TELECOM ITALIA S P A
Form 20-F
June 10, 2004
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20-F

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

OR

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

For the fiscal year ended: December 31, 2003

OR

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

For the transition period from N/A to N/A

Commission file number: 1-13882

Telecom Italia S.p.A.

(Exact name of Registrant as specified in its charter)

Italy

(Jurisdiction of incorporation or organization)

Piazza degli Affari 2, 20123 Milan, Italy

(Address of principal executive offices)

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

Title of each class	Name of each exchange on which registered
American Depositary Shares, each representing 10 Ordinary Shares of 0.55 par value each	The New York Stock Exchange
Ordinary Shares of 0.55 par value each (the Shares)	The New York Stock Exchange*
American Depositary Shares, each representing 10 Savings Shares of 0.55 par value each	The New York Stock Exchange
Savings Shares of 0.55 par value each (the Savings Shares)	The New York Stock Exchange*

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

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of Class)

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.

Not applicable

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 x No ¨ Not Applicable ¨

Indicate by check mark which financial statement item the registrant has elected to follow. Item 17 ¨ Item 18 x

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* Not for trading, but only in connection with the registration of American Depositary Shares representing such Shares or Savings Shares, as the case may be, pursuant to the requirements of the Securities and Exchange Commission.

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INTRODUCTION

Telecom Italia S.p.A. is incorporated as a joint stock company under the laws of Italy. As used in this Annual Report, unless the context otherwise requires, the term Company means Telecom Italia S.p.A. the operating company for fixed telecommunications services in Italy and the holding company for various businesses, principally telecommunications, and the terms we , us and our refers to the Company, and, as applicable, the Company and its consolidated subsidiaries.

Unless otherwise indicated, the financial information contained in this Annual Report has been prepared in conformity with the Italian law governing consolidated financial statements interpreted and integrated by the accounting principles established or adopted by the Italian Accounting Profession (Italian GAAP), which, as described in Note 27 of Notes to the Consolidated Financial Statements, differ in certain material respects from generally accepted accounting principles in the United States (U.S. GAAP). Unless otherwise indicated, any reference in this Annual Report to Consolidated Financial Statements is to the Consolidated Financial Statements of the Telecom Italia Group (including the notes thereto) included herein.

Cautionary Statement for Purposes of the Safe Harbor Provisions of the United States Private Securities Litigation Reform Act of 1995. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. This Annual Report contains certain forward-looking statements, including, but not limited to, the discussion of the changing dynamics of the marketplace, including the continuing developments in competition in all aspects of our businesses from new competitors and from new and enhanced technologies, our outlook for growth in the telecommunications industry both within and outside of Italy, including our targets under our 2004-2006 business plan and our outlook regarding developments in the telecommunications industry, including certain trends we have identified particularly in our core Italian market, continuing regulatory measures regarding pricing and access for other local operators. Such statements include, but are not limited to, statements under the following headings: (i) Item 3. Key Information Risk Factors , (ii) Item 4. Information on the Telecom Italia Group Business Significant Developments during 2003 Updated Business Plan and Strategy , (iii) Item 4. Information on the Telecom Italia Group Regulation , (iv) Item 5. Operating and Financial Review and Prospects , (v) Item 8. Financial Information Legal Proceedings and (vi) Item 11. Quantitative and Qualitative Disclosures About Market Risk , including statements regarding the likely effect of matters discussed therein. Actual results may differ materially from those projected or implied in the forward-looking statements. Such forward-looking information involves risks and uncertainties, which are outside our control, that could significantly affect expected results and are based on certain key assumptions.

The following important factors could cause our actual results to differ materially from those projected or implied in any forward-looking statements:

- the continuing impact of increased competition in a liberalized market, including competition from global and regional alliances formed by other telecommunications operators in our core Italian domestic fixed-line and wireless markets;
- our ability to introduce new services to stimulate increased usage of our fixed and wireless networks to offset declines in the traditional fixed-line voice business due to the continuing impact of regulatory required price reductions, market share loss, pricing pressures generally and shifts in usage patterns;
- the level of demand for telecommunications services, particularly wireless telecommunications services in the maturing Italian market and for new higher value added products and services such as broadband;
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our ability to achieve cost-reduction targets in the time frame established or to continue the process of rationalizing our non-core assets;

- the success of our customer loyalty and retention programs, particularly in the fixed line business, and the impact of such programs on our revenues;
- the impact of regulatory decisions and changes in the regulatory environment, including implementation of recently-adopted EU directives in Italy;
- the impact and consequences of the Merger;
- the impact of the slowdown in Latin American economies and the slow recovery of economies generally on our international business focused on Latin America and on our foreign investments and capital expenditures;
- the continuing impact of rapid or disruptive changes in technologies;

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- the impact of political and economic developments in Italy and other countries in which we operate;
- the impact of fluctuations in currency exchange and interest rates;
- our ability to successfully implement our 2004-2006 Industrial Plan;
- our ability to successfully achieve our debt reduction targets;
- our ability to successfully roll out our UMTS networks and services and to realize the benefits of our investment in UMTS licenses and related capital expenditures;
- our ability to successfully implement our internet and broadband strategy both in Italy and abroad;
- our ability to achieve the expected return on the significant investments and capital expenditures we have made and continue to make in Latin America;
- the amount and timing of any future impairment charges for our licenses, goodwill or other assets; and
- the impact of litigation or decreased mobile communications usage arising from actual or perceived health risks or other problems relating to mobile handsets or transmission masts.

The foregoing factors should not be construed as exhaustive. Due to such uncertainties and risks, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events. See Item 3. Key Information Risk Factors and the related cautionary statement under Item 5. Operating and Financial Review and Prospects .

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KEY DEFINITIONS

The following terms appearing in this Annual Report have the meanings set forth below.

Telecom Italia	means the entity which resulted from the Merger.
Telecom Italia Group	means the Company and its consolidated subsidiaries.
Old Telecom Italia and Old Telecom Italia Group	means Telecom Italia and its consolidated subsidiaries as they existed immediately prior to the effective date of the Merger.
Olivetti	means Olivetti S.p.A., the holding company and controlling shareholder of Old Telecom Italia.
Olivetti Group	means Olivetti and its consolidated subsidiaries, including Old Telecom Italia.
Merger	means the merger of Old Telecom Italia into Olivetti, approved by the shareholders of Old Telecom Italia and Olivetti on May 24, 2003 and on May 26, 2003, respectively, which became effective on August 4, 2003.
Shares	means the ordinary shares, 0.55 par value each, of Telecom Italia.
Savings Shares	means the savings shares, 0.55 par value each, of Telecom Italia.
TIM	means Telecom Italia Mobile S.p.A., the Telecom Italia Group s subsidiary operating in the mobile telecommunications business.
Telecom Italia Media	means the corporate name of the remaining part of Seat Pagine Gialle S.p.A., which resulted after the proportional spin-off of the directories and almost all of the directory assistance and business information business segments of SEAT into New SEAT. The spin-off became effective on August 1, 2003 and new SEAT was disposed of on August 8, 2003. Telecom Italia Media is the Telecom Italia Group s subsidiary operating the Internet & Media business.
EU	means the European Union.

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PART I

Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not Applicable

Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not Applicable

Item 3. KEY INFORMATION

RISK FACTORS

Strong competition in Italy may further reduce our core market share of domestic and international traffic and may cause further reductions in prices and margins.

Strong domestic competition exists in all of the principal telecommunications business areas in Italy in which we operate, including, most significantly, our fixed-line and mobile voice telecommunications businesses. This competition may increase further due to the consolidation and globalization of the telecommunications industry in Europe and elsewhere. Consolidation is increasing rapidly and competition is expected to rise at all levels in the future. In addition, the use of the single European currency and the liberalization of the Italian telecommunication market has further intensified competition by facilitating international operators entry into the Italian market and direct competition with our fixed line and mobile telephony businesses, particularly in the local and long-distance markets. As of December 31, 2003, there were a number of significant competitors offering fixed-line services and three other operators offering mobile services in the Italian domestic market; the third mobile competitor (H3G) entered the market in 2003, offering third generation commercial services. Although we stopped the decline in our market share of voice traffic in our fixed line business during 2003, continuing pressures on prices due to competition and further erosion in market shares could adversely affect our results of operations. Additional changes in the regulatory regime, including carrier preselection, number portability and local loop unbundling as well as the implementation of new EU telecommunications directives could further increase competition for the services we provide, particularly in our fixed line business, which could also adversely affect our business.

Our business may be adversely affected and we may be unable to increase our revenues if we are unable to continue the introduction of new services to stimulate increased usage of our fixed and wireless networks.

In order to sustain growth in revenues despite increased competition and lower prices, particularly in our core Italian domestic market, our strategy has been to introduce new services in our fixed-line and wireless services to increase traffic on our networks and find alternative revenue sources, in addition to carrying voice traffic on our networks. These services include non-voice services such as ADSL, which provides services such as fast Internet, multimedia and video conferencing, data traffic and value-added services such as interactive mobile services that allow users to receive news or engage in simple banking transactions. Other revenue sources also include increased interconnection traffic from other operators using our fixed-line network. In addition to the introduction of new services in recent years, we continue to develop new products and services, such as new data services for business customers, broadband services, enhanced communication services and new equipment and voice packages, in order to attract and retain customers, particularly business customers, and to stimulate usage of our fixed and wireless telecommunications network. We are also investing in new infrastructure and technologies to enable us to introduce new products and services. We expect that these strategic initiatives will require substantial expenditures and commitment of human resources. Although these initiatives are core to our strategy, we may be unable to introduce commercially these new products and services, and even if we introduce them, there can be no assurance they will be successful.

Our business will be adversely affected if we are unable to successfully implement our business plans, particularly in light of the Merger. Factors beyond our control may prevent us from successfully implementing our strategy.

Following the change in control of Old Telecom Italia in late 2001, we adopted our 2002-2004 Industrial Plan (the Industrial Plan) and established priorities for this three year period. The main objectives were to:

- Strengthen competitive capabilities;

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- Improve cost efficiency; and
- Strengthen the financial structure.

Significant portions of the Industrial Plan were completed during 2002 and 2003, particularly the sale of non-core assets and debt reduction. We also took steps to strengthen our competitive position in our core Italian domestic market through the introduction of new products and tariff packages and our focus on lowering costs through the reduction of operating expenses and capital expenditures.

In connection with the Merger, we confirmed the objectives and guidelines of the Industrial Plan and stated that we had established certain targets, which include strict limits on capital expenditures and cost controls, together with further assets sales, to reduce the significantly higher levels of debt we have as a result of the Merger.

Factors beyond our control that could affect the further implementation and completion of the Industrial Plan and reaching our targets for the period 2004-2006 include:

- our ability to manage costs;
- our ability to attract and retain highly-skilled and qualified personnel;
- our ability to divest additional non-core businesses and the adequacy of the returns of such divestitures;
- our ability to leverage on our core skills with particular focus on Latin America mobile and international broadband operations;
- difficulties in developing and introducing new technologies, managing innovation, providing value-added services and increasing usage of our networks;
- our ability to manage the fixed to mobile substitution trends;
- the need to establish and maintain strategic relationships;
- declining prices for some of our services and increasing competition;
- the effect of adverse economic trends on our principal markets;
- the effect of foreign exchange fluctuations on our results of operations; and
- the success of new disruptive technologies that could cannibalize fixed and mobile revenues.

Regulatory decisions and changes in the regulatory environment could adversely affect our business.

Our fixed and mobile telecommunications operations, as well as our broadband services businesses, are subject to significant extensive regulatory requirements in Italy and our international operations and investments are subject to regulation in their host countries. In Italy, we are the only operator subject to universal service obligations, which requires us to provide:

- fixed line public voice telecommunications services in non-profitable areas;
- subscriber information services at affordable prices; and
- public payphones.

In addition, the Italian regulator responsible in Italy for the regulation of the telecommunications, radio and television broadcasting sector (the National Regulatory Authority) has identified the Company as an operator having significant market power in all relevant markets. As a result, we are, or will be, subject to a number of regulatory constraints, including:

- a requirement to conduct our business in a transparent and non-discriminatory fashion;
- a requirement to have our prices for fixed voice telephony services and Reference Interconnection Offer, the tariff charged to other operators to utilize our network, subject respectively to a price cap and a network cap mechanism. This cap mechanism places certain limits on our ability to change our prices for certain services; and
- a requirement to provide interconnection services, leased lines and access to the local loop to other operators at cost-oriented prices. These services include allowing other operators to connect to our network and transport traffic through the network as well as offering certain services related to our local access network, or local loop, on an unbundled basis to these other operators to enable these operators directly to access customers connected to the network by leasing the necessary components from us.

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As a member of the EU, Italy is required to adapt its telecommunications regulatory framework to the legislative and regulatory framework established by the EU for the regulation of the European telecommunications market. The EU Commission approved a new electronic communications framework in March 2002 which has been effective in Italy since September 2003. The implementation of these revised telecommunications regulations and possible future decisions relating thereto may change the regulatory environment in a manner adverse to us. Please see Item 4. Information on the Telecom Italia Group Regulation in this report for more information on the regulatory requirements to which we are subject.

We are unable to predict the impact of any proposed or potential changes in the regulatory environment in which we operate both in Italy and internationally. Changes in laws, regulation or government policy could adversely affect our business and competitiveness. In particular, our ability to compete effectively in our existing or new markets could be adversely affected if regulators decide to expand the restrictions and obligations to which we are subject or extend them to new services and markets. In addition, changes in tax laws in countries in which we operate could adversely affect our results of operations. Finally, decisions by regulators regarding the granting, amendment or renewal of licenses, to us or to third parties, could adversely affect our future operations in Italy and in other countries where we operate.

We may not achieve the expected return on our significant investments and capital expenditures made in Latin America due to the competitive environment in these markets.

In recent years we have repositioned our international strategy, sold significant non-core international assets, and elected to focus our international strategy on:

- consolidating our international presence in Latin America;
- developing our international investments in high-growth market segments, such as wireless, data and internet (broadband);
- strengthening our role of strategic partner in existing investments by increasing the transfer of our technological expertise and marketing know-how; and
- rationalizing our existing international portfolio by divesting minority participations in non-strategic geographical markets.

As a result of this change in strategy, in the 2002-2003 period we divested certain of our most significant European assets such as BDT (Bouygues Decaux Telecom), Autel (Mobilkom Austria), Telekom Austria, 9Telecom group and Auna and we are still seeking to divest certain international non-strategic assets. In addition, certain investments which were made during the 1999-2001 period declined significantly in value resulting in write-downs and asset impairments which materially adversely affected our results of operations in 2001 and 2002, with a lesser impact in 2003. We will continue to target our international investments in Latin America, particularly mobile telecommunications in Brazil, European broadband and mobile telecommunications in selected markets. These investments will require significant capital expenditures and there can be no assurance that we will be able to achieve a return on our investments in markets where we have previously suffered losses and writedowns.

Continuing rapid changes in technologies could increase competition or require us to make substantial additional investments.

Many of the services we offer are technology-intensive and the development of new technologies may render such services non-competitive. We make and will have to make substantial additional investments in new technologies to remain competitive. The new technologies we choose may not prove to be commercially successful. In addition, we may not receive the necessary licenses to provide services based on new technologies in Italy or abroad. As a result, we could lose customers, fail to attract new customers or incur substantial costs in order to maintain our customer base.

The value of our operations and investments may be adversely affected by political and economic developments in Italy or other countries.

Our business is dependent on general economic conditions in Italy, including levels of interest rates, inflation and taxes. A significant deterioration in these conditions could adversely affect our business and results of operations. We may also be adversely affected by political and economic developments in other countries where we have made significant investments in telecommunications operators. Some of these countries have political, economic and legal systems that are unpredictable. Political or economic upheaval or changes in laws or their application in these countries may harm the operations of the companies in which we have invested and impair the value of these investments. We have had investments in Turkey, Argentina and Brazil in recent years in which we have had to take significant write-downs in value due to political and economic developments in those countries. A significant additional risk of operating in emerging market countries is that foreign exchange restrictions could be established. This could effectively prevent us from receiving profits from, or from selling our investments in, these countries.

Fluctuations in currency exchange and interest rates may adversely affect our results.

Because we have made substantial international investments, primarily in U.S. dollars, and have significantly expanded our operations outside the euro zone, particularly in Latin America, movements in the exchange rates of the euro against other currencies can adversely affect our revenues and operating results. A rise in the value of the euro relative to other currencies in certain countries in which we operate or have made investments will reduce the relative value of the revenues or assets of our operations in those countries and, therefore, may adversely affect our operating results or financial position. In addition, we have raised, and may raise in an increasing proportion in the future, financing in currencies other than the euro, principally the U.S. dollar. Accordingly, the value of those liabilities will be affected by fluctuations of the currencies of the countries in which we operate against the currency in which the financing is denominated. We generally enter into a number of forward currency transactions, swaps and options to manage foreign currency risk exposure with respect to our non-euro denominated liabilities. However, we can give no assurances that we will be successful in managing foreign currency risk exposure, taking into consideration that appropriate foreign currency swaps and options may not be available as needed on the relevant financial markets. In recent years reported results of our Latin American operations have been adversely affected by changes in local currencies against the euro. During 2003, in particular, the strengthening of the euro against local currencies in Latin America adversely affected our reported revenues in euro by 641 million.

Our total gross financial debt at year end 2003 was 41,465 million (40,631 million at year end 2002) and included borrowings of 5,274 million relating to the cash out for the Merger. Although our total interest payable has decreased as the result of average debt exposure reduction and of interest rate fluctuations our exposure of total debt subject to floating interest rates increased as a result of the Merger. We enter into derivative transactions to hedge our interest exposure and to diversify debt parameters in order to reduce debt cost and volatility within predefined target boundaries. However, we can give no assurance that fluctuations in interest rates will not adversely affect our results of operations.

We may not realize the benefits of our investment in UMTS licenses and related capital expenditures.

Through our mobile businesses, we have acquired two third generation mobile telephone, or UMTS, licenses to commence operations of UMTS services in Italy and Greece. Our Italian mobile company, TIM, committed to pay 2,417 million for its license, with 2,066 million paid in December 2000 and three installments of 117 million paid in November 2001, November 2002 and December 2003, for its UMTS license in Italy and, through its subsidiary STET Hellas, a further 145 million for a UMTS license in Greece (of which approximately 101 million has already been paid). The size of the market for UMTS products and services is unknown and may fall short of the industry s expectations. We cannot be certain that the demand for such services will justify the related costs. In some locations, we have made investments, although required under the licenses, which may not be commercially desirable. In addition, we have a number of significant competitors in each of these geographic markets planning to offer these services.

We will be rolling out the UMTS networks, together with our competitors, in compliance with the terms and conditions of our respective licenses. Given the substantial costs of upgrading our existing networks to support UMTS and the uncertainty regarding the commercial adoption of UMTS, we may not be able to recoup our investment according to our estimates, if at all. The commercial success of UMTS will also depend on handset availability and their price. We have entered into and intend to enter into arrangements with other operators to share the costs and infrastructure of our planned UMTS networks. However, we cannot give any assurance that we will succeed in concluding the necessary agreements with other operators on satisfactory terms. Moreover, while network sharing is intended to reduce costs, we cannot give any assurance that this will be the case or that we will be able to make such network sharing work commercially or technically.

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The mobile telecommunications market in Italy has matured and become saturated in recent years and growth has slowed significantly which means our revenues may not grow as rapidly as in the past.

In recent years, our consolidated revenues have grown or remained stable in large part because of the rapid growth in the mobile communications business which has offset flat or declining revenues in our Italian fixed line business. This growth has been driven largely by the rapid expansion of the mobile telecommunications market in Italy. However, as a result of this growth, the Italian market is approaching saturation levels, with penetration rates now around 99%. TIM s domestic market share has remained relatively stable at approximately 46% in the past two years so revenue growth is no longer driven by the rapid subscriber growth which TIM experienced in the 1998-2001 period.

Continued growth in the mobile telecommunications markets in which we operate will depend on a number of factors, many of which are outside our control. These factors include:

- the activities of our competitors, including consolidation, tariff reductions and handset subsidies;
- the development and introduction of new and alternative technologies for mobile telecommunications products and services and the attractiveness of these to customers;
- the success of new disruptive technologies;
- customer usage habits;
- general economic conditions; and
- health risks or safety concerns associated with mobile telephones and transmission equipment.

If the mobile telecommunications markets in which we operate do not continue to expand, or we are unable to retain our existing customers or stimulate increases in customer usage, our financial condition and results of operations may be harmed.

Devaluations of telecom assets and write-downs could adversely affect our financial condition and results of operations.

