection offers, ADSL bitstream offers (in those areas considered non-competitive), access to ducts, leased lines trunks and local segments;
- obligations to allow our competitors to interconnect with and use our wireline network;
- certain wireline services that we are obliged to provide to the public under our "universal service obligation";
- measures that are intended to make it easier for our customers to migrate to our competitors' services, including carrier pre-selection, number portability, unbundling of the local loop, and wholesale line rental; and
- the terms of our concession and our licenses, including the third-generation mobile license that TMN received at the end of 2000.

EU Regulatory Framework and Relevant Markets

In February 2002, the European Union agreed upon a new regulatory framework for electronic communications networks and services, consisting of five directives governing procedures, authorizations, 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 February 10, 2004 as part of Law 5/2004, the Basic Law of Electronic Communications, or "Law 5/2004." The fifth directive was adopted into law on August 18, 2004. In 2006, the European Commission began a review of the new EU framework, for electronic communications services and networks. The new regulatory package was approved on November 25, 2009 and published in the Official Journal of the European Union of December 18, 2009 (OJ L 377, 18.12.2009). The new EU Framework is due to be transposed into national law by May 26, 2011.

The implementation of the new EU framework is changing the current regulatory framework applicable to us. 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 us in Portugal.

Under the new regulatory regime, regulatory obligations can be imposed on operators having significant market power in any one of the relevant retail and wholesale markets identified by the European Commission. On December 17, 2007, the European Commission issued its European Relevant Markets Recommendation in 2007, which defines one retail market and six wholesale markets. Since we are active in all of these markets, any new regulatory measures could affect our businesses and operations.

Prior to the release of the new European Relevant Markets Recommendation, ANACOM had analyzed 16 of 18 retail and wholesale markets (as defined under a prior European Commission

Recommendation). ANACOM found 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 notified the European Commission regarding its conclusions about the markets it 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. Now, under the new European Commision Recommendation on Relevant Markets, ANACOM will be required to re-analyze the 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 conducted a market analysis to determine the regulatory obligations that should be imposed on operators with significant market power in the provision of wholesale (physical) network infrastructure access and wholesale broadband access.

Wholesale markets numbers 4 and 5 (for the provision of wholesale (physical) network infrastructure access and wholesale broadband access) were analyzed by ANACOM in 2008 and early 2009. ANACOM decided to segment the broadband market geographically between "C" (competitive) areas and "NC" (non competitive) areas. ANACOM also removed the regulation that was imposed on PT regarding wholesale broadband access in "C" areas, namely the retail-minus rule. Additionally, the obligation imposed on Portugal Telecom to provide a bitstream reference offer (Rede ADSL PT) expired after a transitional period of one year from the date of the final decision in January 2009. However, we have decided to maintain the bitstream reference offer (Rede ADSL PT). During 2011, ANACOM intends to revise relevant markets numbers 4 and 5 to integrate the changes due to the development of Next Generation Networks.

In addition to Portugal Telecom, 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. We expect that, in the near future, ANACOM will provide further analysis on relevant markets, which are leased line terminal segments, leased line transit segments, roaming services and access and call origination on mobile telephone networks. In 2010, ANACOM conducted a market analysis on the wholesale leased lines terminal and transit segments, on minimum sets of retail leased lines and on mobile termination rates. ANACOM eliminated the minimum set of retail leased lines and the retail-minus rules with respect to this set of leased lines. ANACOM found Portugal Telecom to have significant market power in the wholesale leased lines terminal market and segmented the transit segments between "C" (competitive) routes and "NC" (non competitive) routes. In these wholesale markets, ANACOM included Ethernet connections and imposed the retail-minus rule over Ethernet solutions. In the "C" routes, Portugal Telecom has no significant market power. We expect that in the near future, ANACOM will provide further analysis on the other relevant markets.

On January 7, 2009, a protocol was signed between the Portuguese government and four operators, including Portugal Telecom, on the roll-out of next-generation networks. Under this protocol, the operators committed to bring forward during 2009 the allocation of resources needed to connect 1.5 million users to a fiber optic network, working with the Portuguese government and with the national regulatory authority in the identification of existing barriers to investment in next generation networks and actively disseminating the benefits of broadband.

Moreover, with respect to the roll-out of optic fiber networks, on May 21, 2009, Decree-Law No. 123/2009 was published. This law, as amended by Decree-Law No. 258/2009, of September 25, 2009, establishes a legal framework for the construction of and access to infrastructures suitable for the accommodation of electronic communications networks and the construction of infrastructures for telecommunications in housing developments, urban settlements and concentrations of buildings. As for rights of way especially access to the public domain, expropriation and the constitution of public easements this law reinforces the rights already given to electronic communications undertakings under Law No. 5/2004 by introducing a new level of harmonization and transparency in procedures. In particular, Decree-Law No. 123/2009 sets forth several obligations in order to allow electronic communications operators to enjoy better conditions necessary for the installation and development of electronic communications networks.

Decree-Law No. 123/2009 also foresees the implementation of a Centralized Information System ("SIC") to be managed and operated by ANACOM and whose main objective is to make available information on infrastructure appropriate for the installation of electronic communications networks based on information provided by the Portuguese Government, autonomous regions, municipalities, publicly held companies or concessionaires, other entities owning or using infrastructure in the public domain of the State, autonomous regions or municipalities and electronic communications undertakings.

On December 16, 2009, ANACOM approved the launch of a public consultation process on the format providing information within the SIC.

On November 11, 2010, ANACOM approved the final decision regarding the registration of objects in the SIC and the terms and formats for providing information for the SIC. In the final report, ANACOM set forth, in particular, the objects and the defining elements that are required to be included in the SIC. Other elements, such as the terms upon which objects will be geographically defined through the combination of their administrative location and georeferencing, are also determined.

Since PT Comunicações already has a reference offer under which it is obligated to provide a substantial amount of information to operators that wish to use its ducts and associated infra-structure, we are paying close attention to the implementation of the SIC, since we do not wish for the SIC to compound PT Comunicações's obligation to provide information regarding its ducts and associated infrastructure.

Decree-Law No. 123/2009 also contained a rule regarding installing wiring in existing buildings, in which it was set forth that the first operator entering an existing building to adapt its telecommunications infrastructure to optic fiber is obligated to adapt the infrastructure to allow sharing with other electronic communications companies that wish to provide electronic communications services based on fiber. This rule ceased to be in effect on January 1, 2010 with the entering into force of the second edition of the technical rules and norms for infrastructure of telecommunications in buildings (ITED 2nd Edition). Under the ITED 2nd Edition, the first electronic communications undertaking entering a building with fiber remains obligated to install fiber optic wiring in order to allow sharing with other operators. However, ITED 2nd Edition only sets forth the technical rules that apply to installing wiring and does not solve other problems, such as those related to cost sharing, relationships of operators with the buildings' owners or management and technical harmonization needed within the sharing of the infrastructure.

Table of Contents

Regulatory Institutions

ANACOM. The *Autoridade Nacional das Comunicações*, or "ANACOM," created in January 2001 (formerly *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 our compliance with our concession. It also has certain supervisory powers with respect to our activities. The Portuguese government delegated a significant number of those powers and functions to ANACOM in our concession agreement.

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 us by our competitors, our customers and other interested parties. It can impose fines on us if we do not meet our obligations under our concession, including our obligations to supply public switched wireline telephone services, leased lines and other services to our competitors on a timely basis. ANACOM has, from time to time, addressed complaints against us by our competitors. However, such complaints have been resolved in a manner that has not had a material adverse effect on our 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 us 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 our business activities or Portuguese government regulations are inconsistent with the key provisions of the Treaty of Lisbon, also known as the TFEU Treaty, relating to competition in the EU. Article 101 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 102 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.

We understand 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 Our Concession and Existing Licenses*." Since we have not been party to the communications between the Directorates-General and the Portuguese government, we are 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. We further understand 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. We understand that in January 2009, the European Commission referred the case to the European Court of Justice. On October 7, 2010, the European Court of Justice ruled that by failing to correctly transpose into national law the provisions of European Union law governing the designation of universal service providers, the Portuguese Republic failed to fulfill its obligations under Articles 3(2) and 8(2) of Directive 2002/22/EC of the European Parliament and of the Council of March 7, 2002 on universal service and users' rights relating to electronic communications networks and services (Universal Service Directive).

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 our A shares. The European Commission believes that the special powers granted to the Portuguese government through the sole ownership of our A shares act as a disincentive for investment by other EU member states in a manner that violates European Community Treaty rules. The Portuguese authorities have taken the position that these special rights are justified in order to protect relevant public interests. In 2008, the European Commission referred the case to the European Court of Justice, and in 2009, the Advocate General in charge for the case issued an opinion stating that the Portuguese Government's ownership of our A shares does not comply with the European rules on the free movement of capital. At an Extraordinary Shareholders' Meeting held on June 30, 2010, the Portuguese Government used its A shares to reject an offer by Telefónica S.A. to purchase our interest in Brasilcel N.V., the joint venture that held our interest in Vivo, even though 73.9% of the ordinary shareholders present at the meeting voted in favor of Téléfonica's offer. On July 8, 2010, the European Court of Justice ruled that the Portuguese Government's ownership of our A shares was illegal under European law.

On January 19, 2011, the European Commission opened an investigation into an agreement between Telefónica and Portugal Telecom allegedly not to compete in the Iberian telecommunications markets. Portugal Telecom has developed various strategic partnerships with Telefónica in recent years. Although we do not believe the existence of these partnerships has impeded competition and ordinary activities of our company and Telefónica, our relationship with Telefónica is now subject to investigation. The European Commission has stated that the initiation of proceedings does not imply that the Commission has conclusive proof of an infringement but that the Commission will deal with the case as a matter of priority.

Autoridade da Concorrência. Our activities are also overseen by the 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 our business practices or other business arrangements. We and our subsidiaries are permitted under Portuguese law to appeal any adverse decision of the Autoridade da Concorrência to the courts. Such an appeal suspends the decision of the Autoridade da Concorrência pending a decision by the courts.

On February 10 and 11, 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. In 2004, we appealed to the courts regarding the seizure of certain documents by Autoridade da Concorrência, and in 2007, the Commerce Court 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. The Autoridade da Concorrência returned those documents to us in August 2007. We believe the investigation has been closed.

To our knowledge, there are also several other complaints related to our alleged anti-competitive practices in our wireline business pending before the Autoridade da Concorrência.

Table of Contents

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 2005, the Autoridade da Concorrência issued a revised statement of objections on this matter. In August 2007, the Autoridade da Concorrência imposed a fine of €38 million on PT Comunicações. PT Comunicações appealed to the Commercial Court (Tribunal do Comércio) later that month. On March 2, 2010, PT Comunicações was cleared by the Commercial Court of Lisbon of the fine imposed in 2007. On March 12, 2010, the Autoridade da Concorrência appealed the decision of the Commercial Court to the Lisbon Court of Appeals (*Tribunal da Relação*). On December 22, 2010, the Lisbon Court of Appeals confirmed the judgment of the Lisbon Commercial Court, which judgment is non-appealable.

In 2007, the Autoridade da Concorrência also accused PT Comunicações of alleged abuse of dominant position for granting discriminatory discounts on lease lines. In September 2008, PT Comunicações was notified by the Autoridade da Concorrência of its decision imposing a fine of €2.1 million for PT Comunicações' alleged abuse of its dominant position in the lease line segment. PT Comunicações considers these allegations unfounded and appealed the fine to the Commercial Court (Tribunal do Comércio) later that month. The appeal suspended the decision of the Autoridade da Concorrência pending a decision by the court.

In 2003, the Autoridade da Concorrência initiated a proceeding against PT Comunicações alleging that Telepac and TV Cabo, which were than part of the Portugal Telecom group, abused their dominant position. Specifically, the Autoridade da Concorrência alleged that our "Rede ADSL PT" wholesale offer of broadband services between May 22, 2002 and June 30, 2003 did not allow the remaining competitors to generate a sufficient profit margin. In September 2009, we announced that we had been notified by the Autoridade da Concorrência that it had concluded its investigation and had decided to impose a fine of €45.0 million on us. We strongly disagree with this ruling and appealed the decision to the Commercial Court of Lisbon later that month. We believe, among other things, that the wholesale offer was permitted under the competition law then in force (DL 371/2003) and was supervised by ANACOM. In addition, we have argued that the wholesale offer was maintained in place for 14 days after the new competition law was approved (Lei 18/2003) only to permit ANACOM to determine the terms of the new offer and that the fine imposed exceeds the maximum €1 million fine allowed under the prior competition law. We intend to defend against these proceedings vigorously. The appeal suspended the decision of Autoridade da Concorrência pending a decision by the higher court.

ERC. The *Entidade Reguladora para a Comunicação Social* ("ERC") is the independent regulatory authority for the Portuguese media. It was established by Law 53/2005 of November 8, 2005 and began activity on February 17, 2006. ERC's primary responsibilities are the regulation and supervision of all entities that undertake media activities in Portugal. ERC is a legal entity endowed with administrative and financial autonomy.

ERC is responsible for ensuring respect for fundamental rights such as freedom of the press, right to information, independence from political and economic power and freedom of speech. It is also responsible for monitoring compliance by all companies operating in the media sector, with standards for media and broadcast content, as well as for promoting the proper and effective functioning of the market where such companies operate.

ERC's decisions may affect, among others, news agencies, periodicals, radio or television operators, and radio and television broadcasters. PT Comunicações and TMN are usually considered television broadcasters, and as such we must pay ERC supervisory and regulatory fees, which are calculated based on the amount of work ERC does related to PT Comunicações and TMN, the technical complexity of matters, the geographic range of networks used by the broacasters, and the impact of the activity developed by each broadcaster.

Table of Contents

Pricing of Wireline Services

ANACOM established a pricing regime for wireline services in 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:

- The price cap applying a basket composed of residential access and domestic calls is the Portuguese Consumer Price Index ("CPI") minus 2.75%;

- The fixed component of fixed-to-mobile calls (residential and non-residential) are required to be cost-oriented, and price controls are in place in the form of a cap of €0.063 on the amount retained by the fixed operator with respect to fixed-mobile calls;

- The tariffs for domestic payphone calls are required to correspond to a maximum of three times the tariff for a residential phone call; and

- Also, since January 2007, we have been required to grant a 50% discount on our monthly fee for retired people, a price accessibility obligation that was included under the Universal Service.

In 2006, PT Comunicações submitted to the regulator a new pricing scheme that included a flat-rate plan with unlimited off-peak calls on weekdays. This new price plan was approved and came into effect in 2007. Since September 2008, off-peak calls on weekends have also been unlimited.

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.

Prices for Leased Lines. In July 2010, following ANACOM's final decision on the leased lines markets, the retail leased lines market was deregulated, which meant that our prices in this market ceased to be subject to a 26% retail-minus rule. However, for the wholesale leased lines markets, in which we were declared as the SMP operator, ANACOM decided to make Ethernet circuits subject to a retail-minus rule that is still to be defined by ANACOM.

See also "*Interconnection*" below.

Universal Service Obligations

Law 5/2004 and our concession impose universal service obligations on us 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 us accordingly. Since 2004, it has been the responsibility of ANACOM to calculate the costs of providing the universal service. We believe that obtaining significant compensation under this provision of the law will be very difficult and may not be possible.

In 2008, ANACOM issued a decision in which it refused to accept our calculations related to the costs of universal service for 2001, 2002 and 2003. ANACOM proposed to define a methodology to calculate the net costs of universal service ("NCUS") and to provide definitional clarity on the concept of "excessive burden." During 2009, with assistance from its consultants, PT Comunicações developed a methodology to calculate the NCUS for 2008, and several meetings occurred between PT Comunicações and ANACOM regarding the results obtained and the methodological choices that were made. ANACOM was expected to launch a consultation on these issues during the first half of 2010, but both consultations (on excessive burden and on the methodology to calculate the NCUS) were launched in February 2011 and continued until March 22, 2011. In the consultations, ANACOM proposed to aknowledge the existence of an excessive burden in the universal service provision from 2007 forward and to calculate the NCUS using historical cost accounting data. A final decision is expected in the coming months.

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 our proposed interconnection rates and arrangements in our 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 2004 on call origination on fixed telephone networks provided at a fixed location, 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, we are subject to price controls in these markets based on our costs and other factors and must publish a reference offer that includes these prices and quality of service standards.

Mobile Interconnection. In 2005, all mobile operators were declared to have significant market power in call termination in mobile networks market. ANACOM has imposed price controls on interconnection rates for the termination of calls on mobile networks. These reductions have had, and are expected to continue to have, a significant impact on TMN's interconnection revenues and consequently its earnings.

In May 2010, ANACOM imposed a new glide path that would reduce mobile termination rates by €0.005 per quarter, to reach €0.035 in August 2011. Following the EC Recommendation on fixed and mobile termination rates in May 2009, which requires national regulatory authorities (NRAs) to develop bottom-up LRIC cost models to regulate mobile termination rates, ANACOM is consulting on the definition of a cost model to regulate mobile termination rates. This consultation will run until May 13, 2011, and a further consultation is expected in June regarding the implementation of the cost

model and the definition of a new glide path to be set from November 2011 onwards. This expected new glide path will bring the mobile termination rates by the end of 2012 to the interval defined by the EC (€0.015 €0.030).

Internet Access. As a result of past ANACOM decisions, we offer two access regimes to ISPs: (1) the Reference Offer for Internet Access, which includes two alternative pricing methods, namely a monthly flat rate and a per minute origination charge, and under which the connection of the ISP's infrastructure to our wireline network is based on DSS1 signalling, and (2) the Reference Interconnection Offer, which includes a pricing method based on call origination, and under which the connection of the ISP's infrastructure to our wireline network is based on SS7 signalling. The ISPs determine which regime will apply to their arrangements to connect with our wireline network.

Next Generation Access Networks

In 2008, ICP-ANACOM launched a public consultation on the regulation of Next Generation Access Networks ("NGA"), which addressed several issues, namely market and technological issues, the impact of NGAs on existing networks, the development models, public policy considerations and regulatory models. In a decision announced in February 2009, ANACOM defined a segmented approach: in areas designated "C Areas," the main obligation is access to ducts, and in areas designated "NC Areas," obligations are access to ducts, access to fiber and advanced bitstream, subject to conditions.