In the past three years the market for telecom stocks and credit ratings of market participants, as well as our ongoing review and refinement of our business plan, has resulted in substantial impairment write-downs of our assets which materially adversely affected our results of operations in 2001 and 2002. There can be no assurance that similar events in the future may not result in further substantial impairment write-downs from assets. Accounting standards relating to asset valuations and impairment may be refined to require the use of new criteria or methodology. Beginning in fiscal year 2002, under U.S. GAAP, we tested goodwill for impairment pursuant to SFAS 142 Goodwill and Other Intangible Assets . In accordance with the provisions of SFAS 142, goodwill is no longer amortized, but is subject to annual impairment tests based on fair value. An interim assessment of goodwill may be necessary if an impairment indicator indicates that the fair value of a reporting unit may have decreased. Future changes in the fair value of our business units could adversely affect our U.S. GAAP results and financial conditions.

We may be adversely affected if we fail to successfully implement our Internet and broadband strategy in Italy and internationally.

The introduction of internet and broadband services are an important element of our growth strategy and means to increase the use of our networks in Italy and expand our operations outside of Italy, particularly in Europe. Our strategy is to replace the mature, traditional voice services with value added contents and services to consumers and small and medium-sized companies. Our ability to successfully implement this strategy may be affected if:

- Internet usage in Italy grows more slowly than anticipated, for reasons such as changes in Internet users preferences;
- broadband penetration in Italy and other European countries does not grow as we expect;
- competition increases, for reasons such as the entry of new competitors, consolidation in the industry or technological developments introducing new platforms for internet access and/or internet distribution or other operators can provide broadband connections superior to that we can offer; and
- we experience any network interruptions or related problems with network infrastructure.

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Outside of Italy our ability to implement this strategy will depend on whether we are able to acquire assets or networks or utilize networks of incumbent operators that will allow us to offer such services.

Any of the above factors may adversely affect our business and results of operations.

System failures could result in reduced user traffic and reduced revenue and could harm our reputation.

Our technical infrastructure (including our network infrastructure for fixed-line and mobile telecommunication services) is vulnerable to damage or interruption from information and telecommunication technology failures, power loss, floods, windstorms, fires, terrorism, intentional wrongdoing, human error and similar events. Unanticipated problems at our facilities, system failures, hardware or software failures, computer viruses or hacker attacks could affect the quality of our services and cause service interruptions. Any of these occurrences could result in reduced user traffic and reduced revenue and could harm our reputation.

Actual or perceived health risks or other problems relating to mobile handsets or transmission masts could lead to litigation or decreased mobile communications usage.

Various reports have alleged that certain radio frequency emissions from wireless handsets and transmission equipment may be linked to various health concerns and may interfere with various electronic devices. We cannot rule out that exposure to electromagnetic fields or other emissions originating from wireless handsets will not be identified as a health risk in the future. Our mobile communications business may be harmed as a result of these alleged health risks. For example, the perception of these health risks could result in a lower number of customers, reduced usage per customer or potential consumer liability.

In addition, although Italian law already requires strict limits in relation to transmission equipment, these concerns may cause regulators to impose greater restrictions on the construction of base station towers or other infrastructure, which may hinder the completion of network build-outs and the commercial availability of new services.

As a result of the Merger of Old Telecom Italia and Olivetti we remain highly leveraged.

Under Italian GAAP, our gross financial debt was 41,465 million at December 31, 2003, compared with 40,631 million at December 31, 2002, and our total net financial debt was approximately 33,346 million as of December 31, 2003 compared with 33,399 million at December 31, 2002. See Note 9 of Selected Financial and Statistical Information which reconciles our net financial debt to our gross debt. The amounts at December 31, 2003 take into account the Merger, including indebtedness of 5.3 billion incurred to finance the withdrawal rights and the tender offers which were part of the overall Merger transaction. We were able to maintain our overall gross and net financial debt levels after giving effect to the 5.3 billion described above due to:

- significant cash flow generation by our core businesses as well as by our focus on the management of working capital, and

- net proceeds from disposals completed during 2003 used to reduce outstanding debt which offset the borrowings needed for the cash out for the Merger.

By the end of 2004, we are targeting to reduce our net financial debt below 30 billion principally through cash flow generation. There can be no assurance that factors beyond our control, including but not limited to deterioration in general economic conditions, will not significantly affect our ability to reduce such debt.

In 2005 we will be obliged to adopt International Financial Reporting Standards (IFRS) which will impact our financial results as they differ in significant respects from Italian GAAP.

We currently prepare our financial statements in accordance with Italian GAAP. In June 2002, the Council of Ministers of the EU adopted new regulations requiring all listed EU companies, including us, to apply IFRS (previously known as International Accounting Standards or IAS) in preparing their consolidated financial statements from January 1, 2005. Because IFRS emphasizes the measure of the fair value of certain assets and liabilities, applying these standards to our financial statements may have a considerable impact on a number of important areas, including, among others, goodwill and intangible assets, employee benefits and financial instruments, accounting for share-based payments, long-term assets and business combinations. Because our financial statements prepared in accordance with IFRS will differ from our financial statements prepared in accordance with Italian GAAP, the methods used by the financial community to assess our financial performance and value our publicly-traded securities could be affected. Please see Item 5. Operating and Financial Review and Prospects Adoption of International Accounting Standards .

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EXCHANGE RATES

We published our consolidated financial statements in euros. References to , euro and Euro are to the euro, the single unified currency that was introduced in Italy and 10 other member states of the European Union on January 1, 1999. References to lire , lira and Lit. are to Italian lire, the former Italian non-decimal denomination of the euro, and references to U.S. dollars , dollars , U.S.$ or $ are to U.S. dollars, the currency of the United States. The exchange rate at which the lira was irrevocably fixed against the euro is Lit.1,936.27 = 1.00.

For convenience only (except where noted otherwise), certain euro figures have been translated into dollars at the rate (the Euro/Dollar Exchange Rate) of 1.00 = U.S.$1.2210, using the noon buying rate in The City of New York for cable transfers in foreign currencies as announced by the Federal Reserve Bank of New York for customs purposes (the Noon Buying Rate) on June 1, 2004. These translations should not be construed as a representation that the euro amounts actually represent such dollar amounts or have been or could be converted into dollars at the rate indicated.

The Federal Reserve Bank of New York no longer quotes a Noon Buying Rate for the legacy currencies of any of the Member States.

For the purpose of this Annual Report, billion means a thousand million.

The following table sets forth for the years 1999 to 2003 and for the beginning of 2004 certain information regarding the Noon Buying Rate for Dollars expressed in U.S.$ per 1.00.

Calendar Period	High	Low	Average(1)	At Period End
1999	1.1812	1.0016	1.0588	1.0070
2000	1.0335	0.8270	0.9207	0.9388
2001	0.9535	0.8425	0.8909	0.8901
2002	1.0485	0.8594	0.9495	1.0485
2003	1.2597	1.0361	1.1411	1.2597
2004 (through June 1, 2004)	1.2853	1.1801	1.2265	1.2210
Monthly Amounts				
December 2003	1.2597	1.1956	1.2284	1.2597
January 2004	1.2853	1.2389	1.2638	1.2452
February 2004	1.2848	1.2426	1.2640	1.2441
March 2004	1.2431	1.2088	1.2261	1.2292
April 2004	1.2358	1.1802	1.1989	1.1975
May 2004	1.2274	1.1801	1.1989	1.1975
June 2004 (through June 1, 2004)	1.2210	1.2210	1.2210	1.2210

(1) Average of the rates for the last business day of each month in the relevant period except for 2004 for which the date used is June 1, 2004.

The shares and savings shares of Old Telecom Italia and the shares of Olivetti have traded on *Mercato Telematico Azionario* (Telematico), managed by Borsa Italiana S.p.A. (Borsa Italiana) in euro since January 4, 1999. Fluctuations in the exchange rate between the euro and the U.S.

dollar will affect the U.S. dollar equivalent of the euro price of the Shares and the Savings Shares and the price of the American Depositary Shares (ADSs) and the Savings Share American Depositary Shares (Savings Share ADSs), on the New York Stock Exchange (NYSE). Cash dividends were paid by Old Telecom Italia and Olivetti in lire until 2001 (Olivetti paid no dividend in 2001) and in euro starting from 2002 (Olivetti paid no dividend in 2002). Exchange rate fluctuations will affect the U.S. dollar amounts received by owners of ADSs and Savings Share ADSs upon conversion by the Depositary of cash dividends paid in euro on the underlying Shares and Savings Shares. See Item 10. Additional Information Description of American Depositary Receipts .

On completion of the Merger, Telecom Italia (formerly Olivetti) became a successor registrant to Old Telecom Italia under the Securities Exchange Act of 1934, as amended (the 1934 Act) and, therefore, became subject to and continues to file periodic reports under the 1934 Act required for a foreign private issuer. Telecom Italia (formerly Olivetti) obtained a listing of the Shares and Savings Shares issued at completion of the Merger, on the NYSE where such Shares and Savings Shares trade in the form of ADSs.

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SELECTED FINANCIAL AND STATISTICAL INFORMATION

The Merger of Old Telecom Italia with and into Olivetti became effective on August 4, 2003. Olivetti was the surviving company in the Merger (and changed its name to Telecom Italia S.p.A.), and succeeded to the business of Old Telecom Italia.

As a result of the Merger, the summary selected financial data set forth below are consolidated financial data of Olivetti, not Old Telecom Italia, and are presented on the following basis:

- the Telecom Italia Group s selected financial data as of and for the year ended December 31, 2003 have been extracted or derived from the consolidated financial statements of the Telecom Italia Group prepared in accordance with Italian GAAP and which have been audited by Reconta Ernst & Young S.p.A. independent auditor;
- the Telecom Italia Group s selected financial data as of and for each of the years ended December 31, 2002, 2001, 2000 and 1999 have been extracted or derived (other than the 2000 pro forma data) from the Olivetti Group s consolidated financial statements prepared in accordance with Italian GAAP and which have been audited by the following independent auditors: Reconta Ernst & Young S.p.A. (for the years ended December 31, 2002 and 2001), PricewaterhouseCoopers S.p.A. (for the years ended December 31, 2000 and 1999); and
- the summary historical consolidated financial data for the Telecom Italia Group as of March 31, 2004, and for the three months ended March 31, 2004 and 2003, have been derived from unaudited interim consolidated financial statements which, in our opinion, reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of our results of operations for the unaudited interim periods. Results for the three months ended March 31, 2004 are not necessarily indicative of results that may be expected for the entire year.

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Unless otherwise indicated, amounts presented are based on Italian GAAP. The selected financial data below should be read in conjunction with the Consolidated Financial Statements and notes thereto included elsewhere in this Annual Report.

	Year ended December 31,						Three Months ended March 31,	
	1999(1)	2000(1)	2000 pro forma (Unaudited) (1)(2)	2001(1)	2002(1)	2003(1)	2003(1)	2004(1)
	(millions of Euro, except per share amounts)						(Unaudited)	
Statement of Operations Data in accordance with Italian GAAP:								
Operating revenues	28,207	30,116	28,374	32,016	31,408	30,850	7,291	7,418
Other income	512	483	459	476	504	345	69	58
Total revenues	28,719	30,599	28,833	32,492	31,912	31,195	7,360	7,476
Cost of materials	3,689	3,058	2,931	2,640	2,315	2,081	415	452
Salaries and social security contributions	5,231	5,245	4,965	4,919	4,737	4,303	1,115	1,033
Depreciation and amortization(3)	6,013	6,946	6,509	7,612	7,227	6,779	1,653	1,590
Other external charges	9,612	11,136	10,476	12,687	12,188	11,934	2,813	2,813
Changes in inventories	(79)	(318)	(296)	92	62	114	(18)	(44)
Capitalized internal construction costs	(1,066)	(912)	(831)	(583)	(675)	(805)	(145)	(156)
Total operating expenses(3)	23,400	25,155	23,754	27,367	25,854	24,406	5,833	5,688
Operating income(3)	5,319	5,444	5,079	5,125	6,058	6,789	1,527	1,788
Financial income	1,468	1,202	1,162	1,446	1,569	992	288	292
Financial expense(3)	(2,252)	(3,857)	(3,648)	(6,559)	(4,647)	(3,256)	(940)	(722)
Of which write-downs and equity in losses in affiliated and other companies, net	*(569)*	*(1,037)*	*(1,025)*	*(1,771)*	*(487)*	*(91)*	*(82)*	*(14)*
Other income and (expense), net	5,667	135	165	(3,109)	(5,496)	(1,083)	(7)	(14)
Income (loss) before income taxes and minority interests	10,202	2,924	2,758	(3,097)	(2,516)	3,442	868	1,344
Income taxes	(3,207)	(1,923)	(1,813)	(579)	2,210	(1,014)	(713)	(809)
Net income (loss) before minority interests	6,995	1,001	945	(3,676)	(306)	2,428	155	535
Minority interests	(2,056)	(1,941)	(1,885)	586	(467)	(1,236)	(552)	(258)
Net income (loss)	4,939	(940)	(940)	(3,090)	(773)	1,192	(397)	277

Net income (loss) per Share(4)	1.03	(0.20)	(0.20)	(0.36)	(0.09)	0.07	(0.05)	0.01
Dividends per Share	0.0310	0.0350	0.0350			0.1041(5)		
Dividends per Savings Share	0.1937					0.1151(5)		
Dividends per Preferred Shares	0.0362							

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	Year ended December 31,					
	1999(1)	2000(1)	2000 pro forma (Unaudited) (1)(2)	2001(1)	2002(1)	2003(1)
	(millions of Euro, except per share amounts)					
Amounts in accordance with U.S. GAAP:						
Total revenues				30,849	30,432	30,519
Operating income				3,661	7,225	8,095
Net income (loss) before minority interests, discontinued operations and cumulative effect of accounting changes				(2,932)	6,231	3,135
Minority interests				18	(3,016)	(1,523)
Net income (loss) from discontinued operations				(1,112)	(1,259)	250
Cumulative effect of accounting changes, net of tax				20		(21)
Net income (loss)				(4,006)	1,956	1,841
Net income (loss) per Share before discontinued operations and cumulative effect of accounting changes Basic				(0.85)	0.79	0.18
Net income (loss) per Share before discontinued operations and cumulative effect of accounting changes Diluted				(0.85)	0.79	0.18
Net income (loss) per Share from discontinued operations Basic				0.01	0.00	0.00
Net income (loss) per Share from discontinued operations Diluted				0.01	0.00	0.00
Net income (loss) per Share from cumulative effect of accounting changes Basic				0.01	0.00	(0.00)
Net income (loss) per Share from cumulative effect of accounting changes Diluted				0.01	0.00	(0.00)
Net income (loss) per Share Basic(6)				(1.17)	0.48	0.20
Net income (loss) per Share Diluted(6)				(1.17)	0.48	0.20

	As of December 31,						As of March 31,
	1999(1)	2000(1)	2000 pro forma (Unaudited) (1)(2)	2001(1)	2002(1)	2003(1)	2004(1)
	(millions of Euro)						(Unaudited)
Balance Sheet Data in accordance with Italian GAAP:							
Total current assets(3)	15,892	21,097	20,957	23,417	22,597	22,498	22,082
Fixed assets, net	23,865	23,776	21,072	22,097	19,449	18,324	17,977
Intangible assets, net(3)	28,006	39,528	39,062	39,045	34,412	33,853	33,474
Total assets	75,526	95,360	91,832	94,227	83,384	80,501	79,537
Short-term debt	6,000	16,927	16,536	9,072	6,827	10,613	6,863
Total current liabilities	20,099	30,179	29,207	22,984	20,385	23,373	19,222
Long-term debt	24,291	27,485	25,950	37,747	33,804	30,852	33,071
Total liabilities	49,216	63,994	61,304	67,874	62,760	59,912	58,358
Total stockholders equity before minority interest	9,549	13,856	13,856	12,729	11,640	16,092	16,390
Total stockholders equity	26,310	31,366	30,528	26,353	20,624	20,589	21,179

Amounts in accordance with U.S. GAAP:			
Total current assets	22,786	21,599	21,342
Fixed assets, net	24,331	21,503	21,593
Intangible assets, net	45,880	41,170	58,479
Total assets	103,588	92,911	108,093
Total current liabilities	22,725	18,599	23,196
Long-term debt	43,117	38,375	32,586
Total liabilities	76,436	68,314	67,946
Stockholders equity(7)	13,612	15,224	35,067

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	As of December 31,						As of March 31,	
	1999(1)	2000(1)	2000 pro forma (Unaudited) (1)(2)	2001(1)	2002(1)	2003(1)	2003(1)	2004(1)
							(Unaudited)	
Financial Ratios in accordance with Italian GAAP:								
Gross operating margin (Gross operating profit/operating revenues)(%)(8)	43.0	43.6	43.1	42.7	44.6	46.3	45.4	47.1
Operating income/operating revenues (ROS) (%)	18.9	18.1	17.9	16.0	19.3	22.0	20.9	24.1
Net debt/Net invested capital (debt ratio)(%)(9)	51.0	54.5	53.9	59.3	61.8	61.8	60.7	59.2
Ratio of Earnings to fixed charges(10)	11.82	2.76	2.87	0.58	0.21	2.55	2.59	3.56
Financial Ratios in accordance with U.S. GAAP:								
Ratio of Earnings to fixed charges(10)				0.71	2.15	3.02		
Statistical Data:								
Subscriber fixed lines in Italy (thousands)(11)	26,502	27,153	27,153	27,353	27,142	26,596	27,107	26,429
ISDN equivalent lines in Italy (thousands)(12)	3,049	4,584	4,584	5,403	5,756	6,027	5,888	6,008
Broadband Access in Italy and abroad (ADSL + XDSL) (thousands)(13)				390	850	2,200	1,100	2,800
Voice Offers in Italy (thousands)(14)				4,094	5,224	5,547	5,392	5,546
Network infrastructure in Italy:								
- access network in copper (millions of km pair)	103.4	104.0	104.0	104.3	104.3	105.2	104.3	105.2
- access network and transport in fiber optics (millions of km of fiber optics)	2.9	3.1	3.1	3.2	3.6	3.6	3.60	3.65
Network infrastructure abroad:								
- european backbone (km of fiber optics)		36,600	36,600	36,600	36,600	39,500	36,600	39,500
TIM lines in Italy (thousands)(15)	18,527	21,601	21,601	23,946	25,302	26,076	25,657	26,036
TIM group foreign lines (thousands)(16)	4,788	7,637	7,637	10,923	13,809	18,438	14,514	21,601
TIM group lines total (Italy + foreign in thousands)(16)	23,315	29,238	29,238	34,869	39,111	44,514	40,171	47,637
GSM penetration in Italy (% of population)	99.2	99.6	99.6	99.7	99.8	99.8	99.8	99.8
E-TACS penetration in Italy (% of population)	97.9	98.0	98.0	98.0	98.0	97.9	97.9	97.9
Page views Virgilio (millions)	505	2,218	2,218	3,945	5,267	6,612	1,641	1,905
Group s employees (at period-end)	129,073	120,973	113,475	116,020	106,620	93,187	104,379	93,036
Group s employees (average number)	128,603	131,266	123,994	113,974	107,079	95,804	99,982	89,083
Operating revenues/Group s employees (average number) (thousands)	219.3	229.4	228.8	280.9	293.3	322.0	72.9	83.3

(1) Beginning with the consolidated financial statements for the year ended December 31, 2001, under Italian GAAP, Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group), which in 2000 were consolidated proportionally, have been accounted for using the equity method. Prior to 2000 the
Nortel Inversora group was accounted for on the equity method. Under U.S. GAAP, the Nortel Inversora group is accounted for using the equity method. These differences in accounting treatment for 2000 did not affect net income and stockholders equity but had an impact on other line items, such as operating revenues and operating expenses, as well as a number of balance sheet line items.

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(2) The 2000 unaudited pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(3) Beginning in 2003, Telecom Italia changed the manner in which it accounts for bond issuance expenses including them under current assets (prepaid expenses). Previously, such costs were included in Intangible assets, net. Consequently this change also impacted certain statement of operations items. As a result of this change, the previous periods have been reclassified and presented consistent with the 2003 presentation.

(4) Net income per Share in 1999 is calculated on the basis of 4,812,541,305 shares outstanding, of which 4,721,387,429 Shares, 15,221,888 Preferred Shares and 75,931,988 Savings Shares (net of 2,697,500 Shares of treasury stock acquired from employees in the prior years). Net loss per Share in 2000 is calculated on the basis of 4,700,065,553 Shares outstanding, net of 214,628,828 Shares of treasury stock of which 2,697,500 Shares were held by the Company and 211,931,328 Shares were held by its subsidiary Olivetti International S.A..

Net loss per Share in 2001 is calculated on the basis of 8,569,072,736 Shares outstanding, net of 214,628,828 Shares of treasury stock held by the Company and by its subsidiary Olivetti International S.A.. Net loss per Share in 2002 is calculated on the basis of 8,630,610,804 Shares outstanding, net of 214,628,828 Shares of treasury stock.

Net income per Share in 2003 is calculated on the basis of 15,996,955,942 shares outstanding, of which 10,201,034,873 Shares and 5,795,921,069 Savings Shares; the 10,201,034,873 Shares outstanding are net of 101,208,867 Shares of treasury stock already held by the Company and its subsidiary Olivetti International S.A. resulting from the redistribution of the share capital in connection with the Merger.

The significant changes in share capital compared with the end of 2002 were mainly due to the Merger of Old Telecom Italia into Olivetti, effective from August 4, 2003, which provided for an exchange ratio of 7 Olivetti ordinary shares, par value 1 each, for every ordinary share of Old Telecom Italia, par value 0.55 each, and 7 Olivetti savings shares, par value 1 each for every savings share of Old Telecom Italia, par value 0.55 each. From August 4, 2003, the Shares and Savings Shares of Telecom Italia were issued as a result of the Merger. The change in the number of issued shares in the year 2003 can be analyzed as follows:

- *until August 4, 2003*: (a) issuance of 11,361,740 ordinary shares of which 11,137,324 ordinary shares were issued on conversion of Olivetti 1.5% 2001-2010 convertible bond with redemption premium , 141,134 ordinary shares were issued on the exercise of Olivetti 2001-2002 ordinary share warrants and 83,282 ordinary shares were issued on the conversion of Olivetti 1.5% 2001-2004 convertible bond with redemption premium ; (b) cancellation of 10,958,057 ordinary shares following the exercise of withdrawal rights of dissenting shareholders as permitted in accordance with the terms of the Merger; (c) cancellation of the remaining 8,845,643,315 ordinary shares (including 214,628,828 treasury shares), par value 1 each, to be replaced by new Shares;

- *on and after August 4, 2003*: (a) issuance of 10,287,061,839 new Shares, par value 0.55 each (including 101,208,867 treasury shares), and 5,795,921,069 new Savings Shares, par value 0.55 each, in substitution for the cancelled shares; (b) issuance of 15,181,901 new Shares, of which 11,009,743 shares were issued on the exercise of ex Telecom Italia 1999 Stock Option Plan , 4,028,290 shares were issued on the conversion of Olivetti 1.5% 2001-2010 convertible bonds with redemption premium and 143,868 shares were issued on the conversion of Olivetti 1.5% 2001-2004 convertible bonds with redemption premium .

For more details on changes in stockholders equity for the years ended December 31, 2001, 2002 and 2003, respectively, please see page F-6, Telecom Italia S.p.A. Statements of Consolidated Stockholders Equity for the Years Ended December 31, 2001, 2002 and 2003 of our Consolidated Financial Statements included elsewhere herein.

The calculations take into account the requirement that holders of Savings Shares are entitled to an additional dividend equal to 2% of the par value of shares above dividends paid on the Shares; until July 2000 the par value of ordinary, savings and preferred shares was Lire 1,000 per share. Furthermore, the Extraordinary Shareholders Meeting of Telecom Italia (formerly Olivetti S.p.A.) held on July 4, 2000 approved the conversion of 15,221,888 preferred shares and 78,629,488 savings shares, at par value, into an equal number of ordinary shares. Approval was also given during the same Extraordinary Shareholders Meeting to the free of charge share capital increase by utilizing unrestricted reserves, increasing the par value from Lire 1,000 to Lire 1,936.27 (corresponding to Euro 1) of all the ordinary shares (both issued ordinary shares and shares that would have been issued in the future by implementing the resolutions previously passed with regard to conversion of bonds and the exercise of warrants), with the concurrent redenomination of share capital in Euro. Finally, following the Merger, effective from August 4, 2003, the

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Telecom Italia share capital consists of Shares and Savings Shares. Net income per Savings Share was 1.04 in 1999, 0.08 in 2003 and 0.02 in the first quarter of 2004.

(5) Telecom Italia s dividend coupons for the year ended December 31, 2003, were clipped on May 24, 2004, and such dividends for the year ended December 31, 2003 were payable from May 27, 2004.

(6) In accordance with U.S. GAAP, the Net income (loss) per Share has been calculated using the two class method, since the Company has both Shares and Savings Shares outstanding. Under this method, set forth in Statement of Financial Accounting Standards No. 128, Earnings per Share , Basic earnings per share is computed by dividing income available to shareholders by the weighted average number of shares outstanding, and diluted earnings per share is increased to include any potential common shares and is adjusted for any changes to income that would result from the assumed conversion of those potential common shares. For the purpose of these calculations, the weighted average number of Shares was 3,424,694,178 for the year ended December 31, 2001 and 4,054,375,543 for the year ended December 31, 2002 and the weighted average number of Shares and Savings Shares was 6,620,513,494 and 2,414,967,112 for the year ended December 31, 2003. The calculations take into account the requirement that holders of Savings Shares are entitled to an additional dividend equal to 2% of the par value of Savings Shares above dividends paid on the Shares. The calculations take also into account that 2001 and 2002 (after the redenomination of the share capital into Euro following the resolution taken by the Extraordinary Shareholders Meeting held on July 4, 2000) the par value of Shares was 1 per share, and that in 2003, after the Merger, the par value of Shares and Savings Shares was reduced to 0.55 per share. In addition, in accordance with U.S. GAAP, net income (loss) per Savings Share Basic was 0.21 in 2003.

(7) Stockholders equity under U.S. GAAP is calculated after elimination of minority interest. See Note 27 of Notes to Consolidated Financial Statements included elsewhere herein.

(8) Gross Operating Profit was 12,131 million, 13,117 million, 12,216 million, 13,655 million, 14,015 million and 14,280 million in each of 1999, 2000 (historical), 2000 (pro forma), 2001, 2002 and 2003, respectively. Gross Operating Profit was 3,308 million and 3,494 million in the three months ended March 31, 2003 and 2004, respectively. Because Gross Operating Profit includes certain financial statement items and excludes others it is considered a non-GAAP financial measure as defined in Item 10 of Regulation S-K under the 1934 Act. Telecom Italia believes that Gross Operating Profit provides the best indication of the Telecom Italia Group s operating performance and is meaningful information for investors and is consistent with how we present ourselves to the analyst community. In addition the Telecom Italia Group also believes (although other telecommunication operators will calculate such information differently) that Gross Operating Profit permits an adequate comparison of the Telecom Italia Group s performance against its peer group. The following table reconciles operating income to the calculation of Gross Operating Profit by showing the Statement of Operation items included in calculating Gross Operating Profit.

	Year ended December 31,						Three months ended March 31,	
	1999	2000	2000 pro forma (Unaudited)	2001	2002	2003	2003	2004
	(millions of Euro)						(Unaudited)	
Operating income	5,319	5,444	5,079	5,125	6,058	6,789	1,527	1,788
Depreciation and Amortization	6,013	6,946	6,509	7,612	7,227	6,779	1,653	1,590
Other external charges: (*)								
• Provision for bad debts	416	495	412	448	546	471	75	51
• Write-downs of fixed assets and intangibles	88	48	48	17	58	6		1
• Provision for risk	263	154	143	389	114	70	32	12
• Other provisions and operating charges	522	417	388	431	466	485	83	106
Other income (excluding operating grants, reimbursements for personnel costs and costs of external services rendered)	(490)	(387)	(363)	(367)	(454)	(320)	(62)	(54)
Gross Operating Profit	**12,131**	**13,117**	**12,216**	**13,655**	**14,015**	**14,280**	**3,308**	**3,494**

(*) The following items included as part of Other external charges are added back to operating income in the calculation of gross operating profit.

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(9) Net financial debt is a non-GAAP financial measure as defined in Item 10 of Regulation S-K under the 1934 Act. Although net financial debt is a non-GAAP measure, it is widely used in Italy by financial institutions to assess liquidity and the adequacy of a company s financial structure. Therefore, we believe it is useful information for investors to receive and also is consistent with how we present ourselves to the analyst community. Net financial debt is calculated as follows:

	As of December 31,						As of March 31,
			2000 pro forma (Unaudited)				
	1999	2000		2001	2002	2003	2004
			(millions of Euro)				(Unaudited)
Short-term debt, including current portion of long-term debt	6,000	16,927	16,536	9,072	6,827	10,613	6,863
Long-term debt	24,291	27,485	25,950	37,747	33,804	30,852	33,071
Gross debt	30,291	44,412	42,486	46,819	40,631	41,465	39,934
Cash and cash equivalents:							
• Bank and postal accounts	(1,149)	(2,763)	(2,745)	(3,626)	(4,363)	(4,870)	(7,514)
• Cash and valuables on hand	(13)	(8)	(7)	(76)	(7)	(7)	(6)
• Receivables for securities held under reverse repurchase agreements	(133)	(1)	(1)	(4)	(56)	(60)	(12)
Marketable securities(*)	(1,749)	(2,909)	(2,759)	(3,616)	(1,927)	(2,719)	(1,456)
Financial accounts receivable (included under Receivables and Other current assets)	(232)	(1,210)	(1,210)	(894)	(995)	(826)	(446)
Financial prepaid expense/deferred income, net and accrued financial income/expense, net (long-term)		(328)	(328)	(705)	(511)	(307)	(265)
Financial prepaid expense/deferred income, net and accrued financial income/expense, net (short-term)	364	331	292	464	627	670	551
Net Financial Debt	**27,379**	**37,524**	**35,728**	**38,362**	**33,399**	**33,346**	**30,786**

(*) In 1999, 2000, 2001 and 2002 data include Old Telecom Italia shares held by Olivetti.

(10) For purposes of calculating the ratio of earnings to fixed charges :

- earnings is calculated by adding:
  - pre-tax income from continuing operations before adjustment for minority interests in consolidated subsidiaries;
  - fixed charges (as defined below);
  - amortization of capitalized interest and issue debt discounts or premiums;
  - dividends from equity investees; and
  - equity in losses of equity investees;

and then subtracting:

  - capitalized interest for the applicable period; and
  - equity in earnings of equity investees.
- fixed charges is calculated by adding:
  - interest costs (both expensed and capitalized);
  - issue costs and any original issue debt discounts or premiums; and
  - an estimate of the interest within rental expense for operating leases.

The term equity investees means investments that Telecom Italia accounts for using the equity method of accounting.

A ratio of less than one indicates that earnings are inadequate to cover fixed charges. The amount by which fixed charges exceeded earnings for the years ended December 31, 2001 and 2002 under Italian GAAP was 1,172 million and 2,037 million, respectively. The amount by which fixed charges exceeded earnings for the year ended December 31, 2001 under U.S. GAAP was 931 million.

(11) Data include multiple lines for ISDN and exclude internal lines.
(12) Data exclude internal lines.
(13) Number of contracts. Broadband access contracts in Italy as of December 31, 2001, 2002 and 2003 were 390,000, 850,000 and 2,040,000, respectively, while as of March 31, 2003 and 2004 were 1,100,000 and 2,575,000, respectively.
(14) Number of contracts; data include Teleconomy, Hellò and other Business voice offers.
(15) Data refer to TACS and GSM services lines, including holders of Prepaid Cards.
(16) The foreign lines include those of mobile telecom affiliates in Turkey and the Czech Republic.

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Dividends

The determination of Telecom Italia s future dividend policy, and the amounts thereof, will depend upon a number of factors, including but not limited to the Company s earnings, financial condition and cash requirements, prospects and such other factors as may be deemed relevant at the time. Subject to the foregoing, Telecom Italia plans to maintain its dividend over the life of the 2004-2006 Industrial Plan at a level comparable to that paid out for 2003.

Dividends declared by Old Telecom Italia. The following table sets forth the dividends per share and per savings share declared by Old Telecom Italia with respect to the last four fiscal years ended December 31, 1999, 2000, 2001 and 2002, respectively, and the aggregate dividend paid in such years. Actual dividends paid are rounded to the nearest whole cent.

	Dividends on Shares			Dividends on Savings Shares		
Year ended December 31,	**Euros per Share**	**U.S. dollars per Share(2)**	**(millions of euros)**	**Euros per Share**	**U.S. dollars per Share(2)**	**(millions of euros)**
1999(1)	0.3099(3)	0.29	1,638.10	0.3218(3)	0.30	688.58
2000(1)	0.3125	0.27	1,643.93	0.3238	0.28	664.84
2001	0.3125(4)	0.28	1,644.19	0.3237(4)	0.29	662.33
2002	0.1357(5)	0.13	713.47	0.1357(5)	0.13	273.11

(1) Dividends for 1999 and 2000 were paid in lire. The lire amounts were translated into euros at the irrevocably-fixed rate of exchange of Lit. 1,936.27 = 1.

(2) Euro amounts have been translated into U.S. dollars using the Noon Buying Rate in effect on the respective payment dates.

(3) The per share amount paid with respect to the fiscal year ended December 31, 1999 includes the distribution to all shareholders of Old Telecom Italia of the dividends payable on 26,046,820 savings shares held in treasury on the date the dividend was paid. A total of approximately 3.12 million was also distributed from the statutory reserve in order to round up such per share amounts.

(4) Approved at the Annual Meeting of Shareholders of Old Telecom Italia held on May 7, 2002. Old Telecom Italia s dividend coupons for the year ended December 31, 2001 were clipped on May 20, 2002 and were payable from May 23, 2002. Dividends for the year ended December 31, 2001 were paid also utilizing reserves.

(5) In order to ensure shareholders dividends commensurate with those paid out for 2001, in December 2002, reserves were distributed and paid corresponding to a dividend of 0.1357 per Old Telecom Italia ordinary share and a dividend of 0.1357 per Old Telecom Italia savings share. Furthermore, the shareholders Meeting of Old Telecom Italia held on May 24, 2003 approved an additional dividend of 0.1768 per Old Telecom Italia ordinary share and 0.1878 per Old Telecom Italia savings share, payable from income and capital reserves.

Dividends declared by Telecom Italia (formerly Olivetti). The following table sets forth the dividends per share, per savings share and per preferred share declared by Telecom Italia (Olivetti prior to the Merger) with respect to each of the last five fiscal years and the aggregate dividend paid in such years. Actual dividends paid are rounded to the nearest whole cent.

	Dividends on Shares			Dividends on Savings Shares			Dividends on Preferred Shares		
Year ended December 31,	**Euros per Share**	**U.S. dollars per Share(2)**	**(millions of euros)**	**Euros per Share**	**U.S. dollars per Share(2)**	**(millions of euros)**	**Euros per Share**	**U.S. dollars per Share(2)**	**(millions of euros)**
1999(1)	0.0310	0.0289	148.92	0.1937	0.1807	15.23	0.0362	0.0338	0.55

2000(1)(3)	0.0350	0.0299	254.87			
2001	0	0	0			
2002	0	0	0			
2003(4)	0.1041	0.1278	1,072.95	0.1151	0.1413	667.11

(1) Dividends for 1999 and 2000 were paid in lire. The lire amounts were translated into euros at the irrevocably-fixed rate of exchange of Lit.1,936.27 = 1.

(2) Euro amounts have been translated into U.S. dollars using the Noon Buying Rate in effect on the respective payment dates.

(3) On July 24, 2000, the compulsory conversion of the Olivetti savings and preferred shares into Olivetti ordinary shares (approved by the Extraordinary Shareholders Meeting held on July 6, 2000) became effective.

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(4) Approved at the Annual Shareholders Meeting held on May 6, 2004. Pursuant to Italian Stock Exchange rules, dividends on the Shares and the Savings Shares are payable from the fourth business day after the third Friday of each month, and in any case, at least four business days after the Annual Meeting of Shareholders approving the dividends. Telecom Italia s dividend coupons for the year ended December 31, 2003 were clipped on May 24, 2004, and were payable from May 27, 2004.

Payment of annual dividends is subject to approval by the holders of ordinary shares at the annual general shareholders meeting, which must be convened within 120 days after the end of the financial year to which it relates or, in case specific reasons arise, within 180 days, the reasons for the delay to be described in the annual report. In addition, Article 21 of the Company s Bylaws gives the Board of Directors the power to approve the distribution of interim dividends . Pursuant to Italian law, the distribution may be approved after the final approval of the preceding year s financial statements, and the interim dividends may not exceed the lower of (i) the difference between profits from the preceding fiscal year and amounts required to be attributed to legal and statutory reserves and (ii) available reserves. Once paid in compliance with applicable laws, shareholders cannot be required to repay interim dividends to the Company if the shareholders collected such dividends in good faith. Dividends not collected within five years from the date they become payable will be forfeited in favor of the Company. If profits are not fully distributed, additional reserves are created.

According to the Italian Civil Code, before dividends may be paid with respect to any year, an amount equal to 5% of the net income of the Company for such year must be set aside to the legal reserve until the legal reserve, including amounts set aside during prior years, is at least equal to one-fifth of the par value of the Company s issued share capital. This legal reserve is not available for payment of dividends. Such restriction on the payment of dividends applies, on a non-consolidated basis, to each Italian subsidiary of the Telecom Italia Group. The Company may also pay dividends out of available retained earnings from prior years or other reserves.

Dividends in respect of Shares and Saving Shares held with Monte Titoli S.p.A (Monte Titoli) are automatically credited to the accounts of the beneficial owners with the relevant participant of Monte Titoli, without the need for presentation by such beneficial owners of any documentation. See Item 10. Additional Information Description of Bylaws and Description of Capital Stock .

Arrangements between Euroclear or Clearstream and Monte Titoli permit the shareholders to collect the dividends through Euroclear or Clearstream. Holders of American Depositary Receipts (ADRs) are entitled to receive payments in respect of dividends on the underlying Shares and Savings Shares, as the case may be, in accordance with the relevant Deposit Agreement.

Dividends payable on the Company s Shares and Savings Shares may be subject to deduction of Italian withholding tax. See Item 10. Additional Information Taxation . Italian regulations do not contain any specific restrictions on the payment of dividends to non-residents of Italy. See Item 10. Additional Information Exchange Controls and Other Limitations Affecting Security Holders .

Pursuant to Italian law, in connection with the payment of dividends, participants of Monte Titoli are required to supply to the Italian tax authorities certain information concerning the identity of non-resident shareholders holding Shares or Savings Shares. Shareholders are required to provide their Italian tax identification number, if any, or alternatively, in the case of legal entities, their name, country of establishment and address, or in the case of individuals, their name, address and place and date of birth, or in the case of partnerships, the information required for legal entities and the information required for individuals with respect to one of their representatives.

In the case of Ordinary Share ADSs and Savings Share ADSs owned by non-residents of Italy, Telecom Italia understands that the provision of information concerning the Depositary, in its capacity as holder of record of the Shares and Savings Shares, as the case may be, will satisfy these requirements. However, Telecom Italia will be required to provide information concerning non-resident beneficial owners of Ordinary Share ADSs and Savings Share ADSs, to the extent such owners wish to benefit from reduced withholding tax rates on dividends under an income tax convention, and claims for such benefits therefore must be accompanied by the required information. See Item 10. Additional Information Taxation .

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Item 4. INFORMATION ON THE TELECOM ITALIA GROUP

BUSINESS

Background

The legal and commercial name of the company is Telecom Italia S.p.A. The company is incorporated as a joint stock company under the laws of Italy. The duration of the company extends until December 31, 2100. The registered office and principal executive offices of Telecom Italia are at Piazza degli Affari 2, 20123 Milan, Italy. The telephone number is +39-02-85951.

On July 18, 1997, Old Telecom Italia s predecessor company was merged with and into STET Società Finanziaria Telefonica per Azioni (STET), its parent holding company, with STET as the surviving corporation. As of the effective date of the merger, STET changed its name to Telecom Italia S.p.A . In November 1997, the Ministry of the Treasury of the Republic of Italy completed the privatization of Telecom Italia selling substantially all of its stake in the Old Telecom Italia Group through a global offering, and a private sale to a stable group of shareholders.

On May 21, 1999, Olivetti, through a tender offer, obtained control of the Old Telecom Italia Group when approximately 52.12% of Old Telecom Italia ordinary shares were tendered to Olivetti. Through a series of transactions which started in July 2001, Olimpia S.p.A. (Olimpia) acquired a 28.7% stake in Olivetti which resulted in the replacement of the then boards of directors of Olivetti and Old Telecom Italia. Please see Item 7. Major Shareholders and Related-Party Transactions Major Shareholders The Olimpia Shareholders Agreements .

On December 9, 2002, the Ministry of the Treasury sold its remaining stake in Old Telecom Italia ordinary and savings share capital.