In September 2008, the European Commission launched a consultation on a draft recommendation on the regulated access to NGAs, which intends to define general regulatory principles, as well as regulatory solutions for FTTH and FTTN, including access to ducts, the unbundling of fiber and bitstream solutions. In June 2009, the European Commission launched a second consultation on a draft recommendation on the regulated access to NGAs. In September 2010, The European Commission approved the recommendation on the regulated access to NGAs, maintaining the primary regulatory principles. During 2011, ANACOM intends to revise markets numbers 4 and 5 to integrate the changes due to the development of Next Generation Networks.

Following the public tenders for the installation, management, operation and maintenance of high-speed electronic communication networks in the Centre, North, Alentejo and Algarve Zones of Mainland Portugal, as well as in Azores and Madeira, on February 6, 2010, the Minister of Public Works and Communications announced the decision on the public tenders for the installation, management, operation and maintenance of high-speed electronic communication networks in the Centre, North, Alentejo and Algarve Zones of Mainland Portugal.

On January 19, 2011, the European Commission determined that the state aid was compatible with the EU Treaty.

Number Portability and Carrier Selection

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 in July 2001. Number portability for mobile services was introduced in January 2002.

On August 18, 2005, ANACOM approved Regulation 58/2005, which sets out the rules applicable to number portability proceedings. Due to the increase of competition and the need to promote mobile number portability, on February 4, 2009, ANACOM approved Regulation 87/2009, which amends Regulation 58/2005, as well as the respective final consultation report. Regulation 87/2009 came partially into force on March 4, 2009, and on July 20, 2009, the rules concerning technical aspects and new deadline for number portability within mobile telephone services came into effect. On July 8, 2009, ANACOM approved Regulation 302/2009, implementing an additional amendment to the number portability regulation, which clarified the method for calculating the terms applicable to the prior notice for submission of the electronic portability request and maximum response time to that request by the donor operator.

These rules are expected to be amended in the near future following the transposition of the new regulatory package into national law, particularly with respect to the term for implementation of portability, either of mobile or fixed numbers.

ANACOM has required call-by-call carrier selection to be offered by us for long distance and international calls since January 1, 2000. We have been offering it for local and regional calls since January 1, 2001 and for fixed-to-mobile calls since October 1, 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. This removes the need for customers to dial any code to connect to their selected carrier when making calls. Full carrier pre-selection has been available throughout Portugal since October 15, 2000. Regulations for carrier pre-selection were published in early 2006, extending carrier pre-selection to some non-geographic services. These regulations were revised in 2007, reinforcing contractual relations between pre-selection carriers and consumers.

Unbundling of the Local Loop

In 2000, the European Commission approved a regulation requiring wireline network operators to make the local loops 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 invest in the local loop or to rely upon the network operator's relationship with the customers. According to the regulation and Law 5/2004, we are required to maintain a reference offer for unbundled access to our local loops and related facilities and to meet reasonable requests for unbundled access to our local loops and related facilities under transparent, fair and non-discriminatory conditions. Prices charged must be cost-oriented. The conditions under which the local loop unbundling services are provided are set forth in a published reference offer for unbundled access to our local loops in accordance with terms established by ANACOM. This reference offer covers all of our main distribution framework buildings where technical and space conditions allow co-location. 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 we do not achieve such indicators. We must also provide white page directories and certain other facilities to certain specified categories of subscribers free of charge.

Internet and Related Services

Various regulatory developments may affect our Internet business. A Data Protection Directive was adopted by the European Commission in 2006, imposing data-retention obligations on operators. A law implementing this directive was published in July 2008 and requires Internet service providers and other electronic communications providers to preserve data for a specified period of time and imposes other obligations in this field. Although at present there are no specific initiatives regarding these matters, we could also be subject to other self-regulation and content-monitoring requirements that could affect our Internet business.

Table of Contents

EU Competition Directive

The European Commission issued a directive in 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. We believe that the spin-off of our interest in ZON Multimedia in November 2007 satisfied the requirements of the directive as implemented in Portugal.

Licensing Framework

The EU Authorization Directive (Directive 2002/20/EC of March 7, 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 authorization regime, whereby an operator must have a general authorization 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 authorization regime. The objective of this new authorization regime is to introduce more flexibility into the licensing framework.

Summary of Our Concession and Existing Licenses and Authorizations

Our concession is for the provision of universal service and for the operation of the terrestrial broadcasting network in Portugal, and it permits us to provide public switched wireline telephone, packet switched data (the rights to which were transferred to our subsidiary PT Prime) in X.25 mode, leased lines and telex and telegraphy services in Portugal. We also operate a digital terrestrial television platform and provide mobile telephone services, data communications services and television distribution services under the licenses granted and authorizations issued to our subsidiaries by the relevant entities (the Portuguese Government and ANACOM). The subsidiaries holding the licenses and authorizations are subject to separate financial reporting and other requirements.

Our Wireline Concession. The Portuguese government granted us a concession on March 20, 1995. The concession had an initial term of 30 years, expiring in 2025. As part of a reorganization of our business, we transferred the concession to our subsidiary PT Comunicações in 2000. The concession granted us 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% of our operating revenues from the services provided under the concession, after certain deductions. Some of our 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, we were permitted to receive economic benefits from the use of public domain assets as if we owned them completely. However, such public domain assets would have reverted to the Portuguese government without compensation when the concession expired.

In December 2002, we 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. We acquired full ownership of the basic telecommunications network for €365 million, which included the 2002 concession fee of €16.6 million. As a result of this acquisition, the terms of the concession have been modified so that PT Comunicações is no longer 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. In February 2003, Decree Law 31/2003 was enacted, establishing the basic regulatory principles supporting the terms of our modified Concession. In April

Table of Contents

2003, we entered into an agreement formally modifying the terms of our concession with the Portuguese government.

The Portuguese government retains the ability to suspend or terminate our rights under the concession. In cases of serious non-fulfillment by us of our 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 our obligations. We believe that we have the resources to fulfill all our obligations under the concession.

In addition, 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. If this occurs, we would be entitled to compensation equaling our annual average net profits for the five years prior to notification of revocation multiplied by the number of years remaining before the concession expires.

Our modified concession provides that we are exempt from all taxes, fees and charges with respect to the usage of public rights-of-way for our 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% 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. The new regime replaces Law 91/97, which granted us an exemption from municipal taxes and rights-of-way and other fees with respect to access to and installation and use of our telecommunications network in connection with our obligations under the concession. Our exemption from municipal taxes prior to the enactment of Law 91/97 is still being challenged in court. See "*Item 8 Financial Information Legal Proceedings Claims for Municipal Taxes and Fees*."

We are required to provide a special 50% discount on the monthly line rental fee to certain eligible retired and pensioner Portuguese citizens. Until December 31, 2006, the costs of providing this special discount were directly reimbursed by the Portuguese Government. In May 2007, ANACOM determined that PT Comunicações should bear the costs of providing this special discount, as part of its universal obligations, a decision that applied retroactively from January 2007. In addition, in the past, we voluntarily offered supplementary discounts to eligible senior citizens in the form of an additional 10% discount on the monthly line rental fee and a special discount on telephone calls. We phased out these supplementary discounts in July 2007 as we became burdened with the cost of the mandatory 50% discount.

The concession imposes a universal service obligation on us. 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 million if we fail to fulfill our obligations under the concession or other obligations imposed by law or stemming out of ANACOM's determinations. Disputes concerning the application and interpretation of the concession are dealt with by arbitration.

PT Prime's Data Licenses and Registrations. Our subsidiary PT Prime holds:

- a non-exclusive license to provide wireline services;
- a non-exclusive license to be a "Public Telecommunications Networks" operator; and
- all the licenses formerly held by Telepac, including a data communications license.

Our data communications license authorizes us 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 us to provide value-added services such as electronic data interchange and videotext services. In addition, the license authorizes us to construct certain network infrastructure in connection with licensed services. With respect to packet switched data, the data communications license is valid for 30 years, unless our 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 and a license to offer voice services to corporate networks and other closed groups of users.

TMN's Mobile Service License. Mobile telephone service licenses are valid for 15 years and are issued by ANACOM under Law No. 5/2004. 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% 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, 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 March 2007 and is now valid until March 16, 2022. 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.

We are 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. We are also required to provide ANACOM with information about our mobile telephone operations, including the number of customers, number and average duration of calls on a quarterly basis. We are also required to provide annual information to ANACOM about the development of infrastructure.

ANACOM began issuing UMTS licenses in January 2001. 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 allocated under the UMTS licenses enables operators to supply video and Internet content to mobile handsets at higher transmission speeds. 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 beginning of 2001, and TMN's license expires in January 2016.

In April 2004, TMN launched UMTS in Portugal with an emphasis on new services, such as video telephony and high-speed data. Since then, TMN 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.

In addition, in 2000, TMN and the other mobile operators assumed commitments to make contributions to the information society during the period through the maturity of the license in 2016. In May 2007, pursuant to an agreement between TMN and the Portuguese Government, and based on contributions already made, the outstanding commitments were valued at €355 million. Under the agreement, €260 million of this amount is to be spent on "E Initiatives," an initiative led by the

Portuguese Government to offer to school teachers and students laptops and discounted broadband services. The remaining €95 million is to be spent on subsidies for equipment, service discounts and network investments. The amount related to the "E Initiatives" was recognized as a license cost in 2007 in the amount of its net present value (€233 million), and the remaining €95 million have been and will continue to be recorded when incurred, as its expected that these investments will be made in the ordinary course of business of TMN. In addition, TMN assumed the payment of one-third of the commitment of Oniway, a mobile operator that withdrew from the market, in the amount of €8 million, and in 2009 TMN was required to co-invest with the Portuguese Government in providing laptop computers to young students, in the amount of €11.5 million. As of December 31, 2010, our expenses relating to the €233 million liability recorded in 2007 had been fully reflected in our financial statements, and the only liabilities on our balance sheet relating to our commitments under the terms of TMN's license were liabilities in the ordinary course of our business.

In July 2010, ANACOM decided, within the context of the 900/1800 MHz spectrum refarming process, to unify into a single title the conditions applicable to the rights of use of frequencies allocated to TMN for the provision of the land mobile service, in accordance with GSM 900/1800 and UMTS technologies. The authorization is valid until July 8, 2025.

DTT Services. In 2008, we were notified of the final decision of ANACOM endorsing the Draft Final Decision of the Portuguese Committee of Evaluation to allocate to us the frequency usage rights for Digital Terrestrial Television ("DTT") associated with with the system for combining more than one information stream into a single stream for transmission ("Multiplex" or "Mux"), namely Mux A (transport of free-to-air signal) and Muxes B to F (Pay-TV service). In June 2009, the ERC notified us of its final decision of granting a license to act as a TV distribution operator.

Due to changes in the process of implementation of Muxes B to F and due to the evolution of Pay-TV market, PT asked ANACOM to revoke frequency usage rights associated with Muxes B to F and asked ERC to revoke the license to act as a TV distribution operator.

ANACOM issued its draft decision on January 29, 2010, according to which ANACOM intended to revoke the act granting PT Comunicações the right to use the frequencies associated with Muxes B to F, retroactive to January 29, 2010. As to the request submitted to ERC, this authority also issued a draft decision, under which it considered that reasons of public interest prevented revoking the license granted to PT Comunicações to operate as a TV distribution operator using the frequencies allocated by ANACOM for that purpose. This draft decision was also submitted to a public consultation. The final decision, issued on March 17, 2010, maintained ERC's draft position.

On July 12, 2010, ANACOM decided to revoke the granting of rights of use of frequencies associated with Muxes B to F and, consequently, of the five titles that substantiate the rights assigned to PT Comunicações, without forfeiture of the guarantee bond. It was likewise determined that the decision of revocation is retroactive and in effect from the date of the draft decision issued by ANACOM on January 29, 2010.

On December 22, 2010, ANACOM approved the draft decision regarding the alteration of the operating channels Mux A of the DTT, assigned to PTC. Additionally, on December 22, 2010, ANACOM approved the final decision on the identification of re-transmitters and respective dates of termination of emissions of the pilot phase, provided in the detailed plan for the cessation of analogue terrestrial television emissions (switch-off plan). On December 27, 2010, citing reasons of public interest, ANACOM initiated a proceeding to change the radio channels assigned to PTC with the goal of improving efficient spectrum management and harmonize the conditions of use of frequencies in the 800 MHz band.

Table of Contents

Brazil

Overview

Oi's business, including the nature of the services it provides and the rates it charges, is subject to comprehensive regulation under the General Telecommunications Law and a comprehensive regulatory framework for the provision of telecommunication services promulgated by ANATEL. Oi provides fixed-line, domestic and international long-distance and mobile telecommunication services under concessions, authorizations and licenses that were granted by ANATEL and allow it to provide specified services in designated geographic areas, as well as set forth certain obligations with which it must comply.

Concessions and Authorizations

Under the General Telecommunications Law and ANATEL regulations, the right to provide telecommunication services is granted either through a concession under the public regime (as discussed below) or an authorization under the private regime (as discussed below). A concession is granted for a fixed period of time following a public auction and is generally renewable only once. An authorization is granted for an indeterminate period of time and public auctions are held for some authorizations. These concessions and authorizations allow service providers to provide specific services in designated geographic areas, set forth certain obligations with which the service providers must comply and require equal treatment of customers by the service providers.

Providers of public regime services, such as Oi, are subject to more obligations and restrictions than providers of private regime services. Under Brazilian law, providers of public regime services are subject to certain requirements with respect to services such as quality of service, continuity and universality of service, network expansion and network modernization. Additionally, the rates that public regime service providers may charge customers are subject to ANATEL supervision.

Regulation of Fixed-Line Services

Public Regime Concessions

Each of the public regime service providers operated under a concession agreement that expired at the end of 2005. Each of these providers entered into new concession agreements in December 2005 that extended its concessions for an additional 20-year period expiring in December 2025. Under these new concession agreements, each of the public regime service providers is required to comply with the provisions of (1) the General Plan on Universal Service that was adopted by ANATEL in June 2003, (2) the General Plan on Quality Goals that was adopted by ANATEL in June 2003, and (3) the General Plan on Competition Targets which, as of the date of this annual report, has not yet been adopted by ANATEL.

The concession agreements provide that ANATEL may modify their terms in 2010, 2015 and 2020 and may revoke them prior to expiration under some specific circumstances provided for by law and the concession agreements. The modification right permits ANATEL to impose new terms and conditions in response to changes in technology, competition in the marketplace and domestic and international economic conditions. ANATEL is obligated to engage in public consultation in connection with each of these potential modifications. The amendments of Oi's concession agreement that were expected to become effective at the end of 2010 have been delayed. ANATEL may also terminate the concessions upon the occurrence of certain events, such as an extraordinary situation jeopardizing the public interest, a provider's material failure to comply with its universalization targets or insurance requirements. In the event a concession is terminated, ANATEL is authorized to administer the provider's properties and its employees in order to continue rendering services.

Table of Contents

Rate Regulation

Public regime service providers must offer a basic service plan comprised of the following basic services: (1) installation; (2) monthly subscription; and (3) switched local minutes. Modifications of the rates charged for these basic services are determined by reference to a local rate basket that represents the weighted average of the rates for monthly subscriptions and switched local minutes. Rates for long-distance services originated and terminated on fixed lines vary in accordance with specified criteria. Modifications of the rates charged for these long-distance services are determined by reference to a long-distance rate basket that represents the weighted average of the rates for long-distance calls. The rates for international long-distance services charged by long-distance service providers other than Embratel, including Oi, all of whom provide these services under authorizations rather than concessions, are not subject to ANATEL regulation.

The concession agreements establish a price-cap mechanism for annual rate adjustments for basic service plans and domestic long-distance rates based on formulas set forth in each provider's concession agreement. The formula provides for two adjustments to the price cap based on the local rate basket, the long-distance rate basket and the use of a price index. The price cap is first revised upward to reflect increases in inflation, as measured by an index, then ANATEL applies a productivity discount factor, or Factor X, which reduces the impact of the rate readjustment provided by the index.

ANATEL is analyzing the adoption of a new Factor X regulation under which a new model of rate adjustments that is based on projected improvements in service costs may be adopted in 2011. If ANATEL were to pursue the adoption of this new model, Oi expects that public consultations regarding the new Factor X regulation would begin in 2011.

Unbundling of Local Fixed-Line Networks

On May 2004, ANATEL issued an order establishing rules for partial unbundling of the local fixed-line networks of the public regime service providers, which Oi refers to as "line sharing," and requiring the eventual full unbundling of local fixed-line networks, which will entail these providers making their entire networks available to other telecommunication service providers.

As of the date of this annual report, ANATEL has not yet adopted final unbundling rules or rates for full unbundling, although Oi expects that the rates that it would receive from other telecommunication services providers accessing its fixed-line networks will be lower than the rates it currently charges its customers for providing fixed-line and broadband internet services. As of the date of this annual report, no unbundled lines had been used by competitors in Regions I or II.

Service Restrictions

Pursuant to regulations in effect as of the date of this annual report, public regime providers are subject to certain restrictions on alliances, joint ventures and mergers and acquisitions with other public regime providers, including:

- a prohibition on holding more than 20% of the voting shares of more than one other provider of public regime services;
- a restriction on mergers between regional fixed-line service providers and mobile services providers (a prohibition that also applies to private regime companies); and
- a restriction on offering cable television services, unless the company offering public regime services has won a public auction to provide cable television services in the relevant region and no other bidders participated.

In November 2010, ANATEL announced the opening of the market for subscription television services. The pending amendments to Oi's concession agreements are expected to remove the

Table of Contents

restrictions that currently prohibit it from offering subscription television services over its fixed-line networks, permitting is to offer IP TV. Under the new regulations, ANATEL will no longer limit the number of authorizations that it will grant to provide subscription television services and will permit companies that control public regime providers to also provide subscription television services.