On August 4, 2003, Old Telecom Italia merged with and into Olivetti (the Merger) with Olivetti as the surviving company changing its name to Telecom Italia S.p.A . Please see Merger with Olivetti . Following the Merger, the proportionate ownership of Telecom Italia s share capital by shareholders unaffiliated with Pirelli S.p.A. (Pirelli), Olimpia s largest shareholder or Olimpia, increased substantially to approximately 88.43% of the outstanding Ordinary Shares. Since that date Olimpia has acquired additional shares through market purchases and Olimpia is currently the largest shareholder of Telecom Italia with approximately a 17% holding of Telecom Italia s Shares.

The share capital of Olimpia is presently held by Pirelli, Edizione Finance International S.A. (hereinafter Edizione), UniCredito Italiano S.p.A. (Unicredito), Banca Intesa S.p.A. (hereinafter Intesa) and Hopa S.p.A. (Hopa) in the following respective proportions: 50.4%, 16.8%, 8.4%, 8.4% and 16%. For a discussion of the relationships between Olimpia s shareholders relating to the Telecom Italia Group, please see Item 7. Major Shareholders and Related-Party Transactions Major Shareholders The Olimpia Shareholders Agreements .

In January 2004, Hopa announced it had acquired a further 3.367% of Telecom Italia s Shares, held, in part, directly (slightly over 0.1%, corresponding to 13,203,484 ordinary shares) and the remaining part through Holinvest S.p.A. (Holinvest), a company owned by Hopa (80.001%) and Olimpia (19.999%).

On April 6, 2004, Pirelli, pursuant to a call option agreement entered into with JPMorgan in November 2001, exercised its right to buy 47,155,300 Shares at an exercise price per share of 2.12. On April 15, 2004, Holinvest exchanged with JPMorgan Ltd. 95,606,875 of Telecom Italia s convertible bonds for 46,343,969 Shares. After giving effect to the acquisition of the 47,155,300 Shares, Pirelli may be deemed to beneficially own 1,798,921,123 Telecom Italia Shares (including the 1,751,765,823 Telecom Italia Shares beneficially owned by Olympia), representing approximately 17.46% of the total number of Shares reported to be issued and outstanding.

A glossary of selected telecommunications terms used in the following description of the Telecom Italia Group s business and elsewhere in this Annual Report can be found at the end of Item 4 of this Annual Report.

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General

At the end of 2003, the Telecom Italia Group was one of the world s largest fixed telecommunications operators, with approximately 26.6 million subscriber fixed-lines installed (including ISDN) equivalent lines. Through our subsidiary TIM, we were also the largest mobile telecommunications operator in Italy and one of the largest in the world, with more than 44.5 million mobile lines which includes 26.1 million lines in Italy and more than 18.4 million outside Italy through controlled and associated companies of TIM (35.6 million lines in which we have an economic interest or proportionate lines). At December 31, 2003, we also had 6.6 million mobile lines (2.2 million proportionate lines) through companies indirectly owned through Telecom Italia International. In Italy TIM is one of three operators with the right to provide GSM digital mobile telecommunications services and one of three operators with the right to provide DCS 1800 digital mobile telecommunications services (the fourth operator, Blu, was acquired in October 2002 and merged into TIM in December 2002). TIM is one of five entities which have acquired a UMTS license to provide third generation mobile services in Italy.

The Telecom Italia Group also provides leased lines and data communications services, internet services including broadband, and IT software and services. We also operate in the office products, IT office products and specialized applications for service automation in banking retail, gaming and public authorities services and specialized automation systems sector through Olivetti Tecnost.

Our international portfolio of subsidiaries and investments includes fixed and mobile telecommunications companies which operate mainly in Latin America and certain countries in Europe.

Significant Developments during 2003

Merger with Olivetti

Olivetti was established in Ivrea (Turin) in 1908 as a typewriter manufacturer. Over time, Olivetti shifted the focus of its core business from mechanical office products to electronic equipment, computers, IT systems and services and during the 1990s, to telecommunications. In May 1999, Olivetti and its subsidiary Tecnost S.p.A. (Tecnost) successfully made a joint tender offer for Old Telecom Italia which ultimately resulted in Olivetti obtaining a 54.94% controlling interest in Old Telecom Italia s ordinary shares. The acquisition of Old Telecom Italia marked a major development in the transformation of Olivetti s core businesses.

In May 2003, the shareholders of Olivetti and of Old Telecom Italia approved the Merger of Old Telecom Italia with and into Olivetti with Olivetti as the surviving company. The Merger was part of a strategic plan pursued by Olivetti, as majority owner of Old Telecom Italia, with the aim of focusing on core businesses, improving its corporate structure and reducing debt. Prior to the Merger and the cash tender offers described below, Olivetti had a 54.94% controlling interest in Old Telecom Italia which was Olivetti s largest subsidiary (representing approximately 96.8% of its operating revenues in 2002). The Merger became effective on August 4, 2003, at which time Olivetti, as the surviving company, changed its name to Telecom Italia S.p.A. , succeeded to the 1934 Act registration of Old Telecom Italia and became subject to the foreign private issuer reporting requirements of the 1934 Act. Telecom Italia completed the listing of its Ordinary Share ADSs and Savings Share ADSs on the New York Stock Exchange concurrently with the completion of the Merger. Telecom Italia s Shares and Savings Shares are also listed on the automated screen-based trading system (Mercato Telematico Azionario) of Borsa Italiana.

In connection with the Merger, the following transactions occurred:

- Olivetti shareholders who either voted against the Merger or did not attend the shareholders meeting held on May 26, 2003, benefited from a withdrawal right of 0.9984 per share (which was the arithmetic mean of the daily official share price of the Olivetti shares in the six months preceding the date the Merger resolution was adopted; such date was May 26, 2003). Olivetti shareholders were entitled to such a right by law due to the change in the corporate objectives of Olivetti which, following the completion of the Merger, changed its name to Telecom Italia S.p.A. . Olivetti shareholders exercised such right with respect to 10,958,057 shares representing 0.12% of the outstanding ordinary shares. Olivetti shareholders received an aggregate payment of 10,940,524 when the Merger became effective.

- Voluntary cash tender offers by Olivetti for a portion of the outstanding Old Telecom Italia ordinary shares and savings shares were made in connection with the Merger (although the cash tender offers were not made to savings shareholders in the United States). Olivetti tendered for 908,873,776 (17.3%) of Old Telecom Italia ordinary shares (including those represented by ADSs) and 354,560,274 (17.3%)

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of the Old Telecom Italia savings shares. Olivetti acquired approximately 9.73% and 11.83% of the Old Telecom Italia ordinary shares and savings shares, respectively, through the cash tender offers. Aggregate consideration paid after the Merger became effective was 5,274 million.

In connection with financing the withdrawal right and the cash tender offers, Olivetti entered into a Term Loan Facility with a syndicate of banks pursuant to which it borrowed 5,274 million with respect to the above transactions. Olivetti also entered into a 6.5 billion Revolving Credit Facility to provide funds for working capital and general corporate purposes which replaced Old Telecom Italia s 7.5 billion facility which was cancelled.

As a result of, and immediately after, the Merger, the proportionate ownership of Telecom Italia s ordinary share capital by shareholders unaffiliated with Olimpia or its principal shareholder Pirelli increased substantially from 45.06% to 88.43% of Telecom Italia s outstanding Ordinary Shares. Olimpia owned 11.57% of Telecom Italia s ordinary share capital immediately following the Merger. On October 15, 2003, Olimpia announced that it had acquired an additional 266.3 million Ordinary Shares of Telecom Italia representing approximately 2.6% of Telecom Italia s ordinary share capital. After such acquisition, Olimpia held approximately 14.16% of Telecom Italia s ordinary share capital. The Olimpia Shareholders Meeting, held on November 13, 2003, approved a capital increase of up to 770 million, most of which (approximately 700 million) has been used to purchase Telecom Italia Ordinary Shares. Consequently, on December 18, 2003, Olimpia s holding of Telecom Italia ordinary share capital increased to approximately 17%. Olimpia is Telecom Italia s largest shareholder.

SEAT Spin-off and Sale

On April 1, 2003, the Board of Directors of SEAT approved the proposed proportional spin-off of the directories and almost all of the directory assistance and business information business segments of SEAT into New SEAT, a newly incorporated company which assumed the current name of Seat Pagine Gialle S.p.A. .

Effective as of August 1, 2003, the date of the spin-off, the corporate name of the remaining part of SEAT became Telecom Italia Media S.p.A. . The spin-off plan was approved by a SEAT extraordinary shareholders meeting held on May 9, 2003.

The shares of both companies are listed on the automated screen-based trading system (Mercato Telematico Azionario) of Borsa Italiana. The spin-off created two independent companies, each focused on its core businesses. It was SEAT management s view that SEAT operated in two broad market sectors that had increasingly developed separate and distinct characteristics in terms of strategy, operations and competitive landscape.

The first sector targeted advertising and telephone services, in which SEAT operated through its directories, directory assistance and business information segments, providing answers to queries via printed, online and telephone products and services. The second sector was traditional advertising and the internet, in which SEAT operated through its internet, TV and other business segments, primarily providing access and content services. In SEAT management s view, both sectors presented interesting development prospects (including broadband access and digital TV).

The strategic objective of the spin-off was to allow SEAT s businesses in each of the two sectors to more rapidly respond to market developments and exploit market opportunities, with a more focused management and a resource allocation consistent with the development prospects of each business line.

The spin-off provided for the transfer to New SEAT of the following companies within the directories, directory assistance and business information business segments of SEAT:

- *Directories*: Directory Italia Seat Pagine Gialle S.p.A. division, Annuari Italiani S.p.A., Euredit S.A., TDL Group, Euro directory S.A..
- *Directories Assistance*: Directories Assistance Seat Pagine Gialle division, Telegate Group, Telegate Holding GmbH, IMR S.r.l..
- *Business Information*: Consodata S.A., Consodata Group Ltd (including Netcreations Inc., Pan Adress).

The other companies and business segments remained with Telecom Italia Media.

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Sale of Telecom Italia s stake in New SEAT

On June 10, 2003, Old Telecom Italia and a consortium of investors formed by BC Partners, CVC Capital Partners, Investitori Associati and Permira (Silver S.p.A.) entered into a sale and purchase agreement for the sale of approximately 61.5% of the share capital of New SEAT which, at the time of the agreement, the Telecom Italia Group was expected to receive after the spin-off transaction creating New SEAT, including the shares resulting from the exercise of the J.P. Morgan Chase put option for which Telecom Italia paid 2,272 million. The JPMorgan Chase put option relates to certain put/call arrangements entered into by Telecom Italia at the time of its original acquisition of SEAT. See Note 29 of Notes to Consolidated Financial Statements included elsewhere herein. The parties agreed on a sale price of 0.598 per New SEAT ordinary share, representing an enterprise value of approximately 5.65 billion and a price for Telecom Italia s stake of 3.033 billion. The sale was completed on August 8, 2003. Taking into account New SEAT s net financial indebtedness at the date of finalization of the sale (648 million), the transaction allowed Telecom Italia to reduce its net financial consolidated debt by 3,681 million.

The agreements relating to the sale of Telecom Italia s stake in New SEAT include Telecom Italia s undertaking to provide, on an ongoing basis, Telecom Italia Media with the funds necessary to service Telecom Italia Media s debt and other liabilities in existence as of the date of the SEAT spin-off. The undertaking provides for Telecom Italia Media to have funds sufficient to meet such liabilities and that New SEAT be indemnified from potential liabilities vis-à-vis any creditors of Telecom Italia Media deriving from New Seat s statutory joint liability for such obligations.

As a result of the sale, on July 31, 2003, Telecom Italia and Pagine Italia agreed not to execute the agreements reached in September 2002, regarding the purchase by Telecom Italia of the assets of the Pagine Utili directories. Telecom Italia agreed to pay 55 million to Pagine Italia in connection with the termination of such agreement.

Notes Issue

On October 10, 2003, as part of the plan to refinance short and long-term borrowings falling due, the Board of Directors of Telecom Italia authorized the establishment of a 10 billion Euro Medium Term Note Program (the Euro MTN Program). These notes will be issued, when market conditions permit, by Telecom Italia and/or its subsidiary Telecom Italia Finance, with a guarantee by Telecom Italia.

On the same date, the Board of Directors also approved the undertaking by Telecom Italia of a guarantee for the issue of notes to be placed with qualified institutional buyers principally in the United States of America pursuant to Rule 144A of the U.S. Securities Act of 1933, for a maximum amount of U.S.$4 billion. As a consequence of this resolution, on October 29, 2003, Telecom Italia Capital S.A. (a wholly-owned finance company of Telecom Italia) finalized the issue of fixed-rate multi-tranche notes in U.S.$, with a full and unconditional guarantee by Telecom Italia.

Such notes included:

- Series A notes in the principal amount of U.S.$1 billion, with an annual fixed rate coupon of 4%, issue price of 99.953%, maturing November 15, 2008;

- Series B notes in the principal amount of U.S.$2 billion, with an annual fixed rate coupon of 5.25%, issue price of 99.742%, maturing November 15, 2013;

- Series C notes in the principal amount of U.S.$1 billion, with an annual fixed rate coupon of 6.375%, issue price of 99.558%, maturing November 15, 2033.

On December 18, 2003, as part of the plan referred to above, the Board of Directors passed a resolution to issue notes under the Euro MTN Program during 2004 up to an aggregate amount of 5.1 billion.

Disposition and Acquisition of Significant Equity Investments in 2003

Dispositions

Sale of Telekom Srbija. On February 20, 2003, Telecom Italia International N.V. executed a Share Purchase Agreement, for the sale of its entire participation in Telekom Srbija, corresponding to 29% of the Telekom Srbija share capital for a total consideration of 195 million. The payment of the first tranche of 120 million was completed in June 2003 and the closing occurred on July 7, 2003. The shares will remain in an escrow account until full payment of the remaining 75 million, which constitutes the second tranche of the transaction, is made.

Dedalo project. In January 2003, the Telecom Italia Group completed the early purchase of 12 property units (approximately 300,000 square meters) from Teleleasing S.p.A. that are leased by Telecom Italia S.p.A. and other Telecom Italia Group companies. The transaction involved a total financial payment of approximately 369 million by the entire Telecom Italia Group.

Following a binding offer by Beny Steinmetz Group through its subsidiary Five Mounts Property (FMP), on June 20, 2003, Telecom Italia formalized an agreement with Lastra Holding B.V. (FMP Group) for the transfer of most of the early purchased property units, with a sale price of 355 million. At that time Telecom Italia delivered executed lease agreements on the same units to guarantee their utilization.

On June 30, 2003, the property units were transferred into a vehicle company, FMP Italy 1 s.r.l. , 100% owned by Telecom Italia (FMP Italy). On July 21, 2003, the entire FMP Italy stake was transferred from Telecom Italia to Lastra Holding B.V. for 45,000. On the same date, Telecom Italia, TIM and Atesia received the purchase price for the property units from FMP Italy.

Acquisitions

Acquisition of Consodata shares. On February 12, 2003, Seat Pagine Gialle acquired 1,108,695 ordinary shares in the French subsidiary Consodata S.A. listed on the Paris Nouveau Marché stock exchange after the founding shareholders exercised their option to sell, which was granted to them under an agreement made with previous Seat Pagine Gialle management on July 31, 2000. This transaction, undertaken at an agreed consideration of 44 per share for a total of approximately 48.8 million resulted in Seat Pagine Gialle acquiring a further 8.17% of the company share capital and voting rights, thereby raising its stake in Consodata S.A. to 98.60%. Consodata was among the companies included in the business information business segment of SEAT which was spun-off and later sold.

Acquisition of HanseNet. In September 2003, the acquisition from e.Biscom of 100% of HanseNet Telekommunikation GmbH (HanseNet), a broadband operator in the Hamburg area, was finalized by Telecom Italia for a total investment of 243 million. To this end, Telecom Italia had previously purchased the company Telecom Italia Deutschland GmbH which was used to purchase the entire investment in HanseNet.

Recent Developments during 2004

Sale of shares in Telekom Austria

On January 27, 2004, Telecom Italia International sold through a private placement agreement its remaining shares in Telekom Austria, representing 14.78% of Telekom Austria s total share capital. Gross proceeds were 780 million (approximately 770 million, net of commissions paid to banks) realizing a net gain at the consolidated level of 62 million.

Sale of shares in Euskaltel

On January 16, 2004, a contract was signed with Araba Gertu S.A. for the sale, by Telecom Italia International, of a 3.1% stake in Euskaltel, the regional operator for cable TV and applied telecommunications for Basque countries, for a total price of 13.6 million. The closing took place on February 19, 2004, after the deadline had passed for the exercise of pre-emption rights on the shares held by the other shareholders. The pre-emption right was exercised by the shareholder, Iberdrola and, accordingly, the sale of the shares held by Telecom Italia International occurred through the signing of two separate contracts (149,231 shares sold to Araba Gertu for a consideration of 12.1 million and 18,719 shares sold to Iberdrola for a consideration of 1.5 million). Upon completion of the transaction, Telecom Italia International retained a 3% stake in Euskaltel.

TIM s stake in Digitel

On April 19, 2004, TIM International agreed to settle several lawsuits between TIM International and all the other shareholders of Corporacion Digitel C.A. (Digitel). The lawsuits concerned the covering (which was performed in 2003) of losses for the fiscal year 2002. According to the terms of the settlement, TIM International agreed to acquire the shares held by all the other shareholders (corresponding to 32.88% of Digitel s share capital) for U.S.$110 million. As a consequence of the settlement, TIM International will have total control of the Venezuelan company. The effectiveness of the settlement is subject to certain conditions, the most important of which are: the waiver by all the other shareholders to any further request or lawsuit against TIM/Digitel, and the dismissal of the arbitration proceeding initiated in New York (under the International Chamber of Commerce s rules) between TIM International and Venconsul. The difference between the fair market value of the shares to be acquired and the acquisition price agreed to in the settlement has been covered by a reserve for risks and charges.

Decrease in share capital of Solpart Participaçoes (Solpart)

At the Extraordinary Shareholders Meeting of Solpart, the holding company of Brasil Telecom Partecipaçoes (Brasil Telecom), a provider primarily of fixed line telecommunications services in Rio Grande do Sul, Paraná, Santa Catarina, Mato Grosso do Sul, Mato Grosso, Rondônia, Acre, Goiás, Tocantins, Distrito Federal (Brasilia) of Brazil, held on April 26, 2004, a capital reduction was approved amounting in the aggregate to $Reais 173,350,000.00 of which (i) $Reais 41,898,263.09 is to be proportionally reimbursed to the shareholders in cash and (ii) the proportionally delivery to the shareholders of 3,474,342,842 ordinary shares and 3,491,253,373 preferred shares of its affiliate Brasil Telecom Participaçoes. The valuation of the capital reimbursement through the delivery of shares was made on the basis of the weighted average price at the fixing of Sao Paulo s Stock Exchange on April 23, 2004. The weighted average price was $Reais 17.65 based on the value of the trading lot (1,000 shares) for the ordinary shares, $Reais 19.52 for the same lot of preferred shares and $Reais 1,980,319.91 to cover previous period losses.

As a consequence of the events described under (i) and (ii) above, Telecom Italia International is entitled to receive $Reais 15,917,669.18 in cash, 1,319,945,886 ordinary shares and 1,326,370,406 preferred shares. The transaction will have no effect on the overall control of Brasil Telecom.

Agreement for the sale of GPP

On May 13, 2004, Telecom Italia Media reached an agreement with Wise Venture Sgr, the company that manages the Wisequity closed-end equity fund, in relation to the disposal of 100% of GPP S.p.A., the parent company of the publishing groups Quasar s.r.l., JCE S.p.A. and Faenza Editrice S.p.A..

The disposal of GPP S.p.A. represents yet another step in the process of rationalization of Telecom Italia Media s asset portfolio. Following this transaction, Telecom Italia Media exits the professional publishing sector, which is not considered synergic with its core business.

The disposal is based on the assessment of the overall enterprise value of GPP S.p.A. valued at 14.6 million. The sale will improve the Group s net financial standing by approximately 13.8 million. The transaction is expected to be completed within the first half of 2004.

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Overview of the Telecom Italia Group s Major Business Areas

The following is a chart of the Telecom Italia Group s business units as of December 31, 2003:

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The table below sets forth certain key data for each Business Unit.