Regulation of Mobile Services

In September 2000, ANATEL adopted regulations that established operating rules for providers under the personal mobile service (Serviço Móvel Pessoal) regime. The regulations permitted ANATEL to grant authorizations to provide mobile telecommunication services under the personal mobile service regime. For purposes of the personal mobile service regulations, Brazil is divided into three service regions covering the same geographic areas as the concessions for fixed-line telecommunication services.

Auction of Personal Mobile Services Spectrum

Prior to the establishment of the personal mobile services regime, ANATEL had granted licenses to mobile services providers to operate in each region of Brazil using Bands A and B. In 2001 and 2002, ANATEL successfully auctioned authorizations and licenses to operators in Band D and Band E in each region. Oi was granted its initial authorization to provide personal mobile services in Region I and a license to operate in Band D in March 2001. Brasil Telecom Mobile was granted its initial authorization to provide personal mobile services in Region II and a license to operate in Band E in December 2002.

ANATEL conducted additional auctions of radio frequency licenses in 2004 and 2006. In April 2004, Brasil Telecom Mobile acquired an additional license to operate in Region II.

In December 2007, ANATEL auctioned the remaining spectrum of Bands A, B, C, D and E to existing service providers as extension blocks and auctioned additional spectrum in Band M (1.8 GHz) and Band L (1.9 GHz). In these auctions, Oi acquired (1) an authorization to provide personal mobile services in the State of São Paulo and licenses to operate using Band M throughout the State of São Paulo and Band E outside of the city of São Paulo, and (2) licenses to use additional spectrum in 12 states in Region I.

Auction of 3G Spectrum

In preparation for auctions of spectrum in Bands F, G, I and J (2.1 GHz), the use of which allows personal mobile services providers to offer 3G services to their customers, ANATEL issued regulations that divide the Brazilian territory into nine regions for purposes of operations using these frequency bands. In December 2007, ANATEL auctioned radio frequency licenses to operate on each of these frequency bands in each of the nine regions and the related licenses to use these frequency bands. In this auction, Oi acquired the radio frequency licenses necessary to offer 3G services in six of the nine regions delineated by ANATEL for 3G services (corresponding to Regions I and III under the personal mobile services regime, other than an area that consists of 23 municipalities in the interior of the State of São Paulo that includes the city of Franca and surrounding areas), and Brasil Telecom Mobile acquired the radio frequency licenses necessary to offer 3G services in two of the nine regions (corresponding to Region II under the personal mobile services regime).

Table of Contents

Interconnection Regulations

Under the General Telecommunications Law, all telecommunication service providers are required, if technically feasible, to make their networks available for interconnection on a non-discriminatory basis whenever a request is made by another telecommunication service provider. Interconnection permits a call originated on the network of a requesting fixed-line or personal mobile services provider's network to be terminated on the fixed-line or personal mobile services network of the other provider. ANATEL initially adopted General Rules on Interconnection (Regulamento Geral de Interconexão) in 1998, which were amended and restated in July 2005.

Interconnection Regulations Applicable to Fixed-Line Providers

Interconnection fees are charged at a flat rate per minute of use of a fixed-line provider's network. Interconnection rates charged by a fixed-line provider to terminate a call on its local network (the TU-RL rate) or intercity network (the TU-RIU rate) are subject to a price cap established by ANATEL. The price cap for interconnection rates varies from service provider to service provider based on the underlying cost characteristics of such service provider's network and whether such service provider has significant market power.

Fixed-line service providers must offer the same TU-RL and TU-RIU rates to all requesting providers on a nondiscriminatory basis. The price caps on interconnection rates are adjusted annually by ANATEL at the same time that rates for local and long-distance rates are adjusted. Fixed-line service providers are only required to pay interconnection fees to another fixed-line service provider for traffic in the same local area in the event that the ratio of the outbound traffic generated by that provider (measured in minutes) to the inbound traffic terminated by that provider (measured in minutes) exceeds 55% or was less than 45%. This system is designated the "bill-and-keep" system.

In 2008, ANATEL announced that the method used to determine the TU-RL rates would be based on a cost methodology, known as long-run incremental costs. However, ANATEL has not established a definitive timetable for the completion of the project. Therefore, Oi cannot predict when this new methodology will be proposed.

In 2006, the TU-RIU rates that fixed-line service providers could charge each other to use a portion of their long-distance networks to complete long-distance calls were reduced to 30% of the applicable domestic fixed line-to-fixed line long-distance rates for calls of more than 300 km.

Interconnection Regulations Applicable to Personal Mobile Services Providers

Interconnection fees are charged at a flat rate per minute of use of a personal mobile services provider's network. The terms and conditions of interconnection agreements of all personal mobile services providers, including the rates charged by the operator of the network to terminate a call on its mobile network (the VU-M rate), commercial conditions and technical issues, are freely negotiated between mobile and fixed-line telecommunication service providers, subject to compliance with regulations established by ANATEL relating to traffic capacity and interconnection infrastructure that must be made available to requesting providers, among other things. In July 2006, ANATEL adopted new regulations under which personal mobile services providers recognize interconnection revenues (and costs) for traffic in the same registration area on a gross basis based on the total traffic between personal mobile services providers' networks. This system is designated the "full billing" system.

If the providers cannot agree upon the terms and conditions of interconnection agreements, ANATEL may determine terms and conditions by arbitration. Since no agreement with fixed-line service providers could be reached regarding VU-M rates when Oi and Brasil Telecom Mobile began offering personal mobile services, ANATEL set the initial VU-M rates for each of them. Personal mobile services providers also negotiate annual rate increases for their VU-M charges with the

Table of Contents

fixed-line telecommunications providers. If the providers cannot agree upon the terms and conditions of annual rate increases, ANATEL may determine the annual rate increases by arbitration.Personal mobile services providers must offer the same VU-M rate to all requesting providers on a nondiscriminatory basis. Interconnection agreements must be approved by ANATEL before they become effective, and they may be rejected if they are contrary to the principles of free competition and the applicable regulations.

ANATEL has proposed new regulations under which the VC-1, VC-2 and VC-3 rates would be reduced from current levels, after giving effect to an inflation adjustment based on the IST, by 10% in 2012 and 10% in 2013. These proposed regulations also provide procedures for determining the reference value for VU-M rates in the event that providers cannot agree upon the VU-M applicable in their interconnection agreements. Oi expects these new regulations, as they may be modified as a result of ANATEL's further analysis, to be adopted in the second quarter of 2011.

Regulation of Interconnection Rates Charged by Providers with Significant Market Power

In 2005, ANATEL issued regulations defining a series of cost-based methods, including the fully allocated cost methodology, for determining interconnection fees charged by telecommunication service providers belonging to economic groups with significant market power based on their fixed-line or personal mobile services interconnection networks. All incumbent fixed-line service providers and all personal mobile services providers are deemed by ANATEL to belong to economic groups with significant market power in their respective service areas until ANATEL finalizes its evaluation of each provider under published criteria to determine significant market power.

In July 2006, ANATEL issued regulations regarding the fees that may be charged for the use of mobile networks by personal mobile services providers with significant market power in the mobile interconnection market. The date on which these regulations will become effective has not yet been established by ANATEL. Under these regulations, ANATEL will determine, based on a fully allocated cost model, a reference value for VU-M rates of providers that are deemed to hold significant market power, which is determined based on a number of factors. This reference value will be reassessed every three years.

ANATEL is expected to begin public consultations regarding a proposed General Plan on Competition Targets in the second quarter of 2011. Oi expects that ANATEL's proposal regarding the General Plan on Competition Targets will address a variety of matters including criteria for the evaluation of telecommunications providers to determine which providers have significant market power, regulations applicable to the wholesale markets for trunk lines, backhaul, access to internet backbone and interconnection services, and regulations related to partial unbundling and/or full unbundling of the local fixed-line networks of the public regime service providers.

Regulation of Data Transmission and Internet Services

Under Brazilian regulation, ISPs are deemed to be suppliers of value-added services and not telecommunication service providers. Telecommunication service providers are permitted to render value-added services through their own networks. In addition, ANATEL regulations require all telecommunication service providers and cable television operators to grant network access to any party interested in providing value-added services, including internet access, on a non-discriminatory basis, unless not technically feasible.

ANATEL has adopted regulations applicable to fixed-line service providers with significant market power. Under these regulations, these providers are required to make the forms of agreements that they use for EILD and SLD services publicly available, including the applicable rates, and are only permitted to offer these services under these forms of agreement. Following publication of these forms of agreement, the rates under these agreements may be increased on an annual basis by no more than the rate of inflation, as measured by the IST. ANATEL also publishes reference rates for these services. ANATEL is expected to begin public consultations regarding a proposed General Plan on Competition Targets in the second quarter of 2011. Oi expects that ANATEL's proposal regarding the General Plan on Competition Targets will address a variety of matters including criteria for the evaluation of telecommunications providers to determine which providers have significant market power, regulations applicable to the wholesale markets for trunk lines, backhaul, access to internet backbone and interconnection services, and regulations related to partial unbundling and/or full unbundling of the local fixed-line networks of the public regime service providers.

ITEM 4A UNRESOLVED STAFF COMMENTS

None.

ITEM 5 OPERATING AND FINANCIAL REVIEW AND PROSPECTS

You should read the following discussion in conjunction with our audited consolidated financial statements and the accompanying notes included elsewhere in this report. Our audited consolidated financial statements have been prepared in accordance with International Financial Reporting Standards, or "IFRS," as adopted by the European Commission for use in the European Union. As of and for the years ended December 31, 2008, 2009 and 2010, there was no difference between IFRS, as adopted by the European Commission for use in the European Union, as applied by Portugal Telecom, and IFRS as issued by the International Accounting Standards Board.

Overview

Our Business and Revenue Reporting Categories

Portugal Telecom, SGPS, S.A. is a group holding company. Our business operations are conducted by our subsidiaries, which are classified for financial reporting purposes according to the general type of telecommunications services provided and the manner in which our management views and manages our operations. Portugal Telecom's businesses consist of the following:

Portuguese Operations	Offering the following residential, wholesale and enterprise services within our wireline business: Retail services, including fixed line telecommunications service, internet services, IPTV and satellite Pay-TV services to residential customers; Wholesale services; and Data and corporate services, including data communications, leased lines, outsourcing and net solutions and Internet business-to-business to large corporate entities and to SMEs/SOHOs. Offering personal (mobile) services, such as voice, data and Internet-related services and Pay-TV, through TMN.

Table of Contents

International Operations

International investments, other than our former interest in Vivo (which is presented as a discontinued operation) and our investment in Oi (which occurred after December 31, 2010), our international investments mainly include:

- Dedic/GPTI, providing call center and IS/IT services in Brazil, which we fully consolidate in our audited consolidated financial statements;
- Cabo Verde Telecom, providing fixed and mobile telecommunications services in the Cabo Verde Islands, which we fully consolidate in our audited consolidated financial statements;
- MTC, providing mobile telecommunications services in Namibia, which we fully consolidate in our audited consolidated financial statements;
- Timor Telecom, providing mobile telecommunications services in Timor, which we fully consolidate in our audited consolidated financial statements;
- Unitel, providing mobile telecommunications services in Angola, which we account for using the equity method; and
- CTM, providing fixed and mobile telecommunications services in Macao, which we account for using the equity method.

Business Drivers and Measures

The businesses of each of our segments are affected by a number of significant industry trends. In operating our businesses and monitoring their performance, we also pay attention to a number of operational and other factors. We summarize some of these trends and factors for each of our business segments below.

Wireline Business

Traffic Trends. In recent years, we have experienced a decrease in traffic on our fixed line network, primarily as a result of the trend among consumers to use mobile phones rather than fixed line service and increasing competition from mobile operators, other fixed line operators and, more recently, cable and VoIP providers. This decrease in traffic has negatively affected both our retail and wholesale revenues. However, in the fourth quarter of 2010, positive net additions of fixed lines were achieved for the first time in seven years, primarily due to strong performance of *Meo* double-play and triple-play offers. See "*Item 4 Information on the Company Our Businesses Wireline Business Fixed Line Network*" and " *Traffic*."

Changes in Revenue Mix. Our Pay-TV customers have increased since we introduced Pay-TV service in 2008. In addition, our ADSL retail accesses increased by 16.1% in 2010 due to our marketing of service packages that include Pay-TV and ADSL broadband services, with our overall ADSL revenues increasing by 3.7%, notwithstanding the effects of regulatory changes in the last several years (requiring, among other things, unbundling of the local loop, as described elsewhere in this annual report) which continued to lead to downward pricing pressure for our ADSL wholesale services. The mix of the revenues of our wireline business has therefore shifted significantly in recent years, with Pay-TV related revenues partially offsetting the continued pressure on the traditional voice business. In addition, in the future we expect that Pay-TV and broadband services will continue to be an important driver of our wireline business, and the architecture and regulation of the developing fiber optic network in Portugal will be an important factor affecting our business and revenues.

Decreasing Fixed Line Calling Prices and Greater Focus on Pricing Plans. Retail calling prices, particularly for regional, national and international calls, have been decreasing steadily in recent years, which have negatively affected our retail revenues. One of our strategies in response to this trend has been to aggressively market a variety of pricing plans to promote customer loyalty in our competitive market. Our pricing plans tend to increase our revenues from fixed charges but contribute to a decrease in our traffic revenues, particularly with respect to the growing percentage of pricing plans that offer calls at a flat rate. In our wholesale business, the decrease in regulated fixed-to-mobile interconnection charges has also affected our revenues because our wholesale wireline unit records revenue from international incoming calls through our network that terminate on the networks of mobile operators. Decreases in transit traffic (calls that use our network but neither originate nor terminate on our network) also have affected our wholesale revenues. See "*Item 4 Information on the Company Our Businesses Wireline Business Retail Fixed Line Telephone Services*" and " *Wholesale Prices*."

Increasing Competitive Pressure. Our wireline business faces increasingly strong competition from fixed line operators (including VoIP providers) as well as from mobile players. The telecommunications sector underwent a major transformation in Portugal, with the consolidation of a new operator in 2007 ZON Multimedia. This, coupled with increased commercial aggressiveness from Sonaecom, Vodafone and other corporate solution operators, has enhanced competition in the Portuguese telecommunications sector. Our major competitors compete through their respective multi-play offers, which include traditional voice services as well as Pay-TV and broadband Internet services and, on the corporate side, complex telecom and IT/IS solutions.

Mobile Business

Decreasing Interconnection Charges. In 2005, ANACOM declared all mobile operators, including TMN, to have significant market power in call termination in the mobile networks market. As a result, ANACOM imposed price controls on interconnection charges that caused both fixed-to-mobile and mobile-to-mobile interconnection rates to decrease by an average of 11% in 2008, 32% in 2009 and 10% in 2010. In May 2010, ANACOM imposed a new glide path that would reduce mobile termination rates to €0.035 in August 2011. Both interconnection rates reached €0.05 per minute at the end of 2010. These reductions have had a significant adverse impact on TMN's revenues and results of operations. See "*Item 4 Information on the Company Our Business Personal Services Prices and Revenue Breakdown.*"

Continuing Introduction of New Products. The fast development and availability of new access devices are leading to significant growth in Internet users, and more frequent usage, thus leading to increased bandwidth consumption. Examples of this trend are smartphones, tablet PCs and Internet pads. In 2010, Portugal Telecom continued to develop and introduce a diversified product offering in the mobile market, including touch-screen phones, smartphones and tablet PCs, making available to our customers data and value added services and sophisticated applications and widgets. See "*Item 4 Information on the Company Personal Services Services.*"

Continuing Roll-Out of 3G Services. One of the ways in which we respond to intense competition in the mobile networks market is by continuing to develop and bring to market innovative third generation (3G) services that increase revenues and customer loyalty. We list several of our

Table of Contents

recently launched services in "*Item 4 Information on the Company Personal Services Services*". Remaining competitive requires continuing investments to build out our third generation network and develop new services, and our capital expenditures on our third generation network have increased in recent years.

Introduction of new pricing plans. One of the ways in which we and our competitors are responding to intense competition in the mobile market is by creating new, simple and more aggressive pricing plans which better fits customer needs. TMN recently launched "e" plans, including voice, SMS and internet access, with different options allowing our customers to choose the plan that best fits their needs.

International Operations

Continuing Importance of the Brazilian Market to Our Results of Operations. Although we sold our interest in Vivo to Telefónica S.A. on September 27, 2010, we announced on July 28, 2010 that we intended to enter into a strategic partnership with Oi, the Brazilian telecommunications company. See "*Item 4 Information on the Company Our Businesses Strategic Alliances Strategic Partnership with Oi.*" We closed the Oi transaction on March 28, 2011. Unde the terms of this transaction, we will have a role in the management of Oi, allowing us to share the control of its strategic financial and operating decisions and, as a result, we expect to proportionally consolidate the results of operations of Oi in our results of operations. The results of operations of Oi, and the dynamics of the Brazilian telecommunications markets, will be important to our future operations.

All our business segments are subject to significant competition and operate in highly regulated environments. You should carefully review "*Item 4 Information on the Company Competition*" and " *Regulation*" for more information. In addition, you should be aware of the risks to which each of our businesses is subject. See "*Item 3 Key Information Risk Factors*."

Seasonality

Although our revenues and costs fluctuate from quarter to quarter, we do not experience large fluctuations due to seasonality. We tend to have higher revenues in the fourth quarter due to promotional campaigns centered on the Christmas holiday. To a lesser degree, promotional campaigns at the time of the Easter and Mother's Day holidays also tend to increase our revenues in the second quarter. Our revenues from our Portuguese operations tend to be lower during the Portuguese summer holidays during the third quarter.

Discontinued Operations Vivo

On July 28, 2010, we reached an agreement with Telefónica to sell our 50% interest in Brasilcel N.V., a joint venture that held our interest in Vivo, to Telefónica. The sale was concluded on September 27, 2010. Until the sale, we provided mobile telecommunications services in Brazil through Vivo. Our consolidated statements of income and cash flows present Vivo under the caption "Discontinued Operations" for all periods, and our consolidated balance sheet as of December 31, 2010 no longer includes the assets and liabilities related to Vivo.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with IFRS. We summarize our significant accounting policies, judgments and estimates in Note 3 to our audited consolidated financial statements. Our reported financial condition and results of operations are sensitive to accounting methods, assumptions and estimates that underlie preparation of the financial statements.