		Wireline (1)(3)	Mobile	South America (4)	Internet and Media (5)	IT Market (3)	IT Group (3)	Olivetti Tecnost	Sub-total	Other activities and eliminations (3)(6)	Consolidated Total
		(millions of Euro, except number of employees)									
Gross operating revenues	2003	17,216	11,782	1,126	1,297	891	1,100	655	34,067	(3,217)	30,850
	2002(2)	17,047	10,867	1,409	1,991	1,039	996	914	34,263	(2,855)	31,408
	2001(2)	17,174	10,250	1,534	1,957	1,322	1,039	1,097	34,373	(2,357)	32,016
Gross operating profit (7)	2003	8,255	5,502	400	322	84	96	40	14,699	(419)	14,280
	2002(2)	7,951	5,039	450	593	114	98	59	14,304	(289)	14,015
	2 001(2)	7,730	4,760	527	444	181	198	27	13,867	(212)	13,655
Operating income	2003	4,969	3,786	137	63	58	(36)	2	8,979	(2,190)	6,789
	2002(2)	4,677	3,358	146	232	64	(40)	4	8,441	(2,383)	6,058
	2001(2)	4,338	3,136	187	31	133	51	(26)	7,850	(2,725)	5,125
Capital expenditures	2003	2,302	1,957	130	102	30	174	20	4,715	179	4,894
	2002(2)	2,475	1,715	216	81	39	149	35	4,710	191	4,901
	2001(2)	2,842	3,151	406	175	33	139	62	6,808	423	7,231
Number of employees at the year end	2003	50,766	18,888	5,049	2,029	4,827	4,107	2,395	88,061	5,126	93,187
	2002(2)	53,935	18,702	5,461	7,715	5,506	5,039	4,527	100,885	5,735	106,620
	2001(2)	58,112	16,721	5,746	9,264	7,454	5,127	4,896	107,320	8,700	116,020

(1) As of June 16, 2003, Domestic Wireline changed its name to Wireline.
(2) The data relating to 2002 and 2001 have been reclassified and presented consistent with the 2003 presentation.
(3) Starting from January 1, 2003, the Netikos group, the Webegg group, the TILab, Loquendo and Eustema are no longer consolidated by the IT Group Operating Activity. BBNed is no longer included in Other Activities. The TILab moved to Other activities and Loquendo and BBNed became part of Wireline, whereas the other companies moved to the IT Market Business Unit. The effects of such reclassifications were not material.
(4) The data refer to Entel Chile group, Entel Bolivia group, the company Telecom Italia America Latina and the business segment South America of Telecom Italia. See Item 5. Operating and Financial Review and Prospects Recent Developments Telecom Italia Group Results for the First Quarter Ended March 31, 2004, compared to March 31, 2003.
(5) New SEAT, the beneficiary company of the spin-off from Seat Pagine Gialle which took place on August 1, 2003, was sold on August 2003. As a result of this, the 2003 figures include the results of operations for the first seven months of New SEAT Group, as well as the

results of operations for the entire year of the remaining part of Seat Pagine Gialle that after the spin-off was renamed Telecom Italia Media.

(6) The data include the operations of the International Affairs Corporate Function, the TILab, the Old Business Unit Satellite Services (the Telespazio group) which was disposed of during the fourth quarter of 2002 and consolidated in the statement of operations only for the first nine months of 2002 the 9Telecom group sold in the third quarter of 2002 and for which only the statement of income data was consolidated for the first six months of 2002 as well as the financial companies, the centralized group services and the staff functions.

(7) See Item 3. Key Information Selected Financial and Statistical Information Note 8 .

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The following table sets forth, for the periods indicated, certain selected statistical data for the fixed-line, mobile and internet businesses.

	Year ended December 31,		
	2001	**2002**	**2003**
Subscription and Customers:			
Subscriber fixed-lines at period-end in Italy (thousands)(1)	27,353	27,142	26,596
Subscriber fixed-line growth per annum in Italy(%)	0.7	(0.8)	(2.0)
ISDN equivalent lines at period-end in Italy (thousands)(2)	5,403	5,756	6,027
Broadband Access in Italy and abroad (ADSL + XDSL) (thousands)(3)	390	850	2,200
Voice Offers in Italy (thousands)(4)	4,094	5,224	5,547
Network infrastructure in Italy:			
access network in copper (millions of km pair)	104.3	104.3	105.2
access network and transport in fiber optics (millions of km of fiber optics)	3.2	3.6	3.6
Network infrastructure abroad:			
european backbone (km of fiber optics)	36,600	36,600	39,500
TIM lines in Italy at period-end (thousands)	23,946	25,302	26,076
TIM group foreign lines (at period-end, thousands)(5)	10,923	13,809	18,438
TIM group lines total (Italy + foreign, thousands)(5)	34,869	39,111	44,514
TIM lines in Italy growth per annum(%)	10.9	5.7	3.1
Average revenue in Italy per mobile line per month( )(6)	29.1	28.8	29.1
Cellular penetration in Italy at period-end (TIM lines per 100 inhabitants)(%)	41.6	43.9	45.3
Cellular market penetration in Italy at period-end (lines for the entire market per 100 inhabitants)(%)	89.0	93.7	99.2
GSM penetration in Italy (% of population)	99.7	99.8	99.8
E-TACS penetration in Italy (% of population)	98.0	98.0	97.9
Retail Traffic(7):			
Average minutes of use per fixed-line subscriber in Italy during period(8)	4,739	4,292	4,127
Of which:			
Local traffic during period (in average minutes)(9)	3,575	3,198	2,971
Long-distance traffic during period (domestic and international) (in average minutes)	1,163	1,094	1,156
Total mobile outgoing traffic per month (millions of minutes)	1,795	1,960	2,090
Internet and Media:			
Page Views Virgilio (millions)	3,945	5,267	6,612

(1) Data include multiple lines for ISDN and exclude internal lines.
(2) Data exclude internal lines.
(3) Number of contracts. Broadband access contracts in Italy as of December 31, 2001, 2002 and 2003 were 390,000, 850,000 and 2,040,000, respectively.
(4) Number of contracts; includes Teleconomy, Hellò and other Business voice offers.
(5) The foreign lines include those of the mobile telecommunications affiliates in Turkey and the Czech Republic. Our proportionate share results in total lines of 35.6 million as of December 31, 2003.
(6) Including Prepaid Customers revenues and excluding equipment sales and including non TIM customer traffic.
(7) Retail traffic consists of traffic from Telecom Italia customers for local calls, long distance national and international calls (including calls to mobile phones).
(8) Includes total fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks).
(9) Including district and internet dial-up traffic.

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Updated Business Plan and Strategy

Updated Business Plan

On March 25, 2004, we announced our 2004-2006 Industrial Plan (the 2004-2006 Industrial Plan) and established our priorities. The main objectives are to:

- consolidate our leadership in the domestic wireline market by increasing customer loyalty through innovative offers and stimulating the market for value added and broadband contents and services, with special reference to ADSL technology. ADSL is a telecommunications technology that permits the transmission of data and allows access to the Internet at very high speeds;
- in the mobile market, increase traffic volumes and develop value added services in line with user expectations (MMS, or Mobile Multimedia Services, mobile TV, gaming, videostreaming, videotelephony) and leveraging on technology integration (GSM/EDGE/UMTS);
- in the Internet and Media sector, continue the development of broadband services and portals and strengthen our television channels (La7 and MTV Italia) and launch Digital Terrestrial TV services;
- expand our presence abroad in markets where we can capitalize on our marketing and technological know-how: in the mobile business, in Latin America and especially in Brazil and, in the wireline business, through the development of broadband services in Europe;
- continue to manage our operations according to rigorous criteria of efficiency, relying on synergies deriving from the organizational model based on so-called professional families and service centers, cost control systems (completing the cost efficiency target), and the careful selection of investment projects, aimed primarily at fostering innovation and sustainable growth;
- complete the cost efficiency targets of the 2002-2004 plan and further improve cost efficiency. At December 31, 2003, we had achieved 86% of the 2002-2004 announced target of cost reductions of 2.6 billion through the reduction of both operating expenses and capital expenditures; and
- strengthen our financial structure through strong cash generation.

The 2004-2006 Industrial Plan takes into account the changes in the scope of consolidation (including the sale of New SEAT) and is substantially a confirmation of the plans which have been implemented by Olivetti and Old Telecom Italia since 2002. In addition to debt reduction, the Old Telecom Italia Group sought to strengthen its competitive position in its core domestic market and sustain profitable growth through the introduction of new products and services in its main business areas over the past two years.

Wireline

In Wireline, over the past two years a principal focus has been on broadband and loyalty programs. At the end of 2003, the customer base of broadband accesses was 2,040,000 in the domestic market and 160,000 in the European market (France, Germany and the Netherlands). New services for broadband Internet (Alice and Smart) have supported continued growth. New voice packages and innovative integrated solutions for business clients were also introduced.

The Telecom Italia Group s wireline strategy continues to be driven by defense of market share in voice traffic, strong emphasis on data/internet growth and broadband contents and services development, and focus on obtaining continuing efficiencies and levels of capital expenditures.

In particular, we intend to:

- maintain our domestic leadership in our core business (voice services, internet access, data transmission services for businesses, national and international wholesale services);
- consolidate our operational capabilities with the objective of offering best in class service levels to our customers and leverage opportunities to retain our client base by enhancing customer loyalty (through billing, customer relations management (CRM) and customer contact);
- concentrate on developing value added services, both for corporate and residential customers, to sustain revenue and margin levels, building, in particular, on the increasing penetration of internet and broadband contents and services (including WiFi), but also on innovation in voice and videocommunication services and terminals, equipped with new facilities, similar to mobile phone functions;
- run efficient operations and continue our cost-cutting program (personnel, real estate, general and administrative, network);

- maintain competitive services and focus investment on enhancing network evolution and innovation such as optical transport and IP (Internet Protocol) services; and
- expand the wireline broadband offer in selected areas throughout Europe (such as Germany and France) with the creation of facility-based operators providing broadband access and value-added services by capitalizing on domestic expertise.

There can be no assurance that these objectives and targets will actually be achieved.

Mobile

Mobile, over the past two years, has developed new offerings of both voice and multimedia services (messaging, gaming and videostreaming), and voice portals together with the launch of specialized packages for business.

TIM s strategy is focused on maintaining its leadership and achieving sustainable growth in the wireless market by focusing on highly valuable customers, in particular through:

- continuous innovation in voice and Value Added Services (VAS) offers;
- strong customer care able to respond and anticipate customer needs;
- constant focus on technological innovation to match market expectations, exploiting the potential of the GPRS/EDGE/UMTS network integration; and
- further development of GSM services in Brazil and acquisition of leadership in the GSM Latin American market.

The main strategic tools for the achievement of such objectives are:

- innovative marketing, aimed at generating new and tailored offers to increase voice traffic and VAS utilization;
- a multichannel and integrated approach to caring and distribution, tailored for different customer needs/profile;
- a plug and play system to share resources and know-how via a centralized support of local networks in different countries;
- establishment of FreeMove , an alliance with leading wireless operators to launch new products and services, achieve efficiency through joint procurement of services and develop a Multinational Pan-European offer;

- excellence in human resources, through recruitment, development and retention of key human resources, analysis and selection of methods for increasing flexibility of resources and the management of internal innovation process; and

- profitability and cash flow generation, through maintenance of high efficiency levels on its network, IT and back-office, investments and working capital control.

There can be no assurance that these objectives and targets will actually be achieved.

Internet and Media

Internet & Media launched a new broadband portal and redesigned the programs list of La7 (the Internet and Media business unit television station).

International Actitivites

The 2004-2006 Industrial Plan also provides for the development of our international activities including the expansion of broadband services in Europe, leveraging of our presence and technological leadership in Brazil, increasing market share in high-end segments in Greece and consolidating our presence in Turkey.

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Capital Expenditures

Capital expenditures will be directed towards reinforcing our strategy with a focus on:

- innovation;
- continuing leadership in the domestic market;
- strengthening existing international assets; and
- development of value added services.

The industrial investments planned for the three years 2004-2006 will be approximately 15 billion, in line with the forecast for the three years 2003-2005. The breakdown by sector of activity is shown in the table below.

	Approximate % of Industrial Investments
Wireline	42%
Mobile	47%
Internet and Media	1%
Other	10%

Financial Targets

With respect to strengthening our financial structure, consolidated net financial debt (see Note 9 to Selected Financial and Statistical Information under Item 3. Key Information Selected Financial and Statistical Information which reconciles our net financial debt to our gross debt) of 33.3 billion as of December 31, 2003, meant that we had, post Merger, maintained the level of net financial indebtedness of Olivetti at December 31, 2002, despite the early exercise of the JP Morgan Chase put option associated with the SEAT demerger (2.3 billion) and the incurrence of 5.3 billion of indebtedness to finance the withdrawal right and cash tender offers associated with the Merger. We were able to maintain the level of net financial indebtedness by repayment of debt with significant free cash from our operations as well as net proceeds of approximately 3.8 billion from the disposition of assets. Although our net financial indebtedness has remained relatively constant year-on-year, this nonetheless represents a significant increase over the 18.1 billion of net financial indebtedness of the Old Telecom Italia Group at December 31, 2002. We have established a target of reducing our net financial indebtedness below 30 billion by the end of 2004.

Our 2004-2006 Industrial Plan also establishes certain financial targets. The financial targets (based on Italian GAAP) include:

	Objectives of Telecom Italia on a consolidated basis-CAGR(1)

	2004-2006
Operating revenues	>5%
Gross operating profit	>5.5%
Operating income	>10%
Net financial debt by Year End 2004 (in billions)	<30billion(2)

(1) Compound average growth rate. Assumes no change in scope of consolidation and excludes exchange rate impact.
(2) At December 31, 2004.

Please see Cautionary Statement for Purposes of the Safe Harbor Provisions of the United States Private Securities Litigation Reform Act of 1995 at the beginning of this Annual Report for a discussion of factors which could cause our actual results to differ materially from the targets discussed above. See, also, Item 3. Key Information Risk Factors . There can be no assurance that we will be able to achieve the financial targets we have established under our 2004-2006 Industrial Plan.

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The Organizational Structure

Telecom Italia Group s organizational structure includes:

- Corporate Functions, which are responsible for the Telecom Italia Group s operations; and
- Business Units, which are responsible for business development and managing operations for external markets.

The following diagram highlights the organizational structure of the Telecom Italia Group as of June 4, 2004.

(1) Consortium company which carries out Internal Auditing activities in the Telecom Italia Group.
(2) The International Legal Affairs function, previously under Corporate and Legal Affairs, has, since February 23, 2004, reported directly to the CEO Carlo Buora. It has responsibility for providing support to top management of the Telecom Italia Group with respect to legal issues concerning international operations and development of the business, together with Corporate and Legal Affairs which ensures the coordination on such issues at the Telecom Italia Group level.
(3) On March 1, 2004, the Latin America Operations function was disbanded. This function was set up in 2002 and reported to the head of the Mobile Business Unit for mobile telecommunications and to the CEO Carlo Buora for wireline telecommunications and was responsible for the global coordination of all the activities of the Group in Latin America. Telecom Italia Latam S.A. has now taken over the new role of the delocalized Corporate function in Latin America, consistent with the Telecom Italia Group s chosen strategy to consolidate and develop its international presence in the Latin America geographical area. The Business Units with their present corporate organizational structure are nevertheless responsible for the results of the subsidiaries in Latin America under their control.

On March 1, 2004, Paolo Dal Pino took over as representative of the Telecom Italia Group in Latin America, reporting directly to the Chairman, and a proposal will be put forth to appoint him as Chairman of Telecom Italia Latam.

Reorganization

The Telecom Italia Group continued to reorganize its operations during 2003. As a result, the following organizational changes took place:

- the Corporate Development and Investor Relations Function and the International Affairs Function, which now includes the Foreign Holdings Function, were created and report directly to the CEO Carlo Buora;

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- the International Wholesale Services function of the Wireline Business Unit was moved to TMI Italia S.p.A.; which changed its name to Telecom Italia Sparkle S.p.A.;

- the company Telecom Italia Lab S.p.A. was merged with and into Telecom Italia and operates the Research and Development Function for the Telecom Italia Group.

Starting in January 2004, the Telecom Italia Group Committees have been revised as follows:

- **Management Committee** which coordinates the Telecom Italia Group s activities and ensures coordination in the development and implementation of business strategies.

- **Investments Committee** which approves investments exceeding specific levels of approval.

- **Purchases Committee** which promotes coordination of the Telecom Italia Group s purchasing processes, monitoring their performance and maximizing synergies among the Business Units/Companies.

- **Business Reviews** which control the results of each Business Unit, analyze forecasts and operational progress reports and decide on the resulting action plans.

- **Publishing Committee** which establishes strategic guidelines relating to the publishing lines of reference for the Telecom Italia Group. Reporting to the Publishing Committee is the Operating Content Acquisition Committee which purpose is to ensure a whole vision of the initiatives developed by the Business Units, to leverage the contents of the Telecom Italia Group s offerings and packages and to define a synergic approach with suppliers.

- **Technological Committee** which coordinates the innovation and technological development processes.

- **IT Security Committee** which ensures coordination in the management of the information and computer security of the Telecom Italia Group.

- **Latin America Purchases Committee** which promotes coordination of the purchasing processes in Latin America, monitoring their performance and maximizing synergies among the operating companies.

- **Latin America Image Awareness and Advertising Committee** which is responsible for the uniformity of advertising and image awareness initiatives of the Telecom Italia Group in Latin America.

- **Latin America Regional Coordination Committee** which is responsible for the overall consistency of the Telecom Italia Group s activities in Latin America, ensuring coordination in the development and implementation of business strategies.

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BUSINESS UNITS

Wireline

The Wireline Business Unit operates on a national level as the consolidated market leader in wireline telephone and data services and call centers, for final retail customers and wholesale providers. On an international level, Wireline develops fiber optic networks for wholesale customers, mainly in Europe and South America. Aggressive competition in the Italian domestic market continued during 2003. Competition was particularly significant for national traffic and Wireline countered with new rate plans offered as part of the action to win back and retain customers.

The Wireline Business Unit accounted for gross operating revenues of 17,216 million in 2003, 17,047 million in 2002 and 17,174 million in 2001. The 2003 results of operations reversed last years trend with positive growth of about 1% in gross operating revenues which is one of the most important goals of the Wireline Business Unit s strategy.

The organizational structure of the Wireline Business Unit as of December 31, 2003 was as follows:

Telecom Italia Wireline	National Subsidiaries	International Subsidiaries
Wireline TLC services:	Atesia S.p.A.	Latin American Nautilus Group
	Path.Net S.p.A.	Mediterranean Nautilus Group
• Retail Telephone	Loquendo S.p.A.	Med-1 group
• Internet	Telecontact Center S.p.A.	Telecom Italia Deutschland holding GmbH
• Data Business		HanseNet Telekommunikation GmbH
• Telephone and Data VAS		BBNED Group
• National Wholesale		
	Telecom Italia Sparkle Group	
	• Telecom Italia Sparkle S.p.A.	
	• Pan European Backbone	
	• Telecom Italia of North America Inc.	
	• Intelcom San Marino S.p.A.	

Key Issues in Italy

- The Wireline Business Unit is focused on switching its customers from traditional to innovative technologies to enlarge IP services and applications. The Wireline Business Unit intends to expand its large penetration in the broadband market through ADSL connections offered respectively to the consumer and SOHO (Small Office Home Office) markets with two different branded packages: Alice and Smart .

- This strategy has had significant success in Italy with 2,040,000 broadband points of access sold to the retail and the wholesale market at the end of 2003 (850,000 at December 31, 2002), of which 1,504,000 points of access have been sold to retail customers. The growth is attributable to the success of various tariff structures geared to the mass market (Alice) and to business customers (Smart).

- The Wireline Business Unit is seeking to grow revenues by developing offers for Alice customers through a specialized portal with a growing number of services. During 2003 many new offers were successfully launched on the market, such as ADSL Sat offers to support internet connections through satellite for areas not covered by ADSL connections.

The Wireline Business Unit plans to develop new services, improving innovative use of its fixed network (such as video communications and SMS (Short Message Service) for fixed phones) through penetration with Telecom Italia s new fixed telephone, *Aladino*, with functions and design very close to a mobile last generation phone.

- Another key issue for Wireline is the expansion of its Wi-Fi service which provides the opportunity for customers to work everywhere with their own lap top, keeping in touch with the network (the company intranet, internet and their own private e-mail) with a high speed connection and without the need to connect to a fixed line.

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The service is now available with different formulas (flat and pay per use) in more than 159 hot spots, so called areas where there is an access point with Wi-Fi coverage available.

- In the voice area the key issue is to continue developing voice offers (Teleconomy, Hellò and other business customized offers) to support loyalty and retention and win back customers which have moved to other service providers.

Subscribers in Italy. The table below sets forth, for the periods indicated, certain domestic subscriber data of Wireline.

	As of December 31,				
	1999	2000	2001	2002	2003
Subscriber fixed-lines at period-end in Italy (thousands)(1)	26,502	27,153	27,353	27,142	26,596
Subscriber fixed-line growth per annum in Italy (%)(2)	2.0	2.5	0.7	(0.8)	(2.0)
ISDN equivalent lines at period-end in Italy (thousands)(3)	3,049	4,584	5,403	5,756	6,027
Broadband Access in Italy (ADSL + XDSL) (thousands)(4)			390	850	2,040
Voice Offers in Italy (thousands)(5)			4,094	5,224	5,547

(1) Data include multiple lines for ISDN and exclude internal lines.
(2) For each of the years ended December 31, the percentage growth figure represents growth per annum over the prior year s end.
(3) Excluding internal lines.
(4) Number of contracts.
(5) Numbers of contracts; data include Teleconomy, Hellò and other business voice offers.

As of December 31, 2003, the Wireline Business Unit had approximately 26.6 million fixed subscriber lines, including approximately 18.3 million residential lines (including multiple lines for ISDN), approximately 8.1 million business lines (including multiple lines for ISDN), and approximately 235,000 public telephones lines (including ISDN equivalent lines). As of December 31, 2003, Italy had 47 subscriber lines per 100 inhabitants.

As of December 31, 2003, the Wireline Business Unit had approximately 6.0 million ISDN equivalent lines. The number of subscribers is expected to continue increasing although marketing focus is on ADSL lines which provide greater speed on the Internet. This is evidenced by significant growth in broadband access.

As of December 31, 2003, 59.3% of the public telephones in service were equipped with phone card readers. The density of public telephones in Italy is among the highest in the world, with one public telephone per square kilometer and approximately 4.1 public telephones for every 1,000 inhabitants. During 2003, ISDN technology was introduced to approximately 54.5% of public telephones in order to support the launch of innovative services (approximately 128,000 basic ISDN equivalent lines in public telephony architecture; unlike residential and business ISDN lines, each ISDN public telephone line is linked to only one phone).

Wireline Strategic Business Areas

Retail Telephone

Retail Telephone services consist mainly of services offered using traditional technology (PSTN and ISDN). Main retail telephone services include: access to the network, traffic (in terms of minutes of retail traffic and tariff packages), equipment rental and assurance.

Revenues in the retail telephone segment consist mainly of traffic revenues and fee revenues. Traffic revenues are generated from minutes of traffic carried on the network (volumes), tariffs and fees for tariff packages. Fees include access fees such as basic monthly subscription charges, fees for additional services and for equipment rental and assurance.

Revenues from retail telephone (the Wireline segment addressing the retail and mass market) were 10,368 million in 2003, a decrease of 1.7% compared to 2002 (10,547 million in 2002). The Wireline Business Unit successfully limited the intense competitive impact in the retail segment during 2003. Traffic packages (voice offers), loyalty and retention schemes and win-back strategies resulted in limited revenue losses while market share on traffic volumes was stable.

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Retail Internet

Retail Internet services consist mainly of ADSL services (connections, traffic, services, equipment and portals) and traditional internet traffic (such as dial-up), which is declining as ADSL is growing.

Retail Internet revenues consist primarily of internet dial-up traffic revenues and revenues from access fees for ADSL connections.

During 2003, the Wireline Business Unit focused its efforts on growing its ADSL mass market base and attracting new customers by building an internet portal for Alice customers with a growing offer of services, including, among others videos, pictures and music.

Revenues grew significantly in 2003, to 709 million, an increase of 19.2% over 2002 (595 million in 2002). Revenues from ADSL were approximately 257 million increasing strongly by 190% over 2002 (89 million in 2002) although revenues from internet dial-up traffic decreased due to migration to internet connections from broadband access.

Data Business

Data Services. Data services consist primarily of data transmission and network services for business customers. Revenues from data services are included primarily in fixed subscription and connection fees.

The Wireline Business Unit provides a broad range of data transmission and web application services supported by a wide spectrum of technological platforms ranging from traditional to advanced platforms based on broadband access (Synchronous Digital Hierarchy or SDH, the European standard for high speed digital transmission and XDSL).

During 2003, the Wireline Business Unit introduced several innovative offers for the data transmission networks and Internet access, including:

- Wi Fi service: internet wireless and high speed access (available since the end of 2003);
- new solutions with fiber optic technologies for SMEs (small and medium-sized enterprises), mainly for IP services;
- broadband everywhere project: plan to cover 100% of business customers sites with broadband technology.

Revenues from data services (including data equipment rental and assurance) amounted to 1,103 million in 2003 and increased by 12.3% over 2002 (982 million in 2002). The growth in revenue from data services has been driven mainly by innovative data services (data transmission through broadband and the fiberoptic technology network) that increased by more than 42% in 2003 compared to 2002 (520 million in 2003 and

366 million in 2002) while revenues from data equipment increased to 246 million (approximately 220 million in 2002).

Revenues from traditional data services (data transmission using data packet technology) decreased from approximately 400 million in 2002 to approximately 340 million in 2003 due to customer migration to broadband services.

Leased Lines. Leased lines are trunk lines offering a customer-subscriber a permanent connection for telecommunication services between two geographically separate points. This kind of connection can be used to handle high volume voice, data or video transmission.

In 2003, revenues from lines leased to business customers were 407 million (461 million in 2002). The decrease in revenues in 2003 compared to 2002 was primarily attributable to the migration by customers towards other kinds of connections which are offered at lower prices. Leased lines have been gradually replaced by broadband connections that offer many advantages such as new services and flexible connection packages; prices are gradually falling for new offers and for migration to higher speed lines that allow more data transmission with lower cost.

As of December 31, 2003, there were approximately 274,000 (in points of entry of data network) lines leased to business customers (approximately 320,000 at December 31, 2002) and approximately 107,000 digital leased lines (132,000 at December 31, 2002).

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Retail Value Added Services

Retail VAS include new services for all Wireline customers such as web services, outsourcing and security for business customers and SMS (from fixed telephones), Memotel (centralized mail box) and Chi è (identification of calling number) for residential customers. Revenues from VAS have grown significantly in recent years. In 2003, the Wireline Business Unit VAS revenues were 1,122 million, an increase of 13.3% over 2002 (990 million in 2002) mainly due to an increase in the services offered and the number of new customers.

Wholesale

Wholesale services consist of national and international services to other domestic and international operators. Services offered to other domestic operators (wireline and wireless operators as well as Internet service providers) consist mainly of interconnection to Telecom Italia s network, in terms of access and traffic (carried traffic and transits); broadband access (ADSL and XDSL access); and leased lines. Services offered to international operators consist mainly of traffic (carried traffic and transits) and data access.

Revenues from wholesale services were 3,269 million in 2003, approximately the same amount as the previous year. Domestic wholesale services decreased by approximately 45 million due to price reductions in interconnection services, not completely absorbed by growth in revenues from broadband and other services. International wholesale services increased by approximately 45 million, due to significant growth in traffic volumes, especially in traffic carried to other operators.

Traffic and Tariffs

Domestic Traffic

The table below sets forth, for the periods indicated, certain traffic data for Wireline.

	Year ended December 31,				
	1999	**2000**	**2001**	**2002**	**2003**
Wireline total traffic (Retail and Wholesale) (billions of minutes)	134.8	171.3	209.8	214.9	226.6
of which:					
National(1)	*128.1*	*163.8*	*201.1*	*204.7*	*215.2*
International(2)	*6.7*	*7.5*	*8.7*	*10.2*	*11.4*
Retail Traffic:					
Average minutes of use per fixed line subscriber during period(3)	4,298	4,722	4,739	4,292	4,127
of which:					
Local traffic during period (in average minutes)(4)	*2,767*	*3,621*	*3,575*	*3,198*	*2,971*
Long distance traffic during period (in average minutes)	*1,531*	*1,101*	*1,164*	*1,094*	*1,156*

(1) Data include total retail traffic (international outgoing traffic excluded) and total domestic wholesale traffic.
(2) Data include international retail outgoing traffic and total international wholesale traffic.
(3) Data include total retail fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to mobile networks).
(4) Data for the year 1999 include internet dial-up traffic and excludes district traffic which is accounted for in long distance traffic; data for the years 2000, 2001, 2002 and 2003 include district and internet dial-up traffic.

Domestic Fees and Tariffs. Since November 1, 1999, the Telecom Italia Group s traffic tariffs have been based on a per second billing system with an initial fixed charge (the call set up). The tariff per call set up (VAT included) varies depending on the kind of call: 0.0619 for local calls, 0.0787 for long distance calls and for fixed-mobile calls of business customers, 0.1200 for fixed-mobile calls of residential customers and 0.3098 for international calls. The tariff per second varies according to the kind of call, the time of day and the day of the week. Since December 1997, the Telecom Italia Group has introduced tariff packages for residential and business customers which provide for discounts on national and international traffic tariffs and additional rental charges.

Traffic packages mainly consist of Teleconomy and Hello offers for the Mass Market and SOHO customers. Further customized offers are provided to business customers.

Hello was launched as a brand during 2003 while Teleconomy was launched in June 2000. Both of them include tariff packages with targeted discounts and customized programs for residential and business customers. Hello offers were launched to further support retention efforts and to win back customers.

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Penetration of Teleconomy and Hello offers and ADSL lines are key strategic priorities for the Wireline Business Unit.

Hello offers for retail customers, which Wireline Business Unit introduced in 2003, include:

- Hello Sempre (fixed price of 0.125 for national calls, excluding calls to mobile, at an additional monthly fee of 5.58 euro); and
- Hello Forfait (no payment for national calls, excluding calls to mobile, at an additional monthly fee of 39.0).

For business customers Wireline Business Unit has introduced specific offers for companies with high volumes of traffic, allowing companies to choose among a variety of price plans.

Domestic Tariff Rebalancing. The Telecom Italia Group commenced rebalancing its tariffs in 1991 and made various adjustments until 1997. Since December 1998, the National Regulatory Authority has been responsible for tariff regulation. On July 28, 1999, the National Regulatory Authority introduced a price cap mechanism designed to promote productivity and efficiency for the Telecom Italia Group, as the incumbent operator in markets with a low level of competition. The price cap was applied until December 31, 2002 to a whole basket of public voice telephone services composed of activation fees, basic subscriber charges, local and long distance calls and international tariffs.

On July 23, 2003, the National Regulatory Authority introduced a new price cap mechanism, also referred to as a safeguard cap , which is intended to control the maximum prices Telecom Italia may charge for voice services for the four year period 2003-2006. Such price caps cover:

- basic subscriber charges and other access charges RPI (Retail Price Index) + 0%, as well as a sub-price cap for residential subscription charges of RPI RPI;
- local and out-of-district calls with a cap equal to RPI-RPI;
- fixed to mobile traffic, limited to the fixed call segment belonging to Telecom Italia (the Retention segment) with a cap equal to RPI-6%.

The basket of public voice telephone services includes one-off fees, monthly fees, domestic and fixed to mobile standard tariffs.

Consistent with the new price-cap mechanism, Telecom Italia continued to simplify its pricing structure during the course of 2003. In particular, beginning September 15, 2003, the following price changes became effective:

- access for basic subscription fees and business charges (+6.5%);

- traffic local calls: the discount on local calls exceeding 15 minutes was eliminated (+1.8%); and
- traffic long-distance: the two different pricing levels applied to calls were unified, resulting in one single rate at a point where customer telephone charges would be reduced by 3%.

In addition, on June 1, 2003, the price of wireline to mobile traffic was reduced (-11.7%) as a result of the variation in the termination charge (-10.9%) and retention (-14.3%).

In particular:

- the termination charge represents the cost that Telecom Italia incurs for terminating the traffic generated by its wireline customers on the networks of mobile operators; the rate per minute is fixed by the mobile operators;
- retention represents the difference between the amount paid by the customer and the amount due to the mobile operators for termination: the rate per minute for retention by Telecom Italia is fixed by the National Regulatory Authority (Order No. 47/03 CONS).

With respect to international traffic, after the sharp price reductions in the years 1998-2002, during 2003 a single adjustment was put into place (on November 1) consisting of the introduction of a new rate zone, without causing any change in customers expenditures.

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International Traffic

The table below sets forth, for the periods indicated, information with respect to incoming and outgoing traffic, including direct dial and operator assisted calls and mobile traffic.

	Year ended December 31,				
	1999	2000	2001	2002	2003
Total outgoing traffic (millions of minutes)	2,390	2,706	3,015	3,405	3,682
Growth in outgoing traffic (%)(1)	2.2	13.2	11.4	13.0	8.1
Total incoming traffic (millions of minutes)	3,419	3,415	3,845	3,842	3,299
Growth in incoming traffic (%)(1)	15.9	-0.1	12.6	-0.1	-14.1
Total international transit traffic (millions of minutes)	857	1,310	1,825	2,995	4,382
Growth in international transit traffic (%)(1)	7.6	52.9	39.3	64.1	46.3

(1) For each of the years ended December 31, the percentage growth figures represent growth per annum over the prior year s end.

The trend in international traffic volumes from 1999 to 2003 was mainly impacted by macroeconomic factors such as growth in foreign demand, import/export activities, foreigners and new subscribers. The decline in gross operating revenues from 2002 to 2003 is mainly attributable to the impact of continuing price reductions and increasing competition.

Outgoing international traffic is mostly concentrated in communications traffic with Germany, France, Romania, Switzerland, United States, United Kingdom, Albania and Spain, which together accounted for approximately 48% of toll minutes in 2003.

Incoming international traffic is divided into two general categories: traffic incoming on the fixed network and traffic incoming, or deemed to be incoming, on the mobile network. Such incoming, or deemed to be incoming, traffic, which originates outside Italy, utilizes the fixed network before terminating on the mobile network. With respect to the mobile network, the distinction between incoming or deemed to be incoming is that incoming traffic is the traffic generated abroad and directed to the mobile network through the fixed network in Italy, while traffic which is deemed to be incoming is traffic generated in Italy through the use of international calling cards. Because of the use of international calling cards, such traffic is deemed to be incoming from an international network although the call may be generated in Italy.

The traffic directed to the mobile network decreased because the component of the traffic deemed to be incoming registered a 93% decline due to the introduction of a surcharge for calls directed to the mobile network with a consequent increase in the price of the international calling cards.

In order to make up for the loss in market share following the decrease in incoming traffic, wholesale international activities were focused on managing international transit traffic that resulted in volume increases of 46% due to the competitiveness of Telecom Italia s offer in the worldwide market.

International Settlement Arrangements. The Telecom Italia Group derives revenues from foreign telecommunications operators for incoming calls which use the Telecom Italia Group s network. The Telecom Italia Group has bilateral settlement arrangements with other international telecommunications operators under the general auspices of the ITU (International Telecommunication Union). Because incoming and outgoing international traffic are relatively equal, the Telecom Italia Group s net payments on international accounting rates are negligible. This has the effect of limiting the Telecom Italia Group s exposure to changes in currency exchange rates. The exposure to changes in currency exchange rates has also been reduced due to the adoption of the euro.

Interconnection with Other Operators

On March 22, 2003, the National Regulatory Authority approved the introduction of the Network Cap mechanism to regulate interconnection tariffs until the end of 2006. Starting with the 2003 Reference Offer (RO), the market will have greater transparency with respect to the arrangements relating to interconnection services, allowing the operators to rely on stable economic values in preparing their business plans.

The Authority has defined five main services baskets with relative caps (in the form of RPI-X):

- SGU (Local exchange interconnection and interconnection kit and circuits) = RPI 8%
- SGT (Single transit interconnection) = RPI 6%

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- 2SGT (Double transit interconnection) and international transit by SGT = RPI 3.75%

- Ancillary services (i.e. number portability charges, CPS (Carrier Pre-selection Service) charging, etc.) = RPI RPI

- LLU (Local Loop Unbundling) = As of June 1, 2004, the National Regulatory Authority has not defined the caps related to this service.

With respect to LLU, the National Regulatory Authority in its order has outlined a network cap mechanism to be implemented from January 1, 2004 through December 31, 2006 aimed at moving from historic costs to long run incremental costs (LRIC). LRIC of the access network are likely to be higher than historic costs. Currently, Telecom Italia has been asked to fix a LLU price (8.30/month) which is the lowest in Europe and is significantly lower than the Telecom Italia retail access price. Regarding implementation, the Italian LLU market is one of the fastest growing LLU markets in Europe with its 510,000 fully unbundled lines on December 31, 2003 (Italy is second after Germany where LLU started about two years before), representing an increase of 407,000 lines compared with the end of 2002. In addition, Telecom Italia presents the most detailed and complete LLU offer in Europe (physical LLU, sub loop unbundling, shared access and all different kinds of co-location) and Telecom Italia has satisfied all National Regulatory Authority requests in terms of equipment of the sites requested by OLOs.

In August 2003, the National Regulatory Authority approved, subject to certain technical and economic amendments, the 2003 RO originally submitted by the Telecom Italia Group in April 2003.

The Telecom Italia Group s 2003 RO includes the conditions for FRIACO (Flat-Rate Internet Access Call Origination) service, partial circuits provisions, shared access and sub-loop unbundling, thus enabling a competitive development of internet access and broadband services.

- FRIACO: the Telecom Italia Group has been offering this service since 2001.

- Partial circuits: represent partial circuits from customer premises to the OLOs Point Of Presence (POP), as a segment of an end-to-end leased line. The National Regulatory Authority determined that economic conditions are to be set according to the price ceiling methodology that was established by the European Commission Recommendation C(1999) 3863 of November 24, 1999, and introduced the price ceiling into national legislation with Order No. 10/00/CIR. For speeds and distances of partial circuit different from those included in the Recommendation, the prices are based, according to national as well as European accounting requirements, on Telecom Italia s own costs, evaluated according to the fully allocated current costs model.

- Billing and bad debt service: the Telecom Italia Group must also offer billing to OLOs who decide not to bill the customers (*i.e.* customers that are connected to the network through indirect access service) accessing their non geographic services. The Telecom Italia Group, as required by the National Regulatory Authority, fixed the level of charge for the billing service at 2.9% calculated on the total revenues of each OLOs non geographic service. With respect to bad debt, the level of risk and insolvency is subject to negotiation between Telecom Italia and the OLOs.

Since April 2002, ISPs (Internet Service Providers) (pursuant to law 59/02) have access to the RO of the notified operators with respect to internet traffic origination (both for metered and unmetered interconnection) and termination on 70x codes (dedicated in Italy to Internet access) and partial circuits. On June 26, 2002 the National Regulatory Authority issued an Order to define the criteria for ISPs to gain access to the RO technical and economic conditions.

On April 28, 2003, the National Regulatory Authority approved rules which discipline the manner in which customers can request deactivation of the Carrier Preselection Service . The National Regulatory Authority determined that a client can send his deactivation request both to Telecom Italia and to the preselected OLO.

In 2003, the Telecom Italia Group set up interconnections with the networks of 8 additional operators, making a total of 92 operators at December 31, 2003. In the same period eight operators have disconnected.

During 2003, the following contracts were also signed or renewed:

- Seven new interconnection agreements (for a total of 91 since 1995);
- Seven additional reverse agreements, terminating calls on the network of another operator, for a total of 71, since 1998;
- 39 agreements to supply high-speed access services using xDSL technology;

- Five carrier preselection contracts, one district carrier selection agreement and 12 number portability agreements;
- One contract for local loop unbundling service on the local network for a total of 41 since 2000;
- 29 contracts to supply Digital Data Circuits for a total of 112 since 1998.

Fixed Network

Since 1988, the Telecom Italia Group has installed high levels of fiber optics, intelligent nodes, digital switching, satellite connections and high speed data transmission technology. The technologically advanced nature of its fixed network permits the Telecom Italia Group to offer a variety of advanced services such as toll free numbers, call waiting and call forwarding, VPNs (Virtual Private Networks), premium charges and charge splitting.

Domestic Network

Fixed Network. The Telecom Italia Group s domestic fixed network is made up of 33 gateway areas (each area gateway has two points of interconnection which allows our fixed and mobile network to exchange signals) and 628 main local switches (only for fixed OLOs). Each local switch belongs to only one of the 33 gateway areas. The long distance fixed network includes 3.9 million circuits, while the distribution fixed network includes 105.2 million kilometers of pairs over copper cable. In detail, the national network in statistics at December 31, 2003 was as follows:

Exchange areas	Approximately 10,340
Switching areas	615, served by 628 line SGU (Urban Group Stages)
Gateway Areas	33
Copper access network	105.2 million kilometers-pair
Fiber optic access network	428,741 kilometers-line
Fiber optic carrier network	3.2 million kilometers-line
Direct dialing circuits	3.9 million
Network for direct digital circuits (PARD)	474,690 access points with speed up to 2 Mbit/s
Network for direct analog circuits (PARD)	94,043 access points
Frame Relay Accesses	83,824 gates at 2Mbit/s
PoP main data networks	32

SDH and ATM. The Telecom Italia Group introduced SDH transmission technology into operation in the long distance fixed network in 1996 and introduced such technology into operation for its local fixed network during 1997. These transmission systems are operating on fibreoptics from 155 Mbit/s up to 2.5 Gbit/s. Moreover, in 2002 Telecom Italia began using transmission systems with speed up to 10 Gbit/s. Work on the development of the Arianna network which, by use of the latest generation of SDH technologies and the optical DWDM technology (Dense Wavelength Division Multiplexing) constitutes the basis for the transport network with a high transmission capacity capable of covering the entire Italian territory, continued during 2003. Arianna is based on a SDH rings architecture; since 2000, in order to reduce the number of fibers, DWDM systems have been used to multiply by a factor of 12 up to 40 the available optical fiber band and the current transmission capacity, thus increasing the transport capacity of the connections. In November 2002 Wireline introduced a new generation of Optical Digital Cross Connect on the domestic wireline transmission backbone in order to progress with the transition from Arianna towards the new generation of meshed ASTN (Automatically Switched Transport Network) optical backbone which started during 2003 and will continue during 2004. By using the ASTN approach it is possible to build a multiservice platform with a high level of integration with the IP network. First applications of Metro DWDM systems were developed in the Rome and Milan metropolitan areas.