We base our estimates on historical experience and on various other assumptions, the results of which form the basis for judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

We believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our consolidated financial statements.

Property, Plant and Equipment, and Intangible Assets

Accounting for property, plant and equipment, and intangible assets involves the use of estimates for determining fair value at the acquisition date, in the case of assets acquired in a business combination, and for determining the expected useful lives of those assets. The determination of the fair values of assets, as well as of the useful lives of the assets is based on management's judgment.

The determination of impairments of property, plant and equipment, and intangible assets involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. Impairment analysis is based on a large number of factors, such as changes in current competitive conditions, expectations of growth in the telecommunications industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of services, current replacement costs, prices paid in comparable transactions and other changes in circumstances that indicate an impairment exists. The determination of recoverable amounts and fair values are typically based on discounted cash flow methodologies that incorporate reasonable market assumptions. The identification of impairment indicators, the estimation of future cash flows and the determination of fair values of assets (or groups of assets) require management to make significant judgments concerning the identification and validation of impairment indicators, expected cash flows, applicable discount rates, useful lives and residual values. As of December 31, 2010, we concluded that the carrying value of these assets did not exceed their recoverable amounts.

Goodwill

Goodwill arising on consolidation represents the excess of the cost of acquisition over our interest in the fair value of the identifiable assets and liabilities of a subsidiary at the date of acquisition. The assets and liabilities acquired are measured provisionally at the date on which control is acquired, and the resulting value is reviewed in a maximum period of one year from the date of acquisition. Until the fair value of the assets and liabilities has been definitively determined, the difference between the cost of acquisition and the carrying amount of the company acquired is recognized provisionally as goodwill.

In accordance with IFRS, at the end of each reporting period, we review the goodwill of each cash-generating unit for impairment (*i.e.*, a reduction in its recoverable amount to below its carrying amount) and write it down if necessary. The recoverability analysis of goodwill is performed systematically at the end of each year or whenever it is considered necessary to perform such an analysis. The recoverable amount is the higher of the estimated selling price of the asset less the related selling costs and value in use. Value in use is taken to be the present value of the estimated future cash flows. In calculating the recoverable amount of goodwill, we used the value in use approach for all cases, preparing the projections of future pre-tax cash flows on the basis of the budgets most recently approved by our Board of Directors. These budgets include the best available estimates of the income and costs of the cash-generating units using industry projections, past experience and future expectations. These projections cover the coming four years, and the flows for future years are estimated by applying reasonable growth rates.

In light of the fact that analyzing the impairment of our recorded goodwill requires a combination of various assumptions and variables, it is very difficult to analyze the sensitivity of the projections to changes in any isolated variable on its own, since a change in one variable may have an effect on one or more of the other variables used.

Table of Contents

The goodwill impairment analysis that we conducted as of December 31, 2010 did not suggest that any such impairment was likely in a future period.

The determination of the recoverable amount of a cash-generating unit under IFRS for impairment testing purposes involves the use of estimates by management. Methods used to determine these amounts include discounted cash flow methodologies and models based on quoted stock market prices. Key assumptions on which management has based its determination of fair value include ARPU (monthly average revenue per user), subscriber acquisition and retention costs, churn rates, capital expenditures and market share. These estimates can have a material impact on fair value and the amount of any goodwill write-down.

Accrued Post Retirement Liability

As of December 31, 2010, we recorded an accrued post retirement liability amounting to €966.9 million to cover our net unfunded obligations regarding pension supplements, post retirement healthcare benefits and salaries for pre-retired and suspended employees. We estimate our obligations regarding post retirement benefits based on actuarial valuations prepared annually by our actuaries, which use the projected unit credit method and consider certain demographic and financial assumptions. The key financial assumptions affecting post retirement benefit costs are based, in part, on actuarial valuations, including discount rates used to calculate the amount of the post retirement benefit obligations. The discount rate reflects the weighted average timing of the estimated defined benefit payments (duration of approximately 14 years for pension supplements and healthcare obligations and 4 years for salaries). The discount rate premium is determined based on European corporate bonds with a high quality rating. The assumptions concerning the expected return on plan assets are determined on a uniform basis, considering long-term historical returns, asset allocation and future estimates of long-term investment returns. In the event that further changes in assumptions are required with respect to discount rates and expected returns on invested assets, the future amounts of our post retirement benefit costs may be materially affected.

Provisions and Adjustments

Provisions are recorded when, at the end of the period, we have an obligation to a third party that is probable or certain to create an outflow of resources to the third party, without at least equivalent return expected from the third party. This obligation may be legal, regulatory and contractual in nature. It may also be derived from our practice or from public commitments having created a legitimate expectation for such third parties that we will assume certain responsibilities. To estimate the expenditure that we are likely to bear to settle its obligation, our management takes into consideration all of the available information at the closing date for its consolidated financial statements. If no reliable estimate of the amount can be made, no provision is recorded; information is then presented in the notes to the financial statements.

Contingencies, representing obligations which are neither probable nor certain at the time of drawing up the financial statements, and probable obligations for which the cash outflow is not probable are not recorded. Information about them is presented in the notes to the consolidated financial statements.

Because of the inherent uncertainties in the foregoing evaluation process, actual losses may be different from the original estimated amount provisioned at the closing date.

The allowance for doubtful accounts receivable is stated at the estimated amount necessary to cover potential risks in the collection of overdue accounts receivable balances. A determination of the amount of allowances required is made after careful analysis of the evolution of accounts receivable balances, and, in specific cases, our analysis is also based on our knowledge of the financial situation of our customers. The required allowances may change in the future due to changes in economic conditions and our knowledge of specific issues. Future possible changes in recorded allowances would impact our results of operations in the period that such changes are recorded.

Assessment of the Fair Value of Financial Instruments

We choose an appropriate valuation method for financial instruments not traded in an active market based on our knowledge of the market and of the asset. In this process, we apply the valuation methods commonly used by market practitioners and use assumptions based on market rates.

Assessment of the Fair Value of Certain Assets Using the Revaluation Model

In 2008, we adopted the revaluation model for measuring the carrying value of certain classes of assets, namely the ducts infrastructure and real estate assets. In order to determine the revalued amount of those assets, we used the replacement cost method for the ducts infrastructure and the market value for real estate assets, which required the use of certain assumptions related to construction costs for the ducts infrastructure and the use of specific indicators for the real estate market, respectively. See Notes 3(c) and 34.4 to our audited consolidated financial statements for a more detailed explanation of the assumptions used.

Recent IFRS Accounting Pronouncements

Several new IFRS standards became effective in the year ended December 31, 2010, but most of these are not applicable to us or had no material impact on our consolidated financial statements. As of the date of the issuance of the financial statements included in this Annual Report on Form 20-F, the following standards, revised standards and interpretations had been issued by IASB and IFRIC (some of those not yet endorsed by the European Union) and had not yet been adopted by Portugal Telecom, but their adoption will be required in subsequent periods:

IAS 24, Related Party Disclosures

A revised version of IAS 24, *Related Party Disclosures*, is applicable for annual periods beginning on or after January 1, 2011, modifying the definition of a related party and simplifying disclosures for government-related entities. There will be no material impact on our financial statements as a result of this revised standard.

IFRIC 19, Extinguishing Financial Liabilities with Equity Instruments

In November 2009, the IFRIC issued Interpretation 19, *Extinguishing Financial Liabilities with Equity Instruments*. The interpretation explained the recording by an entity when the periods for a financial liability are renegotiated and result in the issuance by the entity of property instruments to a creditor of the entity to terminate all or part of the financial liability (conversion of the debt). This requires that a gain or loss be acknowledged in the results, which is measured as the difference between the book value of the financial liability and the fair value of the property instruments issued. If the fair value of the financial instruments issued cannot be measured in a reliable manner, the property instruments must be measured to reflect the fair value of the terminated financial liability. This statement will apply to the financial statements for the fiscal years initiated on or after July 1, 2010. To date, we have not entered into transactions of this nature.

Table of Contents

Results of Operations

Our results reflect the changing patterns in our business described above in " *Overview*." The following tables set forth the contribution to our consolidated operating revenues of each of our major business lines, as well as our major consolidated operating costs and expenses, for the years ended December 31, 2008, 2009 and 2010.

	Year Ended December 31,							
	2008		2009			2010		
	EUR Millions	% of Operating Revenues	EUR Millions	% of Operating Revenues	% Increase of Item	EUR Millions	% of Operating Revenues	% Increase of Item
Continuing Operations Operating revenues:								
Wireline business	**1,805.6**	**48.0%**	**1,796.5**	**48.1%**	**(0.5)%**	**1,766.2**	**47.2%**	**(1.7)%**
Retail	952.3	25.3%	970.1	26.0%	1.9%	967.5	25.9%	(0.3)%
Wholesale	386.8	10.3%	371.4	9.9%	(4.0)%	364.9	9.8%	(1.7)%
Data and corporate	279.5	7.4%	295.1	7.9%	5.6%	281.5	7.5%	(4.6)%
Directories	90.2	2.4%	80.1	2.1%	(11.2)%	66.1	1.8%	(17.4)%
Sales	50.5	1.3%	42.5	1.1%	(15.8)%	44.1	1.2%	3.6%
Other	46.4	1.2%	37.3	1.0%	(19.6)%	42.1	1.1%	13.0%
Mobile business	**1,512.4**	**40.2%**	**1,460.4**	**39.1%**	**(3.4)%**	**1,336.0**	**35.7%**	**(8.5)%**
Services	1,355.9	36.1%	1,313.8	35.2%	(3.1)%	1,224.8	32.7%	(6.8)%
Sales	148.5	3.9%	134.4	3.6%	(9.5)%	102.4	2.7%	(23.8)%
Other	8.0	0.2%	12.3	0.3%	54.0%	8.7	0.2%	(29.2)%
Other businesses	**443.2**	**11.8%**	**476.5**	**12.8%**	**7.5%**	**640.1**	**17.1%**	**34.3%**
Services	420.5	11.2%	444.4	11.9%	5.7%	597.3	16.0%	34.4%
Sales	18.7	0.5%	20.3	0.5%	8.5%	19.1	0.5%	(5.6)%
Other	4.1	0.1%	11.8	0.3%	188.0%	23.7	0.6%	100.6%
Total operating revenues	**3,761.2**	**100.0%**	**3,733.4**	**100.0%**	**(0.7)%**	**3,742.3**	**100.0%**	**0.2%**
Costs, expenses, losses and income:								
Wages and salaries	489.4	13.0%	546.7	14.6%	11.7%	637.1	17.0%	16.5%
Direct costs	520.8	13.8%	522.4	14.0%	0.3%	547.6	14.6%	4.8%
Costs of products sold	244.8	6.5%	207.3	5.6%	(15.3)%	179.9	4.8%	(13.2)%
Marketing and publicity	87.9	2.3%	78.6	2.1%	(10.5)%	81.1	2.2%	3.2%
Supplies and external services	695.6	18.5%	733.3	19.6%	5.4%	724.5	19.4%	(1.2)%
Indirect taxes	45.9	1.2%	57.8	1.5%	25.9%	45.4	1.2%	(21.4)%
Provisions and adjustments	29.0	0.8%	30.5	0.8%	5.3%	35.0	0.9%	14.6%
Depreciation and amortization	647.5	17.2%	716.9	19.2%	10.7%	758.6	20.3%	5.8%
Net post retirement benefits costs	44.8	1.2%	89.6	2.4%	100.3%	38.2	1.0%	(57.4)%
Curtailment and settlement costs	100.0	2.7%	14.8	0.4%	(85.2)%	145.5	3.9%	882.9%
Gains on disposals of fixed	(18.3)	(0.5)%	(2.0)	(0.1)%	(89.3)%	(5.5)	(0.1)%	183.4%

assets, net								
Other costs, net	22.6	0.6%	45.6	1.2%	102.2%	141.2	3.8%	209.6%

89

Table of Contents

	Year Ended December 31,							
	2008		2009			2010		
	EUR Millions	% of Operating Revenues	EUR Millions	% of Operating Revenues	% Increase of Item	EUR Millions	% of Operating Revenues	% Increase of Item
Income before financial results and taxes	**851.3**	**22.6%**	**691.9**	**18.5%**	**(18.7)%**	**413.8**	**11.1%**	**(40.2)%**
Net interest expense	205.4	5.5%	227.5	6.1%	10.7%	185.0	4.9%	(18.7)%
Net foreign currency exchange losses (gains)	(3.6)	(0.1)%	0.2	0.0%	(105.9)%	6.8	0.2%	3101.2%
Net gains on financial assets and other investments	(12.1)	(0.3)%	(8.1)	(0.2)%	(33.3)%	(1.9)	(0.0)%	(76.9)%
Equity in earnings of affiliated companies, net	(171.0)	(4.5)%	(456.0)	(12.2)%	166.7%	(141.7)	(3.8)%	(68.9)%
Net other financial losses	13.7	0.4%	35.7	1.0%	161.3%	33.3	0.9%	(6.8)%
Income before taxes	**818.9**	**21.8%**	**892.6**	**23.9%**	**9.0%**	**332.2**	**8.9%**	**(62.8)%**
Income taxes	204.8	5.4%	185.9	5.0%	(9.2)%	77.5	2.1%	(58.3)%
Net income from continuing operations	**614.1**	**16.3%**	**706.7**	**18.9%**	**15.1%**	**254.6**	**6.8%**	**(64.0)%**
Discontinued operations								
Net income from discontinued operations	81.7	2.2%	82.5	2.2%	1.0%	5,565.4	148.7%	6649.1%
Net income	**695.8**	**18.5%**	**789.2**	**21.1%**	**13.4%**	**5,820.1**	**155.5%**	**637.5%**
Attributable to:								
Non-controlling interests	119.7	3.2%	104.5	2.8%	(12.8)%	147.9	4.0%	41.6%
Equity holders of the parent	**576.1**	**15.3%**	**684.7**	**18.3%**	**18.9%**	**5,672.2**	**151.6%**	**728.4%**

Year Ended December 31, 2010 Compared to Year Ended December 31, 2009

Operating Revenues

Our operating revenues increased to €3,742.3 million in 2010 from €3,733.4 million in 2009, an increase of 0.2%, due to our strong performance in our international operations, namely MTC in Namibia, Timor Telecom and Dedic/GPTI, partially offset by lower revenues from our Portuguese operations. Contributions to consolidated operating revenues from the wireline and mobile businesses decreased by 1.7% (€30.3 million) and 8.5% (€124.5 million), respectively. Other businesses increased by 34.3% (€163.6 million) for the reasons explained below.

Our revenues in Portuguese operations in the year ended December 31, 2010 were negatively impacted by, among other things, (1) lower customer revenues in our mobile business (€74.4 million), (2) lower equipment sales (€25.1 million), (3) lower mobile termination rates (€13.4 million) and (4) lower revenues from the directories business (€14.0 million). The performance of customer revenues reflected challenging economic conditions, coupled with increasing competition for youth customers and lower roaming-out revenues, which declined as a result of regulated tariff cuts.

We present below the revenue information for each of our business segments. The revenue information for each segment in the tables below differs from the contribution to our consolidated revenues for each such segment in the table above because it is presented on a stand-alone basis and includes revenues from services rendered to other Portugal Telecom group companies.

Wireline Business. The table below sets forth the operating revenues from our wireline business in 2009 and 2010. As described in more detail in "*Item 4 Information on the Company Our Businesses Portuguese Operations,*" our wireline business includes revenues from residential services and wholesale services and the majority of our revenues from services to enterprises, including large corporate entities and SMEs/SOHOs.

	2009	2010	% Change
	(EUR Millions)		
Wireline Operating Revenues (Stand-Alone)			
Retail	971.0	969.2	(0.2)%
Wholesale	495.4	491.3	(0.8)%
Data and corporate	300.7	287.7	(4.3)%
Other wireline services	180.6	180.8	0.1%
Total	**1,947.8**	**1,929.0**	**(1.0)%**

Retail revenues decreased by 0.2% to €969.2 million in 2010 from €971.0 million in 2009. Our retail revenues benefitted from continued strong performance of our *Meo* triple-play offers (voice, data and Pay-TV), which mitigated the recent revenue loss trend in the wireline business. This performance of retail revenues was achieved mainly by our growth in Pay-TV and fixed broadband retail services, which are growing in line with our stated strategy of increasing market share in the residential market by offering attractive triple-play and double-play services. The increase in revenues from our *Meo* services was more than offset by decreases in wholesale, data and corporate, and directories revenues, as described below, resulting from continuing strong competition from other fixed and cable operators as well as from mobile operators, both in voice and broadband, and against a backdrop of challenging economic conditions.

Wholesale revenues decreased by 0.8% to €491.3 million in 2010 from €495.4 million in 2009, primarily as a result of the 1.0% decrease in leased lines revenues and the 5.2% decrease in other wholesale revenues, notwithstanding an increase of 1.6% in traffic revenues. This performance is explained by the decline in ULL, wholesale line rental and wholesale ADSL revenues in 2010 (€7 million).

Data and corporate revenues decreased by 4.3% to €287.7 million in 2010 from €300.7 million in 2009, as a result of a 6.0% decline in revenues from VPN and leased lines, against a backdrop of challenging economic conditions affecting SME/SOHO and corporate customers, primarily due to strong pricing pressure. This performance is also explained by some lumpiness in relation to the execution of certain large contracts, in some cases delayed due to economic conditions and lack of financial flexibility as well as the reduction in some structural projects.

Other wireline services remained flat in 2010, with a 17.3% decline in directories (€13.8 million), reflecting the negative trend of the directories business, offset by an increase in equipment sales of 7.8% and an increase in other services.

Mobile Business. The table below sets forth the operating revenues from our mobile business in 2009 and 2010.