The evolution of the transport network towards the optical network will make it possible to increase the operational capacity of all types of traffic, from phone calls to Internet traffic.

ATM switching technology, introduced in 1996, allows the transfer of information combining data, video and other services over public and private networks both domestically and internationally. Telecom Italia ATM/Frame Relay networks are overall networks that work together as a multiservice network, using SDH transmission systems as a physical layer. The ATM Network allows for the provision of ATM native services with access rates ranking from 2Mbit/s up to 155 Mbit/s. It also acts as a backbone for both the Frame Relay Access network (with access rates ranking from 64 kbit/s up to 2 Mbit/s), and for the DSL (Digital Subscriber Line) Network, used for the provisioning of xDSL services (ADSL High-bit-rate Digital Subscriber Line or HDSL) and SDSL. The ATM/Frame Relay networks allows access to IP and MPLS services (Multi Protocol Label Switching) by customers with access rate ranking from 64 kbit/s to 155 Mbit/s.

Network Quality and Productivity. Telecom Italia Group s investment in its domestic service network has enabled it to continue to reduce the average time required for the installation of new lines. The effectiveness rate of the fixed network is defined as the ratio of successful calls to the total number of call attempts, not including failures caused by the calling party s behavior, in a specified time period. A successful call is a call attempt to a valid number, properly dialed, where the called party s busy tone, ringing tone, or answer signal is recognized on the access line of the calling user.

To reduce costs and improve efficiency, the Telecom Italia Group undertook in 2001 and continued in 2002 and in 2003 an extensive program to reengineer its network operation and maintenance organization, to permit a more effective use of human resources.

Beginning in 1999, operating systems were developed with the aim of ensuring the offering of new services, optimizing operational activities and pursuing objectives of total quality. Procedures were developed for systems dedicated to supervising traffic for verifying levels, the immediate management of measurements and constant monitoring of the quality of the service provided. In systems that operate the flexible network for data transmission, features were activated which reduce activation and connection time, permit the timely recognition of customers who have experienced malfunctions in services and augment the availability of the connections themselves. Moreover, operating systems have been equipped with new features for marketing new services.

Broadband Network/ADSL. The Telecom Italia Group s broadband network is capable of supporting advanced telecommunications services and multimedia applications and, to this end, the Telecom Italia Group has installed significant levels of fiber optic cables in its fixed network. In 1998, the Telecom Italia Group began introducing ADSL systems over copper pairs to deliver interactive services (e.g., fast-Internet). ADSL allows the Telecom Italia Group to fulfill in the short-term, market driven needs to provide services like fast-Internet, multimedia, video conferencing and teleworking either for business or residential customers. Furthermore, ADSL together with other existing infrastructure and satellite services allows the Telecom Italia Group to focus the commercialization of its broadband network services on a market basis and to tailor investments to the growth of the market. With reference to access services using ADSL technology, in 1999, the technical and commercial trials with fast Internet access for residential and Soho customers, begun in Rome and Milan at the end of 1998, were concluded. In 2003, commercial services with access to ADSL technology for business customers and Internet Service Providers had been extended to 2,100 cities (approximately 1,300 at the end of 2002). The commercial services for business customers include the use of ADSL technology in urban areas to supply access to IP and ATM services of the Telecom Italia Group s data networks. The services for ISPs supply ATM access based on ADSL technology to the public, leaving the commercial interface with the final customer to the service provider. At the end of 2003, the local exchange areas covered by ADSL technology numbered 3,000 (2,120 at the end of 2002).

Fiberoptic Cables. At December 31, 2003, the Telecom Italia Group had installed approximately 3.64 million kilometers of optical fiber for access and transfers, of which approximately one million kilometers were installed on long distance fixed-lines. Fiberoptic cables significantly increase the capacity of the network and permit the Telecom Italia Group to provide new advanced services based on the simultaneous transmission of several kinds of signals, such as voice, data and video. To enable the offer of such services, the Telecom Italia Group is planning to introduce fiberoptics in its local access network.

In 2003, a project which started in the second half of 2000, consisting of the creation of an optical fiber ring between Milan and Palermo (T-Bone), was continued with the installation of cable containing 96 optical fibers on two backbones covering about 6,000 kilometers.

Flexible Data Network. The Telecom Italia Group also operates a flexible network equipped with a centralized system that makes it possible to establish dedicated data links from a work station. At December 31, 2003, 500,000 direct digital line access points and 100,000 direct analog line access points had been installed.

International Network

Since 1997, the Telecom Italia Group has rationalized its international fixed network and enhanced international transmission capacity.

The Telecom Italia Group offers international wholesale services (Voice, Data and IP) and international retail services (Global Corporate Network) for multinational customers utilizing its own cross-border backbone, bilateral links and NNI Agreements (Network Node Interface Agreements).

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The cross-border backbone is based on three regional networks in Europe (PEB), Latin America (LAN) and in the Mediterranean basin (MED):

- **PEB** (Pan European Backbone). A fiber optic network 2 fiber pairs, 400 Gbit/s each laid in the main industrialized European countries: Italy, France, U.K., Netherlands, Belgium, Germany, Switzerland, Austria and Spain with a total length of 12,000 km. The cross-border services available for wholesale customers are: Managed Bandwidth, IP Connectivity, International Private Leased Circuit, Global Voice Services, GRX (GPRS Roaming eXchange for Mobile Operator);

- **LAN** (Latin American Nautilus). A high capacity backbone based on an optical fiber ring network both on earth and under sea, 30,000 km long, including the Miami-New York City link. The ring, having optical automatic traffic protection and a bandwidth up to 320 Gbits, links the most important cities of South America to Central and North America;

- **MED** (Mediterranean Nautilus). A submarine optical ring, in a high-availability network configuration, with a total length of 7,000 km 6 fiber pairs, 64 lambdas (10 Gbit/s each) per fiber pair- linking the main markets of the Central-Eastern Mediterranean area: Italy, Greece, Turkey and Israel. Presently, the optical ring links Catania, Athens, Chania-Crete, Haifa and Tel Aviv.

Telecom Italia Group, with its international network, connects more than 250 world-wide operators and owns capacity on more than 434,500 kilometers of submarine cables that, from Italy, transport traffic along two major paths: longitudinal routes (towards the United States, Middle and Far East) and diagonal routes (toward Central and North Europe).

The multiservice network is based on class-4 softswitch, that are substituted for traditional exchanges, IP/MPLS and ATM switching devices, and state of the art transmission technologies: DWDM and SDH (10 Gbit/s lambda, where lambda represents an optical wavlength) with traffic protection mechanisms (MS SPRING, SNCP and MSP).

Telecom Italia Group s international backbone has been built to offer end-to-end services in strategic areas; it has Points of Presence in Europe (16 POPs), in USA (3 POPs), in the Mediterranean basin (4 POPs) and in South America (7 POPs).

The POPs in the USA belong to Telecom Italia of North America (TINA), a wholly-owned subsidiary of Telecom Italia, that has implemented POPs in Newark (NJ), New York and Miami to offer Voice and IP/Data services that are connected to the Pan European Backbone and to Latin American Nautilus.

The multiservice backbone delivers voice, IP and managed bandwidth services in the USA and Europe and managed bandwidth services in the Mediterranean and in South America where, from 2003, IP services have been added.

During 2003, there were major implementations related to cross-border backbone deployments in Europe, the Mediterranean and Latin America. In particular, the main activities in Europe have been to widen the IP and data services portfolio:

- PanEuropean Backbone extension in Spain with two new POPs (Madrid and Barcelona);

- deployment of optical city rings in London, Paris, Frankfurt, Amsterdam, Zurich and Vienna, with points of presence in the main European telehouse facilities. A telehouse or co-location center (colo) is a type of data center where multiple telecommunications network or service providers, such as telecommunication operations or ISPs, site their connections to other networks;

- new POPs in Lyon and Marseille, also to support ADSL services in France;

- upgrading of access and switching devices to support wholesale Fast Ethernet, Giga Ethernet, IP Burstable, ToIP services and retail services for Multinational Customers.

In addition we have upgraded transmission capacity of the Pan European and transatlantic backbone.

Finally, in order to improve quality of service and decrease operational costs, a project was begun to replace the Italian legacy switching exchanges with the class-4 softswitch now used in the Telecom Italia Group s backbone (Europe and USA).

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Retail International Network

During 2003, Telecom Italia started the European project International Broadband through:

- the start-up of Telecom Italia France, a new licensed French operator;
- the acquisition of HanseNet, an existing German operator active in the Hamburg area.

Telecom Italia intends to offer access to innovative broadband services in the main European metropolitan areas, leveraging on its know-how and technological assets, beginning with France and Germany.

France. In 2003, Telecom Italia France was organized, a start-up company that will offer services mainly based on Local Loop Unbundling.

The main activities carried out during 2003 have been:

- deployment of POPs in the cities of Paris (2 POPs), Lyon, Marseille (also serving Aix-en-Provence) and Nice;
- 116 central offices equipped for local loop unbundling;
- deployment of fiber optic connections among POPs, through Telecom Italia s Pan European Backbone, and between POPs and 106 exchanges for a total of 1,210 Km. The remaining exchanges are connected to the POPs through leased lines;
- creation of interconnectivity with France Telecom for voice and data traffic.

Germany. In September 2003 we acquired HanseNet, a city carrier with its own infrastructure, with the goal of developing broadband services in the Hamburg area. Technical platform enhancement, to support services starting in 2004, was activated.

The main features of Hansenet network as of December 31, 2003 were:

- 3 POPs;
- 100 local exchange for the unbundling service;

- 1,090 Km fiber optical cables;
- 420 interconnection circuits with Deutsche Telecom (2Mbit/s).

Financial data of the main subsidiaries

The following table sets forth operating revenues, gross operating profit and operating income for the main subsidiaries of the Wireline Business Unit on a stand alone basis. The financial data will not tie directly to consolidated segment data due to intercompany, consolidation and other adjustments.

		National Subsidiaries				International Subsidiaries						
		Atesia	Path.Net	Loquendo	Telecom Italia Sparkle Group (*)	HanseNet Telekom-munikation GmbH	Latin American Nautilus Group		Mediterranean Nautilus Group		Med-1 Group	
								U.S.$		U.S.$		U.S.$
Gross operating revenues	2003	93	117	15	1,671	102	40	46	63	71	17	20
	2002	98	93	15	19	83	29	28	64	61	20	19
	Change (%)	(5.1)	25.8			22.9		64.3		16.4		5.3
Gross operating profit	2003	26	10	1	296	18	4	5	22	25	11	12
	2002	38	5	0	(30)	22	11	11	26	24	12	12
	Change (%)	(31.6)	100.0			(18.2)		(54.5)		4.2		
Operating income	2003	17	9	(2)	144	(24)	))	(15)	(29 56	(33)	4 4	4
	2002	32	4	(1)	(43)	(37)	(13	(6)	)	53		4
	Change (%)	(46.9)	125.0	(100.0)		35.1	(6	(150.0)		(162.3)		

(*) 2002 data referred to TMI group, before that Telecom Italia s International Wholesale Services business was contributed to Telecom Italia Sparkle on December 31, 2002.

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Major 2003 corporate events affecting scope of consolidation

Lisit Informatica. On February 4, 2003, Telecom Italia, in a temporary association of companies with Finsiel and Lutech (Lucchini group), won the bid held by the Lombardy Regional Authority for the supply of goods and services needed to disseminate and manage the Regional Services Card throughout the Lombardy Region. The total value of the bid won by the association led by Telecom Italia, scheduled to last until 2009, is approximately 350 million. Within the framework of the obligations undertaken, Telecom Italia and Finsiel acquired 35.2% of the share capital of LISIT, for a total of 54 million. As at December 31, 2003, the total stake held by Telecom Italia Wireline in LISIT was 24.2%.

Loquendo. In March 2003, Loquendo was transferred to Wireline Business Unit from the IT Group Operating Activity.

Agreement for the acquisition of Megabeam. In view of the conditions laid down by the Italian Antitrust Authority on August 7, 2003, on September 18, 2003, Telecom Italia annulled the preliminary contract for the acquisition of Megabeam, the first Italian wireless internet service provider, signed on March 10, 2003. Telecom Italia expects to continue to avail itself of the cooperation of Megabeam, with which there is already a commercial agreement covering 19 locations.

Intelcom San Marino. In August 2003, Telecom Italia International acquired the remaining 30% stake in Intelcom San Marino. Subsequently, in December 2003, Telecom Italia International sold its entire 100% stake in the company to Telecom Italia Sparkle, which is part of the Wireline Business Unit.

Hansenet. In September 2003, the acquisition from e.Biscom of 100% of HanseNet, a broadband operator in the Hamburg area, was finalized by the Wireline Business Unit for a total investment of 243 million. To this end, Telecom Italia had previously purchased the company Telecom Italia Deutschland GmbH which was used to purchase the entire investment in HanseNet.

BBNed group. In September 2003, the BBNed group (previously part of International Affairs) moved to the Wireline Business Unit.

Latin American Nautilus S.A. In December 2003, after the recapitalization of the company, Telecom Italia became the sole shareholder of Latin American Nautilus S.A..

Events subsequent to December 31, 2003

- Effective March 15, 2004, Telecom Italia raised the entry level offering for ADSL from 256/128 Kbps to 640/256 Kbps, one of the highest speeds in Europe in terms of uploading or downloading data.
- On March 15, 2004, Telecom Italia, in keeping with its commitment to develop innovative broadband services, launched the video on demand service for computers through the Rosso Alice portal. This portal, which is organized into six areas (films, sport, music, videoclips, games, information and video-community) will offer the service on demand to all Internet users with an ADSL

connection. Alice customers can purchase the content through a credit card or by direct debit to their phone bill, whereas other users may only purchase content through a credit card.

Mobile

The Mobile Business Unit (TIM group) operates in the sector of national and international mobile telecommunications. Its international operations are concentrated in Latin America and in the Mediterranean Basin.

The Mobile Business Unit accounted for gross operating revenues of 11,782 million in 2003, 10,867 million in 2002 and 10,250 million in 2001.

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As of December 31, 2003, the business unit was organized as follows:

Mobile

National Subsidiaries	International Subsidiaries		Affiliated Companies
TIM Telecom Italia Mobile S.p.A.	TIM International N.V.		IS TIM T.H.A.S. (Turkey)
	• TIM Brasil group	STET Hellas Telecommunications S.A. (Greece)	
	- Tele Nordeste Celular Participacoes group (Brazil)		
	- Tele Celular Sul Participaçoes group (Brazil)		
	- Maxitel S.A. (Brazil)		
	- TIM Celular S.A. (Brazil)		
	- Starcel Ltda (Brazil)		
	• TIM Perù S.A.C.		
	• Corporacion Digitel C.A. (Venezuela)		
	• Blah! S.A. (formerly TIMNet.com S.A Brazil)		

Among the large mobile telecommunications operators in Europe at the end of 2003 TIM had the largest number of lines in its domestic market (source: Mobile Communication magazine) and has been the fastest growing area of the Telecom Italia Group s business for the past several years. Line growth was 11% in 2001, 6% in 2002 and 3% in 2003. Gross operating revenues from TIM totaled 9,469 million, 9,022 million (8,915 million net of Blu merger effect) and 8,357 million in 2003, 2002 and 2001, respectively.

Services Italy. TIM primarily offers digital mobile services as well as its legacy analog service which is being phased out. The GSM digital service, which commenced operations in April 1995, uses digital technology and is the standard throughout Europe. GSM generally provides higher quality transmission than analog service and may be used by customers to make and receive mobile calls throughout Europe and certain other countries. As of May 23, 2004, roaming agreements have been reached with 378 operators in over 203 countries, allowing customers to make and receive calls abroad. See Mobile Tariffs below. The analog service is based on the TACS 900 standard and began operation in 1990. See Cellular Network .

Customers and Lines. The penetration of mobile telecommunications service in Italy is above the Western European average at approximately 99 lines per 100 inhabitants at the end of 2003 and growth rates have been substantially higher than the European average. This compares to a penetration rate of 89 and 94 lines per 100 inhabitants at the end of 2001 and 2002, respectively. The increase is due to innovative services and an increase in customers with multiple lines and the number of operators. TIM s customer base consists of GSM subscribers and customers holding GSM TIM Cards (GSM Prepaid Customers) as well as TACS subscribers and customers holding TACS prepaid services,

(TACS Prepaid Customers and together with GSM Prepaid Customers, Prepaid Customers). TIM is in the process of closing down its TACs service and is transitioning its customers to its GSM network. In 2003, TIM had a 27.3% market share of net additional GSM lines, corresponding to 0.8 million of net lines, compared to 1.6 million for Vodafone Omnitel, 1.2 million for Wind and the remaining 0.4 million attributable to H3G (3).

TIM s statistical data excludes 700,000 silent lines. The Italian market, which has a high penetration of prepaid cards, is characterized by certain customers acquiring multiple lines in order to take advantage of specific/time-limited commercial offers. Once these offers expire these customers tend not to continue the use of such lines which is facilitated by the prepaid nature of the arrangement. As a result, TIM excludes the silent lines in order to provide greater consistency between the number of lines managed by the Company and the development of the business.

At December 31, 2003, the number of lines for TIM s GSM and TACS mobile service was approximately 26.1 million (of which 25.5 million were GSM lines, consisting of 2.6 million GSM subscribers and 22.9 million GSM Prepaid lines). As of March 31, 2004, TIM s customer base remained essentially unchanged at 26.0 million lines.

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The table below sets forth, for the periods indicated, geographic and population coverage data for TIM s TACS and GSM services.

	Year ended December 31,				
	1999	2000	2001	2002	2003
			(%)		
TIM Italian geographic coverage					
TACS	83	83	83	83	83
GSM	89	92	94	94	94
TIM Italian population coverage					
TACS	98	98	98	98	98
GSM	99	100	100	100	100

The table below sets forth, for the periods indicated, selected customer data for TIM s domestic business.

	Year ended December 31,				
	1999	2000	2001	2002	2003
	(number of customers in thousands)				
Lines at period end(1)	18,527	21,601	23,946	25,302	26,076
TACS subscribers	832	495	304	180	95
TACS prepaid lines	2,344	1,950	1,430	815	480
GSM subscribers(2)	2,442	2,485	2,538	2,685	2,595
GSM TIM Prepaid Lines	12,909	16,671	19,674	21,622	22,906
			(in%)		
Customer growth	29.6	16.6	10.9	5.7	3.1
Churn(3)	12.7	15.7	15.6	18.0	13.2
TIM penetration(4)	32.5	37.5	41.6	43.9	45.3
Cellular market penetration(5)	53.1	73.3	89.0	93.7	99.2
			( )(6)		
Average revenue per line per month(7)	34.9	30.5	29.1	28.8	29.1

(1) Includes lines of TACS and GSM services, including Prepaid Customers and excludes the silent lines.
(2) Commenced GSM services in April 1995.
(3) Data refers to total lines. The churn rate for any given period represents the number of TIM customers whose service was discontinued during that period due to a payment default or who voluntarily gave up a mobile telephony service during that period, expressed as a percentage of the average number of customers during that period.
(4) TIM customers per 100 inhabitants.
(5) Customers per 100 inhabitants for the entire market.
(6) The data for the years ended December 31, 1999 and 2000 was in lire and was translated into euros at the irrevocably-fixed rate of exchange of Lit. 1,936.27 = 1.
(7) Including Prepaid Card revenues, non-TIM customer traffic revenues and excluding equipment sales.

The growth in TIM s mobile lines over the five year period reflected in the table above has resulted almost entirely from the marketing success of the GSM TIM Card, a prepaid card which permits the customer to make outgoing calls up to the limit on the card for the 12 months following issuance of the card or the last recharge of the card and receive an unlimited number of calls for the 13 months following issuance of the card or the last recharge of the card. If a GSM TIM Card is not recharged within this 12-month period, the customer will not be able to make outgoing calls but for one additional month such customer will be able to receive incoming calls. The GSM TIM Card can be recharged at any time to permit additional outgoing calls. The GSM TIM Card offers several advantages, including elimination of bad debt charges and lower administration costs, as no statements are sent to customers. Approximately 89.7% of TIM s lines at December 31, 2003, are prepaid.