	2009	2010	% Change
	(EUR Millions)		
Mobile Operating Revenues (Stand-Alone)			
Services rendered:			
Billing	1,198.9	1,122.7	(6.4)%
Interconnection	161.0	141.9	(11.9)%
Sales	144.1	112.4	(22.0)%
Other operating revenues	13.7	10.4	(24.0)%
Total	**1,517.8**	**1,387.5**	**(8.6)%**

Table of Contents

Operating revenues from our mobile business decreased by 8.6% to €1,387.5 million in 2010 from €1,517.8 million in 2009, primarily due to (1) lower customer revenues (€74.4 million) against a backdrop of increased penetration of tribal plans (which are flat-fee prepaid tariff plans offering unlimited voice and SMS traffic for customers using the same tariff plan), especially by youth customers, and lower roaming-out revenues (€4.8 million), primarily due to regulated tariff cuts, (2) lower equipment sales (€31.7 million) and (3) lower interconnection revenues (€19.1 million), partially as a result of the negative impact of lower mobile termination rates (€11.9 million). Notwithstanding the economic environment and the significant growth in fixed broadband on the back of the triple-play bundles, data revenues declined only by 0.9% in 2010 and accounted for 24.6% of service revenues, an increase of 1.5 percentage points over 2009.

Other Operations. Operating revenues from our other operations contributed €640.1 million to our consolidated operating revenues in 2010, an increase of 34.3% from €476.5 million in 2009. This performance was mainly due to (1) the increases of 30.3% and 20.1% at Timor Telecom and MTC, respectively, (2) the improving trends of our Brazilian BPO business, Dedic, and (3) the consolidation of GPTI, an IT/IS company acquired by Dedic as from March 1, 2010.

Costs, Expenses, Losses and Income

As explained in more detail below, our costs increased in 2010 due to, among other factors, increases in net curtailment and settlement costs, wages and salaries, depreciation and amortization and other costs, which were partially offset by reductions in post retirement benefits costs and costs of products sold. For more detail on these costs and expenses as they relate to each of our segments, see Note 7 to our audited consolidated financial statements.

Wages and Salaries. Wages and salaries, including employee benefits and social charges, increased by 16.5% to €637.1 million in 2010 from €546.7 million in 2009, primarily due to higher contributions from (1) Dedic, our call center operation in Brazil, arising from investments made in 2010 to expand this business and also from the impact of the appreciation of the Brazilian Real (€23.2 million); and (2) GPTI, which was consolidated as from March 1, 2010 (€34.2 million).

Direct Costs. Direct costs increased by 4.8% to €547.6 million in 2010 from €522.4 million in 2009, primarily due to an increase at the wireline business (€29.4 million), with the growth in programming costs resulting from the continued growth in Pay-TV customers, strengthened content offerings and a higher uptake of premium and VOD services. The increases in these costs were partially offset by a reduction in interconnection costs, mainly due to lower mobile termination rates and lower costs related to the directories business as a result of the decline in that business. The growth in the wireline business was partially offset by a reduction at TMN, reflecting lower mobile termination rates and a higher proportion of on-net traffic.

Costs of Products Sold. Costs of products sold decreased by 13.2% to €179.9 million in 2010 from €207.3 million in 2009, primarily reflecting a reduction at TMN (€41.6 million) in line with the decrease in sales and our continued focus on increasing the number of exclusive handsets and reducing the breadth of TMN's handset portfolio.

Marketing and Publicity. Marketing and publicity costs increased by 3.2% to €81.1 million in 2010 from €78.6 million in 2009, primarily reflecting higher contributions from MTC, and from the wireline business, especially the marketing of Pay-TV and triple-play offers. These effects were partially offset by a lower contribution from TMN in line with the reduction in operating revenues.

Supplies and External Services. Supplies and external services decreased by 1.2% to €724.5 million in 2010 from €733.3 million in 2009. This decrease is primarily explained by a lower contribution from TMN, mainly due to lower maintenance and repair costs resulting from a more integrated and efficient

Table of Contents

management of our fixed and mobile networks, and lower external supplies, which reflect our continuing operational and cost discipline. These effects were partially offset by (1) the impact of the consolidation of GPTI as from March 1, 2010 (€15.9 million) and (2) an increase in costs from our contact center operations in Brazil, primarily related to rental costs in connection with the construction of new sites completed in 2010 and also related to the appreciation of the Brazilian Real.

Indirect Taxes. Indirect taxes decreased by 21.4% to €45.4 million in 2010 from €57.8 million in 2009, reflecting primarily an increase in credit risk, mainly due to a reduction in spectrum fees, and a reduction in certain foreign operations.

Provisions and Adjustments. Provisions and adjustments increased by 14.6% to €35.0 million in 2010 from €30.5 million in 2009, largely due to an increase in the wireline business (€12.1 million), reflecting primarily a change in the criteria for the calculation of provisions for receivables, partially offset by a reduction in TMN (€6.6 million) resulting from the declining trend in revenues.

Depreciation and Amortization. Depreciation and amortization costs increased by 5.8% to €758.6 million in 2010 from €716.9 million in 2009, primarily reflecting a higher contribution from the wireline business (€27.1 million), as a result of the investments in the continued rollout of our Pay-TV service, and the accelerated depreciation of certain GSM network equipment at TMN, following the decision to roll-out a swap of TMN's 2G network equipment for new equipment that is 4G-enabled.

Post Retirement Benefits. We recorded a €38.2 million charge for post retirement benefits in 2010, compared to €89.6 million in 2009. The decrease in this caption is primarily explained by a prior year service gain recorded in 2010, amounting to €31.2 million, resulting from changes introduced in the pension formula by Portuguese Law 3-B/2010 related to a reduction in benefits granted to employees. Adjusting for this effect, post retirement benefit costs would have decreased by €20.2 million, primarily due to (1) the reduction of €104.6 million in post retirement liabilities that occurred during 2009, (2) the increase in fair value of plan assets occurred in 2009, from €2,131.6 million to €2,369.5 million as a result of the performance of the plan assets and contributions to the pension funds and (3) a reduction of the discount rate from 5.75% to 5.50%. This cost item does not include early termination costs related to our workforce reduction program, which are discussed under "*Curtailment and Settlement Costs*" below.

Curtailment and Settlement Costs. Curtailment costs increased to €145.5 million in 2010, compared to €14.8 million in 2009, primarily due to reengineering of processes and reorganization of our company along customer categories (*i.e.* residential, personal, enterprise (corporate and SMEs/SOHOs) and wholesale).

Other Costs. Other costs increased to €141.2 million in 2010 from €45.6 million in 2009, primarily as a result of (1) the recognition of provisions and adjustments in order to reflect the recoverable amount of certain assets and estimated losses with legal actions and (2) expenses incurred related to the Oi acquisition.

Financial Income and Expenses

Net Interest Expenses. Net interest expenses decreased by 18.7% to €185.0 million in 2010 from €227.5 million in 2009, primarily as a result of a decrease in average net debt (debt minus cash and cash equivalents) following the first installment received from Telefónica in September 2010 (€4,500 million) for the disposal of our stake in Vivo. This effect was slightly offset by an increase in the average cost of debt, which was 4.4% in 2010 and 4.3% in 2009.

Net Foreign Currency Exchange Losses. We had net foreign currency losses of €6.8 million in 2010, compared to €0.2 million in 2009, primarily as a result of the impact of the depreciation of the U.S. dollar against the Euro during the second half of 2010 on dividends paid by Unitel in June 2010.

Table of Contents

Net Gains on Financial Assets and Other Investments. We recorded net gains on financial assets and other investments of €1.9 million in 2010, compared to €8.1 million in 2009. Gains recorded in 2009 are primarily explained by a gain of €5.7 million related to the impact on a free-standing cross currency derivative of the appreciation of the U.S. dollar against the Euro until April 2009, when this financial instrument was settled. This caption also includes the impact of the change in fair value of interest rate derivatives.

Equity in Earnings of Affiliated Companies. Equity in earnings of affiliated companies decreased to €141.7 million in 2010, compared to €456.0 million in 2009, with the decline explained mainly by (1) one-time charges in 2010 totalling €35.9 million to adjust the carrying values of certain of our investments to the corresponding estimated recoverable amounts, primarily in UOL in order to adjust its carrying value to the recoverable amount obtained upon the disposal of this investment, which was completed in January 2011, (2) the capital gain, amounting to €267.0 million, obtained with the sale of Médi Télécom in the fourth quarter of 2009 and our share in the earnings of this company until its sale and (3) the impact of the devaluation of the Kwanza against the Euro. Adjusting for these effects, equity in earnings of affiliates would have amounted to €192.1 million in 2010 and €178.4 million in 2009, as a result of increased earnings of Unitel, in local currency, and UOL. On December 29, 2010, we reached an agreement for the sale of our stake in UOL (28.78% of UOL's share capital) for a consideration of R$ 356 million. The transaction closed on January 27, 2011.

Net Other Financial Expenses. Net other financial expenses decreased to €33.3 million in 2010, compared to €35.7 million in 2009, and include banking services expenses, commissions, financial discounts and other financing costs.

Income Taxes

Income taxes amounted to €77.5 million in 2010, compared to €185.9 million in 2009, corresponding to effective tax rates of 23.3% and 20.8%, respectively. In 2010, this caption includes a gain of €59.0 million related to a corporate restructuring of Africatel businesses that resulted in lower taxable profits. Adjusting for this effect and for the non-taxable gain related to the sale of Médi Télécom (€267.0 million recorded in the fourth quarter of 2009), one-time losses recognized in 2010 without a tax impact and higher interest expenses that were non-deductible for tax purposes, income taxes would have amounted to €136.6 million in 2010, corresponding to an effective tax rate of 28.8%, compared to 26.6% in 2009. This increase in the effective tax rate is primarily explained by an increase in the statutory tax rate in Portugal.

Income from Continued Operations (Before Discontinued Operations and Non-Controlling Interests)

Income from continued operations (before discontinued operations and non-controlling interests) decreased by 64.0% to €254.6 million in 2010 from €706.7 million in 2009 for the reasons described above.

Net income from our wireline business decreased to €10.1 million in 2010 from €171.5 million in 2009, primarily due to increases in curtailment and settlement costs, direct costs, depreciation and amortization costs and other costs. These effects were partially offset by the reduction in post retirement benefit costs.

Net income from our mobile business decreased by 15.7% to €270.4 million in 2010 from €320.7 million in 2009, primarily due to the reduction in services rendered net of the related direct costs. These effects were partially offset by the effects of our cost discipline efforts, which led to reductions in commercial costs and supplies and external service expenses.

Table of Contents

Income from Discontinued Operations

Income from our discontinued operation, which related to Vivo, amounted to €5,565.4 million in 2010, compared to €82.5 million in 2009. The income recorded in 2010 included a gain of €5,423.0, net of related expenses, obtained from the sale of our investment in Vivo, which was completed on September 27, 2010. We received €4.5 billion from Téléfonica on September 27, 2010 and a further €1.0 billion on December 30, 2010. Excluding this effect and positive foreign currency translation adjustments transferred to net income (€31.9 million in 2010 and €21.6 million in 2009) following a share capital reduction at Brasilcel N.V., the joint venture vehicle that held our interest in Vivo, this caption reflects the net income of Vivo, which increased primarily due to an improvement in financial expenses and the appreciation of the Brazilian Real.

Net Income Attributable to Non-Controlling Interests

Net income attributable to non-controlling interests in 2010 amounted to €147.9 million and was related primarily to Vivo (€61.3 million), Africatel (€33.9 million), MTC (€24.9 million) and Cabo Verde Telecom (€14.2 million). In 2009, net income attributable to non-controlling interests amounted to €104.5 million and was related primarily to Vivo (€42.6 million), MTC (€22.4 million), Africatel (€11.3 million) and Cabo Verde Telecom (€17.4 million).

Net Income Attributable to Equity Holders of the Parent

For the reasons described above, our net income attributable to equity holders of Portugal Telecom increased to €5,672.2 million in 2010 from €684.7 million in 2009.

Basic earnings per ordinary and A shares from total operations in 2010 increased to €6.48 in 2010 from €0.78 in 2009 on the basis of 896,512,500 shares issued at December 31, 2010 and 2009.

Year Ended December 31, 2009 Compared to Year Ended December 31, 2008

Operating Revenues

Our operating revenues decreased to €3,733.4 million in 2009 from €3,761.2 million in 2008, a decrease of 0.7%, reflecting lower contributions from: (1) TMN (€52.0 million), whose revenues decreased by 3.4% primarily due to the negative impact of the 32% decline in mobile termination rates, notwithstanding net additions of 319 thousand during the year, equivalent to a 4.6% increase in the customer base, and (2) the wireline business (€9.1 million), with the impact of line loss and pricing pressure on retail revenues largely offsetting continued strong performance of our *Meo* triple-play offer. These effects were partially offset by an increase in the contribuition of other businesses (€33.2 million) for the reasons explained below.

We present below the revenue information for each of our business segments. The revenue information for each segment in the tables below differs from the contribution to our consolidated revenues for each such segment in the table above because it is presented on a stand-alone basis and includes revenues from services rendered to other Portugal Telecom group companies.

Table of Contents

Wireline Business. The table below sets forth the operating revenues from our wireline business in 2008 and 2009.

	2008	2009	% Change
	(EUR Millions)		
Wireline Operating Revenues (Stand-Alone)			
Retail	953.5	971.0	1.8%
Wholesale	488.5	495.4	1.4%
Data and corporate	286.5	300.7	5.0%
Other wireline services	203.0	180.6	(11.0)%
Total	**1,931.4**	**1,947.8**	**0.8%**

Retail revenues increased by 1.8% to €971.0 million in 2009 from €953.5 million in 2008, primarily as a result of continued strong performance of our *Meo* triple-play offer (voice, data and video), which in turn mitigated fixed line net disconnections, which stood at 96 thousand in 2009 compared to 173 thousand in 2008 and 313 thousand in 2007. Retail revenues improved over the course of the year due to significant growth in Pay-TV customers and in high quality broadband customers. This improvement in performance of retail revenues occurred notwithstanding strong competition from other fixed and cable operators as well as from mobile operators, both in voice and broadband, and against a backdrop of challenging economic conditions.

Wholesale revenues increased by 1.4% to €495.4 million in 2009 from €488.5 million in 2008, as a result of higher sales of leased lines, notwithstanding lower traffic revenues, which decreased by 22.3%, primarily as a result of the negative impact of the decline in mobile termination rates.

Data and corporate revenues increased by 5.0% to €300.7 million in 2009 from €286.5 million in 2008, as a result of a 36.6% increase in revenues from network management, outsourcing and IT, which more than offset the 11.8% decrease in revenues from VPN and leased lines.

Mobile Business. The table below sets forth the operating revenues from our mobile business in 2008 and 2009.

	2008	2009	% Change
	(EUR Millions)		
Mobile Operating Revenues (Stand-Alone)			
Services rendered:			
Billing	1,193.7	1,198.9	0.4%
Interconnection	231.2	161.0	(30.3)%
Sales	159.4	144.1	(9.6)%
Other operating revenues	9.3	13.7	47.3%
Total	**1,593.6**	**1,517.8**	**(4.8)%**

Operating revenues from our business decreased by 4.8% to €1,517.8 million in 2009 from €1,593.6 million in 2008, primarily due to the negative impact of regulatory reductions in mobile termination rates (€62.1 million) and lower equipment sales (€15.3 million), which more than offset the 0.4% growth in customer revenues driven by growth in post-paid customers and data revenues. Roaming-out revenues and national traffic revenues also declined due to economic and competitive pressures in voice services.

Other Operations. Operating revenues from our other operations contributed €476.5 million to our consolidated operating revenues in 2009, an increase of 7.5% from €443.2 million in 2008. This increase was primarily due to improved revenue performance in our call center business in Brazil (Dedic), MTC in Namibia and Timor Telecom.

Table of Contents

Costs, Expenses, Losses and Income

As explained in more detail below, our costs increased in 2009 due to, among other factors, increases in depreciation and amortization, wages and salaries, post retirement benefits costs and supplies and external services, which were partially offset by reductions in costs of products sold and curtailment and settlement costs. For more detail on these costs and expenses as they relate to each of our segments, see Note 7 to our audited consolidated financial statements.

Wages and Salaries. Wages and salaries, including employee benefits and social charges, increased by 11.7% to €546.7 million in 2009 from €489.4 million in 2008, reflecting higher wages and salaries at Dedic, primarily due to the expansion of this business.

Direct Costs. Direct costs increased by 0.3% to €522.4 million in 2009 from €520.8 million in 2008, primarily related to the 4.6% increase (€18.2 million) in the wireline business, with the increase in programming costs (€50.0 million) related to the roll-out of our Pay-TV service being partially offset by the impact of the decline in mobile termination rates. The increase at the wireline business more than offset a reduction of TMN's direct costs by 7.1% (€19.8 million), primarily explained by the impact of lower mobile termination rates (€32.3 million) and partially offset by an increase in lease costs.

Costs of Products Sold. Costs of products sold decreased by 15.3% to €207.3 million in 2009 from €244.8 million in 2008, primarily explained by the reduction in TMN (€31.5 million), mainly reflecting lower equipment sales.

Marketing and Publicity. Marketing and publicity costs decreased by 10.5% to €78.6 million in 2009 from €87.9 million in 2008, mainly due to a lower contribution from our Portuguese operations (€10.8 million), primarily explained by higher marketing expenses incurred in 2008 related to the launch of our IPTV service.

Supplies and External Services. Supplies and external services increased by 5.4% to €733.3 million in 2009 from €695.6 million in 2008, primarily explained by a higher contribution from our Portuguese operations (€26.3 million) due to increased commercial activity and higher support service and customer care costs related to demand for our Pay-TV service.

Indirect Taxes. Indirect taxes increased by 25.9% to €57.8 million in 2009 from €45.9 million in 2008, primarily due to an increase at the wireline business (€9.1 million), reflecting higher spectrum fees and other indirect taxes related to the roll-out of our Pay-TV service, which was partially offset by a lower contribution from TMN (€1.4 million), following the reduction in the spectrum fee per customer approved at the end of 2008.

Provisions and Adjustments. Provisions and adjustments increased by 5.3% to €30.5 million in 2009 from €29.0 million in 2008, reflecting a higher contribution from MTC (€1.1 million). Provisions and adjustments in our Portuguese operations, including the wireline business and TMN, remained broadly stable.

Depreciation and Amortization. Depreciation and amortization costs increased by 10.7% to €716.9 million in 2009 from €647.5 million in 2008, reflecting a higher contribution from the wireline business (€68.9 million) as a result of the investments in the rollout of our Pay-TV service and the impact of the revaluation of ducts and certain real estate assets undertaken in 2008 (€42.1 million).

Post Retirement Benefits. We recorded a €89.6 million charge for post retirement benefits in 2009, compared to €44.8 million in 2008. The increase in this caption is primarily explained by a reduction in the expected return on assets (€40.4 million), as a result of the lower return on assets in 2008, leading to a decline in the value of fund assets. This cost item does not include early termination costs related to our workforce reduction program, which are discussed under " *Curtailment and Settlement Costs*" below.

Curtailment and Settlement Costs. Curtailment costs decreased to €14.8 million in 2009, compared to €100.0 million in 2008, due to the halting of our redundancy program in 2009. In 2008, curtailment costs were related to the reduction of 357 employees. See " *Liquidity and Capital Resources Post Retirement Benefits*" for a description of these reductions.

Net Gains on Disposal of Fixed Assets. Net gains on disposal of fixed assets decreased to €2.0 million in 2009, from €18.3 million in 2008. Gains recorded in 2008 were mainly related to the implementation of a new real estate management strategy, which involved disposals of several real estate properties in that period.

Other Costs. Other costs increased to €45.6 million in 2009 from €22.6 million in 2008, primarily reflecting increased costs from the write-off of certain equipment.

Financial Income and Expenses

Net Interest Expenses. Net interest expenses increased by 10.7% to €227.5 million in 2009 from €205.4 million in 2008, primarily as a result of the increase in our average net debt in the period following the completion of our share buyback program in 2008. In 2009, our consolidated average cost of debt remained flat at 4.3% compared to 2008.

Net Foreign Currency Exchange Losses (Gains). We had net foreign currency losses of €0.2 million in 2009, compared to net gains of €3.6 million in 2008. In 2008, this item included primarily foreign currency gains related to the the impact of the appreciation of the U.S. dollar against the Euro on cash applications denominated in U.S. dollars held by Portugal Telecom, mainly resulting from dividends received from Unitel.

Net Gains on Financial Assets and Other Investments. We recorded net gains on financial assets and other investments of €8.1 million in 2009, compared to €12.1 million in 2008. Gains recorded in 2009 primarily related to changes in the fair value of free-standing cross currency derivatives (€5.7 million) as a result of the appreciation of the U.S. dollar against the Euro until April 2009, when these derivatives were settled. In 2008, this item included (1) the gain obtained from the sale of a 3% stake in the share capital of Africatel (€8.8 million) and (2) the impact of changes in the fair value of free-standing cross currency derivatives, which resulted in gains of €3.2 million, primarily related to the appreciation of the U.S. dollar against the Euro.

Equity in Earnings of Affiliated Companies. Equity in earnings of affiliated companies increased to €456.0 million in 2009, compared to €171.0 million in 2008. This caption includes our share in the earnings of Unitel (€152.6 million in 2009 compared to €122.6 million in 2008), CTM (€18.6 million in 2009 and €16.8 million 2008) and UOL (€10.6 million in 2009 and €11.4 million in 2008). In 2009, this caption includes the capital gain related to the sale of the stake in Médi Télécom (€267.0 million), while in 2008 includes a gain resulting from the sale of the 34% stake in Banco Best (€8.8 million).

Net Other Financial Expenses. Net other financial expenses increased to €35.7 million in 2009, compared to €13.7 million in 2008, and include banking services expenses, commissions, financial discounts and other financing costs.

Income Taxes

Income taxes amounted to €185.9 million in 2009, compared to €204.8 million in 2008, corresponding to an effective tax rate of 20.8% in 2009 and 25.0% in 2008.

Table of Contents

Income from Continued Operations (Before Discontinued Operations and Non-Controlling Interests)

Income (before discontinued operations and non-controlling interests) increased by 15.1% to €706.7 million in 2009 from €614.1 million in 2008 for the reasons described above.

Net income from our wireline business decreased by 37.5% to €171.5 million in 2009 from €274.6 million in 2008, primarily due to the increase in post retirement benefits costs, depreciation and amortization costs and supplies and external service expenses. These effects were partially offset by the increase in services rendered and the decrease in curtailment costs.

Net income from our mobile business increased by 1.9% to € 320.7 million in 2009 from €314.8 million in 2008, primarily due to strict cost discipline, which led to reductions in wages and salaries, commercial costs and other expenses, more than offsetting the decrease in services rendered net of the related direct costs.

Income from Discontinued Operations

Income from discontinued operations, which related to Vivo, was €82.5 million in 2009, compared to €81.7 million in 2008. In 2009, this caption includes a gain of €31.9 million related to positive foreign currency adjustments, following share capital reductions undertaken in 2009 by Brasilcel N.V. Excluding this effect, this caption corresponds to the net income from Vivo, which decreased primarily due to increases in financial expenses and income taxes, partially offset by an improvement in operating revenues.

Net Income Attributable to Non-Controlling Interests

Net income attributable to non-controlling interests in 2009 amounted to €104.5 million and was related primarily to Vivo (€42.6 million), MTC (€22.4 million), Africatel (€11.3 million) and Cabo Verde Telecom (€17.4 million). In 2008, net income attributable to non-controlling interests amounted to €119.7 million and was related primarily to Vivo (€51.9 million), Africatel (€24.1 million), MTC (€ 19.2 million) and Cabo Verde Telecom (€16.5 million).

Net Income Attributable to Equity Holders of the Parent

For the reasons described above, our net income attributable to equity holders of Portugal Telecom increased by 18.9% to €684.7 million in 2009 from €576.1 million in 2008.

Basic earnings per ordinary and A shares from total operations in 2009 increased to €0.78 in 2009 from €0.64 in 2008 on the basis of 896,512,500 shares issued at December 31, 2009 and 2008.

Liquidity and Capital Resources

Overview

Our principal capital requirements relate to:

- funding our operations;
- capital expenditures on our network infrastructure, information systems and other investments, as well as acquisitions of interests in other telecommunications companies (see "*Capital Investment and Research and Development*" and "*Contractual Obligations and Off-Balance Sheet Arrangements*" below);
- repayments and refinancing of our indebtedness (see "Indebtedness" below);
- shareholder remuneration in the form of dividend payments; and

funding of post retirement benefits (see " *Post Retirement Benefits*" below).

Table of Contents

Our principal sources of funding for these capital requirements are cash generated from our operations and equity and debt financing. Our cash and cash equivalents and short-term investments increased to €5,106.5 million as of December 31, 2010, compared to €1,476.4 million as of December 31, 2009. We believe that our cash balances, together with the cash that we expect to generate from our operations and available liquidity under our credit facilities and lines of credit, are currently sufficient to meet our present funding needs.

In September 2010, we concluded the sale of our 50% investment in Brasilcel N.V. to Telefónica for a consideration of €7.5 billion. As of December 2010, we have received from Telefónica €5.5 billion, and the remaining €2 billion will be received in October 2011. In December 2010 we paid to our shareholders an extraordinary and anticipated dividend of €1 per share, totaling €876 million. Our cash balance and accounts receivable as of December 31, 2011 were materially impacted by this non-recurring transaction.

In December 2010, we reached an agreement with the Portuguese Government for the transfer of certain regulated pension obligations and related funds and agreed to pay the unfunded obligation amounting to €1,022 million up to December 2012. We paid €100 million in December 2010, and we will pay €468 million in 2011 and €454 million in 2012. See " *Post Retirement Benefits*."

On March 28, 2011, we completed the acquisition of an economic stake of 25.3% in Oi and 42.0% in CTX, respectively, for a total consideration of R$8.4 billion (€3.7 billion). In addition, we proposed to the 2011 Annual General Meeting of Shareholders the payment of an extraordinary dividend of €0.65 per share, totaling €583 million, in excess of the ordinary €0.65 per share dividend.

In 2011, our use of funds will be impacted significantly by these non-recurring transactions.

Cash Flows

The table below sets forth a breakdown of our cash flows from continuing operations for the years ended December 31, 2008, 2009 and 2010. For a discussion of cash flow that includes discontinued operations, see Notes 20 and 35 to our audited consolidated financial statements.

	2008	**2009**	**2010**
		(EUR Millions)	
Cash flow from operating activities	1,828.9	1,927.5	1,506.9
Continuing operations	1,190.6	1,081.2	903.8
Discontinued operations	638.2	846.2	603.0
Cash flow from (used in) investing activities	(108.7)	(597.8)	4,072.4
Continuing operations	603.6	(296.8)	(1,301.2)
Discontinued operations	(712.3)	(301.0)	5,373.6
Cash flow from (used in) financing activities	(1,283.8)	(997.3)	(1,929.1)
Continuing operations	(1,350.1)	(319.2)	(1,571.2)
Discontinued operations	66.3	(678.2)	(357.9)
Total	**436.3**	**332.3**	**3,650.2**

Cash Flow from Operating Activities

Cash flows from operating activities include collections from clients, payments to suppliers, payments to personnel, payments relating to income and indirect taxes and payments related to post retirement benefits activities. Our cash flows from operating activities result primarily from operations conducted by our subsidiaries and not by Portugal Telecom. None of our subsidiaries is subject to economic or legal restrictions on transferring funds to us in the form of cash dividends, loans or advances that would materially affect our ability to meet our cash obligations.

Table of Contents

Net cash flow from operating activities related to continuing operations decreased by 16.4% to €903.8 million in 2010 from €1,081.2 million in 2009. This decrease was primarily due to a €202.5 million reduction in collections from customers and an increase of €88.3 million in payments to employees, mainly related to our contact center operation in Brazil. These effects were partially offset mainly by a decrease of €74.1 million in payments relating to income taxes, primarily in our Portuguese operations, following the reduction in our taxable earnings.

Net cash flow from operating activities related to continuing operations decreased by 9.2% to €1,081.2 million in 2009 from €1,190.6 million in 2008. This decrease was primarily due to a €138.4 million decrease in collections from customers, a €121.2 million increase in payments to suppliers and a €54.4 million increase in payments relating to post-retirement benefits, primarily due to a required extraordinary cash contribution to our pension funds due to their underperformance in 2008. These effects were partially offset by a €150.9 million decrease in payments relating to indirect taxes, primarily due to a reduction in payments of value-added tax (VAT) in Portugal, and by a €93.4 million decrease in payments relating to income taxes.

Cash Flow from (Used in) Investing Activities

Cash flows from investing activities include proceeds from disposals of investments in associated companies and property, plant and equipment, as well as interest and related income on investments. Cash flows used in investing activities primarily include investments in short-term financial applications, capital expenditures for telecommunications equipment and investments in other companies.

Net cash used in investing activities related to continuing operations amounted to €1,301.2 million in 2010, compared to €296.8 million in 2009. The change in this caption was primarily due to (1) an increase of €333.4 million in net cash payments from short-term financial applications, following the disposal of the 50% stake in Vivo, (2) a €397.5 million decrease in cash receipts from disposals of investments, primarily related to the disposal of Médi Télécom in 2009 (which had a €400.0 million effect in that year) and (3) a €269.3 million increase in cash payments for the acquisition of tangible and intangible assets.

Net cash used in investing activities related to continuing operations amounted to €296.8 million in 2009, compared to net cash receipts of €603.6 million in 2008. The change in this caption was primarily due to (1) a decrease in net cash receipts from short-term financial applications (€1,117.8 million) because as the maturity of most of these applications was reached in 2008, they were converted into cash and cash equivalents, which also explains the lower levels of cash receipts and payments in 2008 related to short-term financial applications, and (2) a €225.0 million increase in cash payments for the acquisition of tangible and intangible assets. These effects were partially offset by: (1) a €369.6 million increase in cash receipts from disposals of investments, primarily related to the disposal of Médi Télécom in 2009 (€400.0 million) and (2) a €121.0 million increase in dividends received from associated companies, primarily related to Unitel.

Cash Flows from (Used In) Financing Activities

Cash flows used in financing activities related to continuing operations include repayments of debt, payments of interest on debt and payments of dividends to shareholders. Cash flows from financing activities primarily consist of borrowings. Net cash used in financing activities increased to €1,571.2 million in 2010, compared to €319.2 million in 2009, mainly due to an increase in dividends paid (€916.5 million), primarily explained by the dividends constituting an advance on 2010 profits (€875.9 million) and a decrease in net cash receipts from loans obtained (€302.4 million).

Cash receipts from loans obtained, net of cash payments from loans repaid, primarily relate to commercial paper and other bank loans and amounted to €199.3 million in 2010. As described in more detail in Note 35 to our audited consolidated financial statements, net cash receipts from loans obtained in 2010 primarily included two loans obtained from the EIB totalling €200.0 million. In 2009, cash receipts from loans obtained, net of cash payments from loans repaid amounted to €501.7 million. As described in more detail in Note 35 to our audited consolidated financial statements, cash receipts from loans obtained in 2009 include (1) Eurobonds issued by PT Finance totaling €2,050.0 million and (2) floating rate notes issued by PT Finance in July 2009 amounting to €250.0 million. Cash payments from loans repaid in 2009 included the repayments of (1) the Eurobonds issued by PT Finance in 1999 (€880.0 million), (2) the commercial paper outstanding as at December 31, 2008 (€648.6 million) and (3) the floating rate notes issued by PT Finance in December 2008 (€200.0 million). In 2008, cash receipts from loans obtained, net of cash payments from loans repaid, amounted to €514.0 million and primarily included (1) €200 million and €50 million related to the floating rate notes issued by PT Finance during 2008 and (2) €324.9 million related to the increase in the commercial paper outstanding at year end.

In 2010, 2009 and 2008, dividends paid amounted to €1,452.0 million, €535.5 million and €565.9 million, respectively. In 2010, dividends paid included an amount of €875.9 million related to an advance of 2010 profits.

In 2010 and 2009 we did not acquire treasury shares, while in 2008 we acquired 129,287,500 treasury shares for €1,049.7 million.

Indebtedness and cash and cash equivalents

Our total consolidated indebtedness increased by 2.3% to €7,206.3 million at the end of 2010, compared to €7,046.0 million as at December 31, 2009, reflecting (1) the issuances and repayments of loans obtained described above under " *Cash Flows Cash Flows from (Used In) Financing Activities*," (2) the deconsolidation of Vivo's indebtedness, following the disposal of this investment in September 2010 and (3) the financing relating to the transfer of unfunded pension obligations completed in December 2010, as explained below. Our cash and cash equivalents increased to €4,764.7 million as of December 31, 2010 from €1,449.5 million as of December 31, 2009, primarily explained by the cash receipts from Telefónica in 2010 related to the Vivo transaction. Our short-term investments increased to €341.8 million as of December 31, 2010 from €26.9 million as of December 31, 2009.

Of the total indebtedness outstanding as of December 31, 2010, 86.8% was medium and long-term debt compared to 93.0% as of December 31, 2009.

Table of Contents

The composition of our consolidated indebtedness as of December 31, 2008, 2009 and 2010 was as follows:

	As of December 31,					
	2008		2009		2010	
Debt	**Euro millions**	**% of total indebtedness**	**Euro millions**	**% of total indebtedness**	**Euro millions**	**% of total indebtedness**
Short-term:						
Bond loans	879.3	13.1	41.8	0.6		0.0
Bank loans	497.8	7.4	244.3	3.5	177.9	2.5
Other loans	648.6	9.7	0.0	0.0	568.5	7.9
Commitments under TMN's UMTS license(1)	25.5	0.4		0.0		0.0
Liability for equity swaps on own shares	178.1	2.7	178.1	2.5	178.1	2.5
Financial leases	25.5	0.4	30.3	0.4	27.5	0.4
Total short-term	**2,254.7**	**33.7**	**494.5**	**7.0**	**951.9**	**13.2**
Medium- and long-term:						
Exchangeable bond loans	697.3	10.4	705.6	10.0	714.2	9.9
Other bond loans	2,404.8	35.9	4,734.5	67.2	4,375.7	60.7
Bank loans	1,021.2	15.3	1,027.5	14.6	662.4	9.2
Commitments under TMN's UMTS license(1)	54.0	0.8	0.0	0.0	0.0	0.0
Other loans	159.2	2.4	0.0	0.0	454.3	6.3
Financial leases	104.7	1.6	84.0	1.2	47.7	0.7
Total medium- and long-term	**4,441.2**	**66.3**	**6,551.5**	**93.0**	**6,254.4**	**86.8**
Total indebtedness	**6,695.9**	**100.0**	**7,046.0**	**100.0**	**7,206.3**	**100.0**
Cash and cash equivalents	1,010.7	15.1	1,449.5	20.6	4,764.7	66.1
Short-term investments	52.9	0.8	26.9	0.4	341.8	4.7
Net Indebtedness	**5,632.3**	**84.1**	**5,569.7**	**79.0**	**2,099.8**	**29.1**

(1) For a description of TMN's commitments under its UMTS license, see "*Item 4 Information on the Company Our Businesses Personal Services (Mobile Business) TMN's Commitment to the Portuguese Information Society.*"

Maturity

Of the total indebtedness outstanding as at December 31, 2010, €951.9 million is due before the end of December 2011. The remaining € 6,254.4 million is medium and long-term debt. As of December 31, 2010, the average maturity of our total indebtedness, net of cash and cash equivalents and short-term investments, is 9.9 years.

Interest Rates

As at December 31, 2010, 91.0% of our total indebtedness was at fixed rates, primarily as a result of the fixed-rate bonds issued in 2005, 2007, and 2009.

Table of Contents

Credit Ratings

Our credit ratings are currently as follows:

Rating Agency	Credit Rating	Outlook	Last Change
Moody's	Baa2	Under review for possible downgrade	April 7, 2011
Standard & Poor's	BBB	Credit watch Negative	March 30, 2011
Fitch Ratings	BBB	Negative	April 5, 2011

We have several loans from the European Investment Bank (EIB) totaling €183 million as of December 31, 2010 that contained a provision under which the EIB had the right to require us to provide a guarantee acceptable to EIB in the event our ratings are downgraded from BBB- by S&P, Baa2 by Moody's and BBB by Fitch. In that circumstance, and after notice from the EIB, we would have 60 days to present an acceptable guarantee. If we failed to provide the EIB the required guarantee, the EIB would have the right to accelerate the repayment of the loans.

Debt Instruments and Repayment and Refinancing of Indebtedness

Set forth below is a brief description of certain of our debt instruments. See Note 35 to our audited consolidated financial statements for more information.

Euro Medium Term Note Program. We have established a euro medium term note program providing for the issuance of bonds. The program allows for the bonds to be issued in a range of currencies and forms, including fixed and floating rates, zero coupon and index-linked. As of December 31, 2010, the size of the euro medium term note program was €7.5 billion. Of that amount, we have issued the following bonds which were outstanding as of December 31, 2010:

On March 24, 2005, we issued €1 billion in bonds at a fixed interest rate of 3.75% per annum, maturing in 2012. On February 5, 2009, we issued an additional €300 million in bonds with the same terms, with an annual reoffer yield of 7.27%. Thus, the total outstanding amount of these 3.75% bonds maturing in 2012 is €1.3 billion.

Also on March 24, 2005, we issued €500 million in bonds at a fixed interest rate of 4.375% per annum, maturing in 2017.

On June 16, 2005, we issued €500 million in bonds at a fixed interest rate of 4.5% per annum, maturing in 2025.

On August 7, 2008, we issued €50 million in floating rate notes, bearing interest at the three-month European Interbank Offered Rate ("Euribor") plus 1.50%, and maturing in 2013.

On January 30, 2009, we issued €50 million in floating rate notes, maturing in 2019 with an investor put that may be exercised on January 30, 2012. These notes bear interest at a fixed interest rate of 6.95% during the initial 3 years and at an interest rate based on the seven-year Euro swap rate for January 30, 2012, plus 4.42% for the remaining seven years.

On April 30, 2009, we issued €1 billion in bonds at a fixed rate of 6.0% per annum, maturing in 2013.

On July 30, 2009, we issued €250 million in floating rate notes, bearing interest at a fixed rate of 5.242% per annum and maturing in 2017.

104

On November 2, 2009, we issued €750 million in bonds at a fixed rate of 5.0% per annum, maturing in 2019.

Exchangeable Bonds. On August 28, 2007, we issued €750 million in bonds due 2014, exchangeable into fully paid ordinary shares of Portugal Telecom. The exchangeable bonds carry a coupon of 4.125% per annum and the exchange price is currently €11.06, in accordance with the terms and conditions of the bonds.

Revolving Credit Facilities:

In 2004, we entered into three bilateral revolving credit facilities: one in June 2004 amounting to €150 million and with a maturity of four years, which in 2007 was changed to an amount of €300 million and a maturity of eight years; the second in October 2004 amounting to €100 million and an initial maturity of three years that was changed to seven years in 2008; and a third also in October 2004 amounting to €150 million and with a maturity of three years and six months, which was replaced by another facility with the same amount and conditions in 2008, but maturing in April 2011.

In July 2008, we entered into a revolving credit facility in the amount of €50 million with a maturity of three years. In October 2008, we entered into an additional revolving credit facility in the amount of €365 million, of which €300 million matures in three years and the remaining €65 million matures in five years.

In January 2009, we entered into a revolving credit facility, amounting to €50 million, with a maturity of two years. In 2011, the maturity of this credit facility was extended to four years.

As of December 31, 2010, the aggregate commitments under these bilateral revolving credit facilities was €1,015 million, and we had borrowed a total of €200 million of that amount. All these facilities bear interest at a rate based on the Euribor rate plus a spread.

EIB Loans. We had several amortizing loans from the EIB in the aggregate amount of €565 million as of December 31, 2010. These include (1) loans in the aggregate amount of €211.4 million, bearing an average fixed interest rate of 3.6% per annum and maturing on various dates from 2011 to 2018, (2) loans in the aggregate amount of €190.0 million, bearing fixed interest rates revisable on pre-agreed dates, with an average rate of 3.5% per annum as of December 31, 2010, and maturing on various dates from 2011 to 2021, (3) loans in the aggregate amount of €155.8 million whose floating interest rates have been swapped for fixed rate obligations at an average interest rate of 2.5% and maturing on various dates from 2011 to 2014 and (4) loans in the aggregate amount of US$10.6 million (equivalent to €8.0 million using the Euro/U.S. dollar exchange rate at year-end), maturing in 2011, whose U.S. dollar principal and floating U.S. dollar interest rate have been swapped for Euro principal and floating Euro interest rate obligation at an effective spread of 0.42% over the Euribor rate, generating exchange losses of €2.0 million as of December 31, 2010 (also part of our indebtedness). See "*Item 11 Quantitative and Qualitative Disclosures About Market Risk*" for more information.

Commercial Paper. As of December 31, 2010, we had in place domestic commercial paper programs totaling €550 million, of which an amount of €450 million is underwritten. As of December 31, 2010, we had issued an amount of €88 million under the non-underwritten portion, which matured in January 2011.

Financing Relating to the Transfer of Unfunded Pension Obligations. Following the transfer of certain unfunded pension obligations to the Portuguese Government for a total amount of €1,021.7 million, we paid €100.0 million in December 2010. Of the remaining €921.7 million, €17.4 million was paid in January 2011, €450.0 million must be paid no later than December 20,

Table of Contents

2011 and bears interest at annual rate of 2.74%, and €454.3 million must be paid no later than December 20, 2012 and bears interest at annual rate of 3.25%.

In addition, since December 31, 2010, we have entered the following material financing arrangements:

February 2011 Bonds. On February 8, 2011, we issued €600 million in bonds at a fixed rate of 5.625%, maturing in 2016.

New Revolving Credit Facility. On March 25, 2011, we announced that we had entered into a new €900 million revolving credit facility maturing in 2014. The facility was increased to €1,050 million on April 12, 2011 and to €1,200 million on April 13, 2011.

Covenants

Our debt instruments contain certain covenants, as well as customary default and cross-acceleration provisions. As of December 31, 2010, the main covenants are as follows:

Change in Control. The exchangeable bonds, the credit facilities amounting to €1,015 million, the loans obtained from EIB totalling €565 million as at December 31, 2010 and the loan obtained in 2010 amounting to €50 million grant the lenders the right to demand the repayment of all amounts due in the case of any change in control of Portugal Telecom. According to the terms and conditions of these debt instruments, a change of control would occur if any person or group of persons acting in concert acquires or controls more than 50% of voting rights, whether obtained by ownership of share capital, the holding of voting rights or pursuant to the terms of a shareholders' agreement. In certain cases, gaining the power to appoint or remove all, or the majority, of the directors or other equivalent officers of the company or to give directions with respect to the operating and financial policies of the company with which the directors or equivalent officers of the company are obliged to comply are also considered a change of control.

The Eurobonds amounting to €1,000 million and €750 million issued in 2009 grant the bondholders the right to demand the repayment of all amounts due in the case of any change in the control of Portugal Telecom, as described above, if simultaneously a rating downgrade to sub-investment grade occurs during the Change of Control Period, as defined under the terms and conditions of these notes. This is also applicable to the Eurobond issued in February 2011.

Credit Rating. Certain loan agreements with the EIB totalling €183 million as at December 31, 2010 state that we may be asked to present a guarantee acceptable by the EIB if, at any time, the long-term credit rating assigned by the rating agencies to Portugal Telecom is reduced from the rating assigned by the time the clause was included (BBB- by S&P, Baa2 by Moody's and BBB by Fitch). Current credit ratings are BBB by S&P, Baa2 by Moody's and BBB by Fitch. In addition, the pricing conditions applicable to the commercial paper programs may be revised in case the credit rating assigned to Portugal Telecom is changed. See " *Credit Ratings*" above.

Control and Limitations on Disposals of Subsidiaries. As of December 31, 2010, certain credit facilities and commercial paper programs in the aggregate amount of €615 million state that we must, directly or indirectly, maintain majority ownership and control of each material subsidiary. Material subsidiaries are those companies whose total assets are equal to or exceed 10% of total consolidated assets or whose total revenues are also equal or exceed 10% of total consolidated revenues.

Disposals of Assets. Credit facilities totalling €150 million and EIB loans totalling €565 million as at December 31, 2010 include certain restrictions regarding the disposal of assets by Portugal Telecom.

Table of Contents

Financial Ratios. As of December 31, 2010, certain credit facilities, loans and commercial paper programs totalling €815 million require that the ratio Consolidated Net Debt/EBITDA should not be higher than 3.5. Other credit facilities totalling €200 million require that the ratio Consolidated Net Debt/EBITDA should not be higher than 4.0. In addition, the pricing conditions applicable to certain facilities and commercial paper programs in the total amount of €1,115 million may be changed depending on the ratio Consolidated Net Debt/EBITDA. Finally, certain loan agreements with the EIB, totalling €49 million as at December 31, 2010, state that we may be asked to present a guarantee acceptable by the EIB if the ratio Consolidated Net Debt/EBITDA, as defined in the agreements, is higher than 3.5.

Negative Pledge. The Euro Medium Term Note Program, the exchangeable bonds, the revolving credit facilities, the loan obtained in 2010 amounting to €50 million and one of our commercial paper programs are subject to negative pledge clauses, which restrict the pledge of security interests in the assets of companies included in the consolidation.

Regarding the disposal of the 50% stake in Brasilcel N.V., the joint venture that held our interest in Vivo, we obtained a waiver from a financial institution stating that it did not object to the disposal of this investment.

The penalties applicable in the event of default in any of these covenants are generally the early payment of the loans obtained or the termination of available credit facilities. We believe we are in full compliance with the covenants described above.

We discuss our exposure to interest rate and exchange rate risk, as well as our use of derivative instruments, in "*Item 11 Quantitative and Qualitative Disclosures About Market Risk.*"

Post Retirement Benefits

On December 2, 2010, we reached an agreement with the Portuguese Government for the transfer to Caixa Geral de Aposentações, the Portuguese institution responsible for managing post retirement benefits for civil servants, of the pension liabilities that were guaranteed by PT Comunicações relating to a portion of its active and former employees, as well as the pension fund assets associated with those liabilities. The transfer included the *Plano de Pensões do Pessoal da Portugal Telecom/CGA,* the *Plano de Pensões Regulamentares da Companhia Portuguesa Rádio Marconi* and the liabilities associated with the survival benefit in the *Plano de Pensões Marconi* (collectively, the "Regulated Pension Plans").

The present value of the liabilities associated with the Regulated Pension Plans, as of the date of transfer, was €2,803.8 million, as determined by an independent actuary. The market value of the pension fund assets transferred, as of the date of the transfer, was €1,782.1 million. Accordingly, the unfunded transferred liabilities amounted to €1,021.7 million, of which we paid €100 million in December 2010 and €17.4 million in January 2011. We will pay an additional €450 million in December 2011 and the final €454 million in December 2012.

Following the transfer of the pension plans to the Portuguese Government, we are now responsible for a fixed monthly contribution (23.75% of compensation paid to active beneficiaries) to Social Security and the Caixa Geral de Aposentações in order to fund future benefits for the active beneficiaries included in these plans.

Table of Contents

The following table shows the amount of our liabilities for post retirement benefits recorded on our statements of financial position at December 31, 2008, 2009 and 2010:

	As of December 31,		
	2008	**2009**	**2010**
		(EUR Millions)	
Gross projected pension benefit obligations	2,607.5	2,710.2	129.9
Minus: Pension fund assets at fair value	(1,738.3)	(1,954.8)	(109.3)
Prior years' service gains(1)	10.6	9.4	5.2
Accrued pension liabilities	**879.8**	**764.9**	**25.8**
Gross projected healthcare benefit obligations	426.3	335.3	342.5
Minus: Healthcare fund assets at fair value	(393.4)	(414.8)	(338.8)
Prior years' service gains(1)	14.8	14.0	13.1
Accrued healthcare liabilities/(surplus)	**47.7**	**(65.5)**	**16.8**
Obligations with salaries to suspended and pre-retired employees	907.7	791.4	924.3
Total accrued liability for post retirement benefits(2)	**1,835.3**	**1,490.8**	**966.9**

(1) These prior years' service gains resulted from the effect on unvested pension and healthcare benefits of changes in the plans governing those benefits. These amounts will be recognized in earnings during the estimated period in which those benefits will be earned by employees (9 years for pension benefits and 16 years for healthcare benefits).

(2) As of December 31, 2010, this caption corresponds to the net amount of an accrued post retirement liability of €968.8 million related to pension benefits and a non-current asset of €1.9 million related to the surplus of certain pension plans.

We no longer sponsor any defined benefit plan relating to pensions, but we remain responsible for defined post retirement plans with respect to pension supplement and healthcare benefits. As of December 31, 2010, the projected benefit obligations, or "PBO," of our post retirement benefits, including pension supplements, healthcare benefits and salaries for pre-retired and suspended employees, amounted to €1,396.7 million (€129.9 million for pension supplements, €342.5 million for healthcare benefits and €924.3 million for salaries to pre-retired and suspended employees). The projected benefit obligations were computed based on a 4.75% discount rate for pension and healthcare benefits and 3.75% for obligations related to the payment of salaries to pre-retired and suspended employees and assuming a 1.75% annual salary increase. As of December 31, 2010, our post retirement benefit plans, which are closed to new participants, covered approximately 19,897 employees (around 35% still in service) in the case of pensions and approximately 24,857 employees (around 25% still in service) in the case of healthcare obligations.

According to the rules of the *Instituto de Seguros de Portugal* (ISP), the Portuguese insurance regulator, the liability related to retired employees under the pension plans have to be fully funded. Funding of pension funds for pre-retired employees and employees still in service can be completed up to the retirement age under current rules. The estimated average working life of employees still in service is 14 years. As of December 31, 2010, our pension obligations for retired employees, computed based on ISP rules, are fully funded.

In Portugal, there is no legislation covering the establishment of funds to cover the healthcare obligations and the salaries for pre-retired and suspended employees or healthcare expenses are incurred. We are required to pay for these benefits only when the salaries are paid to pre-retired and suspended employees, or when healthcare expenses are incurred. Accordingly, there is no requirement to fund these benefit obligations at present. However, we have set up a fund managed by our subsidiary

Table of Contents

PT Prestações Mandatária de Aquisições e Gestão de Bens, S.A., or PT Prestações, to finance our healthcare post-retirement liabilities. In previous years, we contributed €602 million to this fund, which is being managed in accordance with the same guidelines as its pension funds. In 2008, 2009 and 2010, we did not make additional contributions to this fund.

The market value of the pension funds amounted to €448.1 million at December 31, 2010, a decrease of €1,921.4 million from 2009, primarily explained by the value of the pension fund assets transferred to the Portuguese Government (€1,782.1 million), payments of pensions and supplements of €152.4 million and the reimbursement to us of excess funding of a healthcare plan in the amount of €75.0 million. These effects were partially offset by the positive performance of assets under management amounting to €52.8 million and our contributions to the pension funds in the amount of €35.5 million. See Notes 14.1, 14.2 and 14.3 to our audited consolidated financial statements. The asset allocation of our pension and healthcare benefit funds as of December 31, 2010 was 25.2% equity, 35.7% bonds, 2.4% real estate and 36.7% cash and others. The effective return of the funds in 2010 was positive by approximately 2.8%.

The accrued liability related to our post-retirement benefits amounted to €966.9 million (including €18.3 million of prior year service gains not recognized in results). In 2010, the accrued liabilities decreased by €523.9 million, primarily because of the transfer of pension liabilities to the Portuguese Government, as described above. The table below shows the evolution of our net responsibilities for post retirement benefits during 2009 and 2010.

	2009	2010
	(EUR Millions)	
Accrued liability for post retirement benefits (initial balance)	**1,835.3**	**1,490.8**
Post retirement benefit expenses	89.6	36.8
Workforce program reduction costs	12.1	141.6
Contributions and payments	(281.5)	(131.2)
Net actuarial losses/(gains)	(164.8)	450.7
Unfunded obligations transferred to the Portuguese Government		(1,021.7)
Accrued liability for post retirement benefits (final balance)	**1,490.8**	**966.9**

The table below sets forth the components of our net post retirement benefit expense in 2008, 2009 and 2010.

	Year Ended December 31,		
	2008	2009	2010
	(EUR Millions)		
Service cost	10.0	6.8	7.2
Interest cost	208.7	216.4	192.0
Expected return on assets	(172.0)	(131.6)	(129.2)
Prior years service gains(1)			(31.2)
Subtotal	**46.8**	**91.6**	**38.7**
Amortization of prior year service gains(2)	(2.0)	(2.0)	(1.9)
Contribution to Social Security(3)			1.4
Post retirement benefit expense	**44.8**	**89.6**	**38.2**

(1) The prior year service gain recognized in 2010 is related to Portuguese Law 3B/2010, which introduced a maximum amount for pension benefits.

(2)
In 2010, 2009 and 2008, this caption is related to the amortization of prior years service gains on unvested pension benefits.

(3)
This caption corresponds to our fixed monthly contribution (23.75% of remuneration) to Social Security and Caixa Geral de Aposentações in order to fund future service of the active beneficiaries included in certain pension plans, following their transfer to the Portuguese Government.

In 2010, net curtailment and settlement costs increased to €145.5 million, as compared to €14.8 million in 2009, reflecting the reengineering of our processes and reorganization of our company along customer segments. In 2009, net curtailment costs decreased to €14.8 million, as compared to €100.0 million in 2008, due to the decision to halt our redundancy program and focus efforts on insourcing certain core functions. In 2008, net curtailment costs amounting to €100.0 million reflected the reduction of 357 employees.

The table below sets forth the components of our cash flows associated with post retirement benefits in 2008, 2009 and 2010.

	Year Ended December 31,		
	2008	**2009**	**2010**
	(EUR Millions)		
Contributions to the pension funds(1)	61.2	75.7	35.5
Payments of pensions to pre-retired and suspended employees	2.4	1.6	0.8
Salary payments (pre-retired and suspended employees)	185.5	174.4	160.3
Regular healthcare payments	23.6	23.0	18.9
Refund(2)	(81.2)	(26.2)	(84.3)
Subtotal	**191.4**	**248.5**	**131.2**
Termination payments	5.4	2.7	4.0
Payment to the Portuguese Government related to the transfer of pension plans			100.0
Payments related to post retirement benefits	**196.8**	**251.2**	**235.2**

(1)
In addition to these cash contributions, during 2008 and 2009, we made contributions in kind (real estate assets) to the pension funds amounting to €37.3 million and €33.0 million, respectively.

(2)
In 2008 and 2010, this caption included €60.0 million and €75.0 million related to the refund of excess financing, respectively.

Our actuarial assumptions are subject to change, including the increase or decrease in the discount rates we use. In determining the appropriate discount rates, we analyze, among other things, the yields of certain investment grade corporate bonds by issuers in the Eurozone with maturities comparable to those of our liabilities. We believe our actuarial assumptions are consistent with those of a number of leading Portuguese companies. Note 14 to our consolidated financial statements contain sensitivity analyses that demonstrate the impact of increases or decreases in our discount rate assumption, our health care cost trend assumption and our assumption about the long-term rate of return on fund assets. Net actuarial losses in 2010 amounted to €450.7 million, as compared to net gains of €164.8 million in 2009.

Net actuarial losses amounting to €450.7 million in 2010 included (1) a loss of €441.8 million resulting from changes in actuarial assumptions, reflecting primarily the reduction in the discount rate from 5.50% to 4.75% for pension and healthcare obligations and to 3.75% for salaries to pre-retired and suspended employees (€352.1 million) and an adjustment in the mortality tables (€100.0 million), and (2) a loss of €8.9 million resulting from differences between actual data and actuarial assumption, including a loss of €76.4 million related to the difference between actual (2.8%) and expected (6.0%)

return on assets and a gain of €67.5 million related to the difference between actual data and actuarial assumptions related to projected benefit obligations, namely lower health care expenses and differences in the salary growth rate.

Net actuarial gains amounting to €164.8 million in 2009 included (1) a gain of €1.7 million resulting from changes in actuarial assumptions, reflecting the impact of the reductions in the discount rate from 5.75% to 5.50% (loss of €98.8 million), changes in the disability table (gain of €39.8 million) and in the percentage of active employees with spouses as additional beneficiaries under the plan (gain of €68.8 million), and (2) a gain of €163.1 million resulting from differences between actual data and actuarial assumption, mainly related to the difference between actual (15.0%) and expected (6.0%) return on assets (gain of €178.6 million).

Equity

Our total equity excluding non-controlling interests amounted to €4,392.4 million as of December 31, 2010, €1,318.3 million as of December 31, 2009 and €232.0 million as of December 31, 2008.

The increase in total equity excluding non-controlling interests in 2010 was primarily related to (1) our net income for the period, amounting to €5,672.2 million and (2) positive currency translation adjustments amounting to €292.4 million primarily explained by the appreciation of the Brazilian Real against the Euro during the period. These effects more than offset (1) the dividends we paid to our shareholders, including ordinary and extraordinary dividends, totaling €1,379.5 million, (2) the accumulated currency translation adjustments relating to our former investment in Brasilcel (Vivo) that were transferred to net income upon our disposal of this investment, which amounted to €1,134.2 million as of the disposal date and (3) the net actuarial losses related to post retirement pension benefits in the amount of €338.0 million, net of taxes.

The increase in total equity excluding non-controlling interests in 2009 was primarily related to (1) the net income for the period amounting to €684.7 million, (2) the positive currency translation adjustments amounting to €673.0 million, mainly related to the appreciation of the Euro/Real exchange rate, which decreased to 2.5113 Reais per Euro at the end of December 2009 from 3.2436 Reais per Euro at the end of December 2008, and (3) the net actuarial gains related to post retirement benefits amounting to €121.1 million (net of taxes). These effects were partially offset by dividends paid to our shareholders amounting to €503.6 million.

Our total equity excluding non-controlling interests as a percentage of total assets increased from 8.9% at the end of 2009 to 29.0% at the end of 2010. Our gearing ratio, calculated as the ratio of net debt to total equity plus net debt, decreased from 70.0% as of December 31, 2009 to 31.3% as of the end of 2010, primarily as a result of the gain obtained with the sale of the 50% stake in Brasilcel N.V.

Table of Contents

Contractual Obligations and Off-Balance Sheet Arrangements

Contractual Obligations and Commercial Commitments

The following table presents our contractual obligations and commercial commitments as of December 31, 2010:

	Payments due by period in millions of Euros				
	Total	Less than 1 year	1-3 years	4-5 years	More than 5 years
Contractual obligations:					
Indebtedness	**7,206.3**	951.9	3,165.7	846.8	2,241.8
Interest on indebtedness(1)	**1,496.9**	279.3	492.6	246.5	478.5
Unfunded post retirement benefits(2)	**1,210.9**	179.0	312.7	256.8	462.3
Operating lease obligations	**210.5**	55.3	56.1	42.1	57.0
Unconditional purchase obligations(3)	**140.4**	139.3	1.1		
Total contractual cash obligations	**10,265.0**	**1,604.9**	**4,028.3**	**1,392.2**	**3,239.6**

(1) Interest on indebtedness is based on our indebtedness as of December 31, 2010 and our assumptions regarding interest rates on our floating rate debt. Our actual interest obligations could vary significantly from these amounts depending on future financing activities and market interest rates.

(2) These amounts correspond to the undiscounted payments to be made by our company for salaries due to pre-retired and suspended employees and to expected contributions to our pension funds, described above in " *Post Retirement Benefits*." The total amount differs from the net accrued post retirement liability recognized on our consolidated statement of financial position, primarily because the amount in this table reflects the discounted unfunded obligations.

(3) Unconditional purchase obligations are related primarily to contractual agreements with our fixed asset suppliers mainly related to network assets, telecommunications equipment and terminal equipment.

Our operating leases relate to the contractual rental agreements entered into by our businesses and include obligations related to leased lines and the rental of buildings. Operating leases are accounted for as a cost in the period that the corresponding expense is incurred. Our intention is to fulfill these commitments from our operating cash flow generated in each of those years.

In addition, on March 28, 2011, we completed the acquisition of an economic stake of 25.3% in Oi and 42.0% in CTX, respectively for a total consideration of R$8.4 billion (€3.7 billion), which was paid on March 30, 2011.

Table of Contents

Off-Balance Sheet Arrangements

In the course of our business, we provide certain guarantees to third parties. These guarantees are given to ensure the proper performance of contractual obligations by Portugal Telecom or its consolidated subsidiaries in the normal course of their business. As of December 31, 2010, we had provided the following guarantees to third parties:

	Guarantees by period in millions of Euros				
	Total	**Less than 1 year**	**1-3 years**	**3-5 years**	**More than 5 years**
Bank guarantees and other guarantees given to Tax Authorities	**267.8**	267.8			
Bank guarantees given to Portuguese courts for outstanding litigation	**2.0**	2.0			
Bank guarantees given to other entities:					
By TMN to ANACOM	**2.1**	2.1			
By PT Comunícações	**12.9**	12.9			
Other bank guarantees	**14.2**	14.2			
Comfort letters and other bank guarantees	**0.4**	0.4			
	299.4	299.4			

Bank guarantees and other guarantees given to tax authorities include €203 million related to tax assessments received by Portugal Telecom regarding the years 2005 to 2007, where the main issue raised by the tax authorities relates to the deductibility of certain financial costs incurred in those years and of a capital loss recorded in 2006 following the liquidation of a subsidiary, as explained in Note 46.3 to our consolidated financial statements.

Bank guarantees given on behalf of PT Comunicações are typically given primarily to the following entities (1) municipal authorities, primarily relating to the payment of taxes and other fees in connection with our use of public rights-of-way; and (2) ANACOM, primarily relating to an open contest for granting the right to use national frequencies for television service.

In addition to the guarantees indicated in the table above, as of December 31, 2010, Portugal Telecom group companies have provided the guarantees described below:

We had assumed commitments in the ordinary course of business for the purchase of network assets, telecommunications equipment and terminal equipment amounting to approximately €137 million.

Guarantees given by third parties on our behalf in connection with bank loans, as described in Note 43 to our audited consolidated financial statements, were as follows:

	Amount (EUR Millions)
Guarantees in favor of European Investment Bank	332.9
Guarantee from the Portuguese Government to Kreditanstalt Für Wiederaufbau	0.4

Finally, as part of certain sale leaseback transactions (Qualified Technological Equipment transactions, or "QTE leases") with different third parties, we have sold and then leased back certain telecommunications equipment. The flow of lease payments and our remuneration were prepaid at the outset of the contracts and, for this reason, are not shown as future lease payments in the table under " Contractual Obligations and Commercial Commitments" above. The remuneration is recognized as income over the period of the transaction. Under cross-border lease transactions entered into by TMN and PT Comunicações, we have agreed with financial institutions to issue letters of credit for the benefit of the trustee, which amounted to US$42.4 million as of December 31, 2010, equivalent to €31.8 million at the exchange rate prevailing at year end. We have recorded these QTE leases as an asset and the corresponding liability on our consolidated statement of financial position. See Notes 3(l)(ix), 30 and 40 to our audited consolidated financial statements for more information on our accounting for these transactions.

We believe that our purchase commitments are in the ordinary course of our business and that our guarantees and other financial commitments are part of our ordinary financing activities. We do not expect these commitments to have a material impact on our liquidity.

Capital Investment and Research and Development

Capital Expenditures and Financial Investments

During the year ended December 31, 2010, we made capital expenditures and financial investments (investments in other companies) totaling €802.1 million.

The table below sets out our total capital investments related to continuing operations for 2008, 2009 and 2010:

	Year Ended December 31,		
	2008	**2009**	**2010**
	(EUR Millions)		
Capital expenditures	732.0	848.1	798.4
Financial investments	2.4	10.6	3.7
Total	**734.4**	**858.7**	**802.1**

Capital Expenditures

During 2010, we made capital expenditures totaling €798.4 million. The table below sets forth our capital expenditures on tangible and intangible assets, excluding goodwill, for 2008, 2009 and 2010:

	Year Ended December 31,		
	2008	**2009**	**2010**
	(EUR Millions)		
Wireline(1)	402.8	565.4	524.1
Mobile(2)	244.6	180.1	133.1
Other	84.6	102.6	141.2
Total	**732.0**	**848.1**	**798.4**

(1) This caption excludes the real estate properties amounting to €226 million acquired from the pension funds, in connection with the transfer of unfunded pension obligations to the Portuguese Government.

(2) This caption excludes the commitments under the terms of TMN's UMTS license (€11.5 million capitalized in 2009).

Table of Contents

Capital expenditures reached €798.4 million in 2010, equivalent to 21.3% of total operating revenues, a decrease of 1.4 percentage points from 2009. The decrease in wireline capital expenditures from €565.4 million in 2009 to €524.1 million in 2010 was primarily explained by (1) lower infrastructure-related capital expenditures following the significant efforts in the fiber-to-the-home coverage undertaken in 2009, (2) lower investment in legacy infrastructure, following the fiber-to-the-home rollout and (3) lower customer-related capital expenditures notwithstanding the continued growth in Pay-TV services. Wireline capital expenditures also reflected synergies from fixed-mobile integration. The decrease in mobile capital expenditures is explained by our decision to focus on cash flow generation and synergies from fixed-mobile integration, and mobile capital expenditures continued to be directed primarily towards 3G and 3.5G networks, for both capacity and coverage, namely in the urban areas and main roads. Other capital expenditures include capital expenditures related to consolidated businesses not included in our primary segments and support companies. In 2010, these other capital expenditures increased to €141.2 million, compared to €102.6 million in 2009, primarily due to investments in African operations, especially MTC and CVT, and the expansion of Dedic's business in Brazil, including the construction of new call center sites.

In 2011, we expect to make investments similar in nature (though amounts may vary) to those made in 2010. We generally fund our capital expenditures from our cash flow from operations and from debt financing. See "*Item 4 Information on Our Company Businesses Brazilian Mobile Business Capital Expenditures*," for additional information regarding Oi's expected capital expenditures.

Financial Investments

Investments in financial assets (including goodwill) related to continuing operations amounted to €3.7 million in 2010, €10.6 million in 2009, and €2.4 million in 2008.

On July 28, 2010, we signed an agreement with Telefónica for the acquisition by Telefónica of the 50% of the capital stock of Brasilcel we owned. Brasilcel owned approximately 60% of the total share capital of Vivo. The acquisition price of such capital stock was €7,500 million, €4,500 million of which was paid at the closing of the transaction on September 27, 2010 and €1,000 million of which was paid on December 30, 2010, with the remaining €2,000 million due on October 31, 2011 (though we may request that this final payment be made on July 29, 2011, in which case this final payment, and correspondingly, the total price of the acquisition, would be reduced by €25 million). The agreement also provided for certain other commercial arrangements between Telefónica and Portugal Telecom that were subsequently rendered inapplicable. Upon closing of the transaction, the respective subscription and shareholders agreements entered into by Telefónica and Portugal Telecom in 2002 relating to their joint venture in Brazil were terminated.

On January 26, 2011, we announced that we had entered into a series of agreements with Oi, Brazil's largest telecommunications group, to acquire a significant stake in that company. In connection with our agreements to establish a strategic partnership with Oi, we also agreed to merge Dedic and GPTI, our subsidiaries that provide call center and IS/IT services in Brazil, with Contax. Contax is currently controlled by the controlling shareholders of Oi, through CTX and Contax Participações. The Oi transaction closed on March 28, 2011. We also completed the acquisition of a 16.2% stake in CTX but have not yet completed the merger of Dedic and Contax, which is subject to the approval of our board of directors and shareholders and other conditions. Following the closing of the transaction, we hold a 25.3% economic stake in Oi, and we expect to hold a 44% economic stake in CTX (42.0% prior to the merger). We paid a total of R$8.4 billion (approximately €3.8 billion at the prevailing exchange rate as of December 31, 2010) in connection with these transactions. For more information about the transaction, see "*Item 4 Information on the Company Our Businesses Strategic Alliances Strategic Partnership with Oi*."

Table of Contents

On December 29, 2010, we reached an agreement for the disposal of our 28.78% stake in Universo Online S.A., Brazil's largest internet provider by revenue, to a Brazilian businessman. The total consideration for the sale was R$356 million (€161 million as of December 31, 2010). The transaction closed on January 27, 2011.

Share Capital and Share Buyback Program

During the years ended December 31, 2010 and 2009 there were no changes in share capital. In 2008, we completed our share buyback program on July 25. We acquired and cancelled a total of 232,344,000 of our own shares within the framework of the program (the last shares we acquired were cancelled in December 2008), corresponding to 20.58% of the share capital on the date the share buyback program was proposed to the shareholders in 2007. As of April 28, 2010, our fully subscribed and paid share capital amounted to €26,895,375, represented by 896,512,500 shares with a nominal value of €0.03 each.

Research and Development

In 2010, we invested approximately €200 million in innovation, research and development, which translates into more than 5% of our total revenues. Our research and development programs focus on intelligent networks, network management systems, advanced services and systems and network integration. Our research and development activities, carried out primarily through PT Inovação, have been responsible for the introduction of innovative products and services and for the development of in-house technology. These activities have allowed our 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.

We have developed narrow and broadband network access solutions for network operators and large customers and intelligent network solutions and services for fixed and mobile operators. We have also developed advanced Web functionalities, capitalizing on our extensive customer base and drawing on a crowdsourcing system.

In addition, we seek new solutions for the rational use of energy in our operations. The selective use of voltaic panels, wind-powered generators, hydrogen fuelcells and climatization systems has enabled greater cost containment and improved efficiency.

We participate in a number of EU research and development programs, including projects in the Information Society Technologies, ACTS and Telematics programs, with Eurescom, a joint venture with our European operators and the SURESCOM Institute. In addition, we work to develop programs in partnership with domestic research and development institutes, with the active involvement of Carnegie Mellon University.

Table of Contents

Exchange Rate Exposure to the Brazilian Real

The composition of our assets and revenue base expose us to significant exchange rate risk in respect of the Brazilian Real, even after the sale of our interest in Vivo, completed on September 27, 2010, following which our total assets and indebtedness in Brazilian Reais decreased significantly. We will continue to be exposed to exchange rate risk in respect of the Brazilian Real due to our investment in Oi, which we completed on March 28, 2011. We make adjustments to equity in response to fluctuations in the value of the foreign currencies in which we have made investments, including the Brazilian Real. See " *Liquidity and Capital Resources Equity*" above.

Currency Composition of Our Assets

The table below shows the amounts of our consolidated assets held in Euro and Brazilian Reais as of December 31, 2009 and 2010.

	As of December 31,			
	2009		2010	
Consolidated Assets	**EUR Millions**	**% of total assets**	**EUR Millions**	**% of total assets**
Euro	7,572.7	51.0%	13,861.3	91.4%
Brazilian Real	6,431.5	43.3%	276.9	1.8%
Other	836.3	5.6%	1,031.7	6.8%
Total	**14,840.5**	**100.0%**	**15,169.9**	**100%**

Currency Composition of Our Indebtedness

The table below shows the amounts of our total consolidated indebtedness denominated in Euro, Brazilian Real and other currencies at December 31, 2009 and 2010. The amounts presented take into account the derivative agreements we have entered into. For further information, see Note 35 to our audited consolidated financial statements included in this report.

	As of December 31,			
	2009		2010	
Indebtedness	**EUR Millions**	**% of total indebtedness**	**EUR Millions**	**% of total indebtedness**
Euro	6,038.8	85.7%	7,186.1	99.7%
Brazilian Real	1,007.0	14.3%	6.8	0.1%
Other currencies	0.3	0.0%	13.4	0.2%
	7,046.0	**100.0%**	**7,206.3**	**100.0%**

Exposure to Exchange Rate Risk

For more detailed information as at December 31, 2010 concerning our market exposure to exchange rate risk, as well as our market exposure to interest rate risk, see "*Item 11 Quantitative and Qualitative Disclosures About Market Risk*."

As a result of our investment in Oi, our investments