UMTS License. The Italian government awarded five UMTS licenses (third generation mobile communication system) in Italy in November 2000. TIM, together with Omnitel S.p.A. (now Vodafone Omnitel N.V.), WIND S.p.A., Andala S.p.A. (now H3G S.p.A.) and IPSE S.p.A., were awarded licenses to provide third-generation mobile services. TIM committed to pay 2,417 million for its license, with approximately 117 million, 117 million, 117 million and 2,066 million having been paid in December 2003, November 2002, November 2001 and December 2000, respectively. The licenses are valid for 20 years starting January 1, 2002. In 2001, TIM began an experimental UMTS service in its service center in Padoa, and a gradual roll-out of the UMTS network has begun. Transition toward third generation will be gradual with a broad launch of the service expected in 2004.

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Traffic. The table below sets forth, for the periods indicated, selected traffic data for TIM s business.

	Year ended December 31,				
	1999	2000	2001	2002	2003
	(millions of minutes)				
Total outgoing traffic per month	1,219	1,569	1,795	1,960	2,090
Total incoming and outgoing traffic per month	1,989(1)	2,479(2)	2,815(3)	3,036(4)	3,202(5)
	(% of total)				
Of which:					
TACS(6)	19.5	10.3	5.4	3.0	2.0
GSM(6)	80.5	89.7	94.6	97.0	98.0

(1) Includes domestic mobile incoming and outgoing traffic (93.9% of total mobile traffic in 1999 compared to 96.2% in 1998), international traffic (3.2% in 1999 compared to 2.3% in 1998) and roaming traffic (2.9% in 1999 compared to 1.5% in 1998). These data include fixed outgoing traffic to the mobile network.
(2) Includes domestic mobile incoming and outgoing traffic (90.4% of total mobile traffic in 2000 compared to 93.9% in 1999), international traffic (2.9% in 2000 compared to 3.2% in 1999) and roaming traffic (6.7% in 2000 compared to 2.9% in 1999). These data include fixed outgoing traffic to the mobile network.
(3) Includes domestic mobile incoming and outgoing traffic (92.8% of total mobile traffic in 2001 compared to 90.4% in 2000), international traffic (2.7% in 2001 compared to 2.9% in 2000) and roaming traffic (4.5% in 2001 compared to 6.7% in 2000). These data include fixed outgoing traffic to the mobile network.
(4) Includes domestic mobile incoming and outgoing traffic (94.5% of total mobile traffic in 2002 compared to 92.8% in 2001), international traffic (2.3% in 2002 compared to 2.7% in 2001) and roaming traffic (3.2% in 2002 compared to 4.5% in 2001). These data include fixed outgoing traffic to the mobile network.
(5) Includes domestic mobile incoming and outgoing traffic (95.5% of total mobile traffic in 2003 compared to 94.5% in 2002), international traffic (1.9% in 2003 compared to 2.3% in 2002) and roaming traffic (2.6% in 2003 compared to 3.2% in 2002). These data include fixed outgoing traffic to the mobile network.
(6) Includes traffic from Prepaid Customers.

Mobile Tariffs. TIM s mobile customers (other than Prepaid Customers) are charged a one-time connection fee, a monthly basic charge and traffic fees for calls, as well as a monthly government tax. Prepaid Customers are charged an initial connection fee of 26 for the GSM TIM Card and TACS prepaid service and are required to pay a fee ranging from 5 to 1 to the dealer for each recharge, according to the cost of each recharge. No other connection or subscription fees or taxes are payable by Prepaid Customers. Mobile customers (including Prepaid Customers) must purchase their own mobile telephone handsets. TIM does not subsidize the cost of mobile telephone handsets to its customers and does not intend to do so in the foreseeable future. In 2003, approximately 75% of revenues from TIM mobile services (net of access charge) were derived from traffic charges, 5% from sales and rental of equipment, 11% from VAS and 9% were miscellaneous revenues (subscription and connection fees).

TIM offers its customers a variety of different pricing packages which are tailored to address different usage patterns. Such packages include offerings to TIM s GSM customers of free minutes packages which are available in various options. TIM also offers packages such as, TIM Menù, a dedicated TACS and GSM pre-paid card. The customer can choose a rate suited to his or her own needs, combining the various items on a menu. The objective is to simplify the service offer and at the same time make them more flexible.

TIM enhanced its voice offers during 2003 in order to stimulate voice usage, traffic among TIM customers (with a positive effect on profitability) and increase customer loyalty. Some of the offers are:

- Chiama Ora : a service aimed to increase usage opportunities, which notifies the customers via SMS that the number called, originally not reachable, is available again;

- Sunday TIM aimed to increase net traffic on holidays and to optimize network utilization;

- 2 in 1 : that provides customers with two different numbers on the same SIM card, the service s goal is to encourage Number Portability and boost usage and ARPU;

- Office network an offer tailored for the SoHo segment to boost traffic among TIM customers (discount on traffic between a network of people defined by customers).

TIM also offers innovative services, such as an offering called AutoRicarica. The AutoRicarica formula has proven to be particularly successful: according to this formula, TIM gives a bonus of 3.70 (VAT included) for each 100 minutes of calls received.

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TIM also offers certain discount packages, which include TopTim, a discount plan for professionals that rewards both length of subscription and volume of traffic, and TimClub, a 15% discount on the three most frequently called wireless numbers (which is only available after the free bonus minutes have been used).

At the beginning of 2002, TIM launched the first exclusive service which allowed TIM customers to reverse billing charges to a rechargeable or contract TACS or GSM TIM mobile, or to Telecom Italia fixed network numbers.

In May 2002, TIM introduced the following new tariff plans: Unica and Unica10; customers can personalize their own tariff choosing between two options: SuperAutoricarica (self recharge from all numbers) and Trio, a special tariff for three TIM numbers or two TIM numbers and a Telecom Italia fixed network number.

GSM and TACS customers are charged on the basis of a per-seconds billing system paying for the actual duration of the call plus a call setup charge of 0.1 (which is not charged when free minutes are being used). At the end of 1997, TIM also introduced local tariffs. From time to time, TIM offers promotional packages to attract additional customers.

Value Added Services. TIM has been building its brand as a platform for content providers by entering into partnerships and developing business synergies.

In order to offer a wider range of services and content to its customers, TIM has strengthened its partnerships with some important providers like Acotel, Zed, Buongiorno Vitaminic and brands like Disney, MTV, Mediaset. TIM also has agreements with leading Italian banks and financial institutions to provide on-line trading and mobile banking and it was the first operator to launch the MSS Mobile Banking service in 2003.

Since 2000, when TIM started GPRS services, TIM has extended its UMTS coverage and has recently launched EDGE services. EDGE will make the use of multimedia services more satisfactory for TIM customers both in relation to consumer market applications, such as the MMS or video streaming, and the more typical corporate applications such as e-mail management, Internet and Intranet navigation due to its ability to transmit data more rapidly.

TIM has been the first in Europe to introduce the PhotoMessage service (TIM Click), and during 2003 it has enriched its multimedia portfolio by offering Java games (including Multiplayer) and Video.

In October 2003, TIM was the first mobile operator to launch mobile TV. The service is currently available only on a limited number of handsets (Nokia 3650/3660/6600 and Nokia N-Gage). The services contents are available pursuant to agreements between TIM and major TV channels such as RAI, La 7, MTV, CNBC and Coming Soon Television.

Billing. TIM s customers (other than Prepaid Customers) are billed in a staggered bimonthly billing cycle. TIM endeavors to minimize bad debts by implementing a credit check on each customer at the time of sign-up and by requiring certain customers to post a security deposit. In addition, if payment is not received, the customer is notified accordingly and his or her ability to place outgoing calls is interrupted. If no payment is received, all services are terminated. The average rate of innovative payments (credit cards, Banco Posta...) made by customers (other than Prepaid Customers) rose, in 2003, to 83% of the total payments.

Marketing and Distribution. TIM believes that its active marketing programs, extensive customer service and distribution network (primarily a nationwide network of independent dealers) and responsiveness to customer needs provide it with a significant competitive advantage. At December 31, 2003, there were 1,445 distribution partners, with 4,188 sales points (including 62 Telecom Italia Group outlets marketing TIM products and 27 shops directly owned by TIM). As of December 31, 2003, 4,191 TIM employees (about 41.8% of its total workforce) were involved in customer service activities.

Cellular Network. TIM s GSM network consists of 12,720 radio base stations and 651,544 radio channels (an increase of 3.4% over 2002). The Telecom Italia Group believes that as a result of TIM s enhancement of the GSM service and increased coverage, TIM s network is in line with the best European GSM networks. TIM s TACS network consists of 2,715 radio base stations and 40,090 radio channels. TIM has reduced the level of investment in its TACS network as the number of TACS customers has decreased.

Services International. TIM continued to consolidate its role in the international mobile market during 2003. TIM International s presence is now primarily concentrated in Latin America and in the Mediterranean

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Basin. In December 2003, in addition to customers in Italy, TIM had 18.4 million total managed lines in its subsidiaries abroad (including minorities), corresponding to 9.5 million proportionate lines (weighted for TIM s stake in each company). 45.3% of TIM s international lines are European mobile lines (other than Italian mobile lines) while 54.7% are Latin American mobile lines. See Companies Controlled by TIM International .

In-Europe , TIM s pan-European tariff, introduced in 2001, combines the preferential roaming agreements among TIM, its foreign subsidiaries and other European partners, allowing TIM customers to roam in 30 countries using the same tariff. As part of its international roaming service, TIM offers its customers the possibility of making calls from abroad with a simplified rate plan. Subscribers are allowed to use the same rates twenty-four hours a day and prepaid customers to charge the cost directly to their remaining credit rather than to a credit card. See Companies Controlled by TIM International .

On July 31, 2003, a cooperation agreement was signed as part of the alliance of TIM, Orange S.A., T-Mobile and Telefónica Móviles. The agreement established the context for developing widespread collaboration and to highlight the joint effort to provide an experience without borders to all customers in the geographical areas in which the companies operate.

The FreeMove alliance, which is initially operating in Europe in the primary service areas of the four mobile companies, will reach nearly 170 million customers in twenty one countries. Its goal is to expand and to include in the project all the activities of each company on a worldwide level.

The initial products and services provided will allow customers who use prepaid cards to utilize their mobile phones in a larger number of countries than is currently possible, enjoying their usual services e.g. voicemail and assistance even when traveling abroad. The service of recharging prepaid cards abroad will gradually become available. In addition, GPRS and MMS roaming will then become available in the leading countries in Western Europe. One of the objectives of the four operators is also to improve services for businesses.

The main goals of the alliance and the corresponding supporting actions are:

- increase roaming services and correlated voice and data traffic;
- reduce costs, leveraging on stronger purchase power towards suppliers;
- improve customer proposition by offering state-of-the-art/exclusive terminals for FreeMove Alliance members. Preferential supply agreements have already been signed with Siemens and Motorola;
- strengthen operators brand and positioning by means of higher quality service perception; and
- improve competitive positioning on the Multinational company market by offering one stop shop solutions.

The alliance s partners shall also guarantee roaming for third generation services within the end of the year.

TIM is focusing its efforts on becoming a technological and marketing partner for its affiliates. Examples of synergies implemented among TIM and affiliated companies are represented by the commercial launches of TIM Celular (formerly TIM Sao Paulo) in 2002 and TIM Perú in 2001. TIM s strategy for international development focuses on consolidation in countries where new markets have greater growth potential. Targeted countries include Brazil (for GSM services), Perú and Venezuela. These markets currently have low penetration rates and dense populations made up of young consumers who are more oriented towards value added services. See Companies Controlled by TIM International .

Holdings of International Operations

As a result of a corporate reorganization completed at the end of 2000, TIM acquired 100% of STET Mobile Holding (SMH), the international holding company of the Telecom Italia Group holding substantially all of the Telecom Italia Group s wireless investments outside of Italy. On December 28, 2001, SMH merged with TIM International, the holder of stakes in Digitel and Is TIM. TIM International is managed by TIM and the international results have been fully consolidated with TIM s results since January 1, 2001. In January 2001, TIM Brasil, a wholly owned subsidiary of TIM International, was formed to act as a sub holding company for the subsidiaries which acquired PCS licenses in Brazil (TIM Celular Centro Sul, TIM Sao Paulo and TIM Rio Norte). In November 2001, TIM International s stake in Bitel (the majority shareholder of Tele Nordeste Celular and Tele Celular Sul) was contributed to TIM Brasil. In December 2002, within the framework of the corporate reorganization process, TIM Sao Paulo was merged with TIM Celular Centro Sul and TIM Rio Norte and, in

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January 2003, changed its name to TIM Celular. In September 2003, Bitel Participaçoes merged its controlling company, TIM Brasil S.A., and changed its name to TIM Brasil Serviços e Participaçoes S.A. In December 2003, following the approval of the Boards of Directors of the Brazilian companies, owners of the 80% interest of Blah! S.A. - formerly TIMNet.com S.A. (Tele Nordeste Celular, Tele Celular Sul, Maxitel and TIM Celular), such stake has been sold to TIM International N.V., that became the sole owner of Blah! S.A.

Digitel and Maxitel, whose controlling stake was acquired at the end of 2000 have been fully consolidated with TIM s results since January 1, 2001.

At December 31, 2003, the overall number of TIM lines calculated on a proportionate basis, in Italy and internationally was approximately 35.6 million. There are approximately an additional 2.2 million equity mobile lines calculated on a proportionate basis that are part of the Telecom Italia Group.

The following tables list the countries in which TIM (through TIM International) currently has operations, the ownership interest in each operator and the number of lines for each operator. Until February 29, 2004, all the Latin America companies owned by TIM International were coordinated by Latin America Operations. Starting from March 1, 2004, the Latin America Operations function is no longer operational (please see South America for further details).

Controlled Operations

Country	Operator	Percentage interest of TIM International	Total Wireless lines per operator at December 31, 2003
			(millions)
Europe			
Greece	STET Hellas	81.40	2.4
Latin America			
Brazil	Maxitel		
	Tele Nordeste	100.00(1)	1.6
	Celular(*) Tele	22.52(2)	2.2
	Celular Sul(*)	22.21(3)	2.1
	TIM Celular	100.00	2.5
Perú	TIM Perú	100.00	0.6
Venezuela	Digitel	67.12(4)	1.2

(*) Represents total of shares held; these entities are consolidated as the Group owns over 50% of the voting common stock.
(1) In February 2002, TIM Brasil acquired 10% of ordinary shares of Maxitel, corresponding to 3.33% of the total capital.
(2) During 2003, the interest in Tele Nordeste Celular increased by 1.34%.
(3) During 2003, the interest in Tele Celular Sul increased by 1.53%.
(4) In May 2003, TIM International increased its interest in Digitel, through a share capital acquisition, by 0.56%. On April 20, 2004, TIM signed an agreement to acquire the remaining 32.88% of Digitel s share capital from its minority shareholders. Upon completion of the transaction, TIM International will own 100% of Digitel s share capital. See Recent Developments During 2004 TIM s stake in Digitel .

Affiliated Companies

Country	Operator	Percentage interest of TIM International	Total Wireless lines per operator at December 31, 2003
			(millions)
Europe			
Czech Republic	T-Mobile CZ (formerly Radiomobil)	4.35	3.9
Turkey	Aria Is TIM	40.00(1)	2.0

(1) On February 19, 2004, Is TIM was merged with Aycell. The new company (TT&TIM) resulting from the merger is currently held by TIM International (40%), Turk Telekom (40%) and by the Is Bank group (20%). Please see below Other investments held by TIM International Turkey .

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Companies Controlled by TIM International

Europe

Greece

The Telecom Italia Group s first international investment in Western Europe was the establishment of STET Hellas. STET Hellas was awarded one of two GSM licenses granted in Greece, in the 900 Mhz frequency band, and commenced commercial services in June 1993.

In July 2001, the company was awarded a UMTS license, for 145 million (of which approximately 101 million has already been paid) and a DCS 1800 license for 26 million. At December 31, 2003, STET Hellas had approximately 2.4 million lines. In 2003, operating revenues were 805 million against 689 million in 2002, gross operating profit was 287 million compared to 255 million in 2002 (a 12.5% increase) and operating income was 166 million against 131 million in 2002 (an increase of 26.7% compared to 2002). The improvement in the economic performance was due to the increase of the revenues, mainly due to significant growth in outgoing traffic.

In January 2004, STET Hellas commercially launched UMTS services in Greece. STET Hellas also announced, in February 2004, the change of its commercial brand to TIM. The adoption of the re-branding is a joint strategic initiative of STET Hellas and TIM to strengthen the image of the Greek operator.

STET Hellas was listed on NASDAQ and on the Amsterdam Stock Exchange in June 1998 through an initial public offering of American Depositary Shares on NASDAQ and of Dutch Depositary Receipts on the Amsterdam Stock Exchange. After completion of the initial public offering, the Telecom Italia Group s stake through TIM International was reduced from 74.8% to 58.14%. In February 2001, a stake of 1.14% was acquired by TIM International. In October 2001, TIM International subscribed to a capital increase to finance the acquisition of its new business, and its stake rose to 63.95%. In August 2002, TIM International acquired the 17.45% stake of Verizon, its original joint venture partner. Consequently, the TIM group s interest in STET Hellas is now 81.40%.

Latin America

Brazil

In 2001, TIM Brasil (a wholly owned subsidiary of TIM International) was incorporated to act as a sub holding company for TIM Celular Centro Sul, TIM Sao Paulo and TIM Rio Norte. In November 2001, TIM International s stake in Bitel (the majority shareholder of Tele Nordeste Celular and Tele Celular Sul) was contributed to TIM Brasil. Consequently, TIM Brasil remained the holding company for all the Brazilian subsidiaries. In September 2003 Bitel Participaçoes S.A. merged with the controlling company TIM Brasil and changed its name to TIM Brasil Serviços e Participaçoes S.A.. In December 2003, following the approval of the Boards of Directors of the Brazilian companies holding an 80% interest of Blah! S.A. formerly TIMNet.com S.A. (Tele Nordeste Celular, Tele Celular Sul, Maxitel and TIM Celular), such stake was sold to TIM International N.V., that became the sole owner of Blah! S.A..

Tele Nordeste Celular Participaçoes group. A controlling interest in Tele Nordeste Celular Participaçoes, a supplier of mobile telephone services in the regions of Alagoas, Cearà, Paraiba, Pernambuco, Piaui and Rio Grande do Norte, was acquired in 1998. At the end of 2003, in a market with a penetration level of 16%, Tele Nordeste had 2.2 million lines (an increase of 12.8% compared to 2002), corresponding to a market share of approximately 47%.

In 2003, Tele Nordeste Celular reported operating revenues of Brazilian reais 1,080 million (311 million), an increase of 9.8% in local currency compared to 2002; gross operating profit of Brazilian reais 509 million (147 million), a decrease of 2.7% in local currency compared to 2002; and operating income of Brazilian reais 279 million (80 million), an increase of 3.0% in local currency compared to 2002.

Tele Celular Sul Participaçoes group. A controlling interest in Tele Celular Sul Participaçoes, a mobile telephone operator in the states of Paranà, Santa Caterina and in the city of Pelotas, was acquired in 1998. In 2003, Tele Celular Sul had 2.1 million lines (an increase of 19.3% compared to 2002) representing an overall market share of 55%. In 2003, Tele Celular Sul reported operating revenues of Brazilian reais 1,202 million (346 million), an increase of 19.0% in local currency compared to 2002; gross operating profit of Brazilian reais 486 million (140 million), an increase of 15.2% in local currency compared to 2002; and operating income of Brazilian reais 245 million (71 million), an increase of 27.6% in local currency compared to 2002.

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Maxitel. In November 2000, TIM, through Bitel Participaçoes, acquired from UGB Participaçoes S.A. and Vicunha S.A., respectively, 19.43% and 18.53% of the ordinary and preferred shares of Maxitel, the Brazilian mobile telephony operator licensee in the states of Minas Gerais, Sergipe and Bahia in which it already held a 58.7% interest (43.15% of ordinary share capital). The transaction involved a total investment of approximately U.S.$240 million.

In February 2002, TIM International, through its wholly owned subsidiary TIM Brasil S.A., acquired from the minority shareholders UGB Participaçoes S.A. and Vicunha S.A. the remaining 10% of Maxitel ordinary shares for the equivalent of 27 million by exercising a call option.

At the end of 2003, Maxitel had 1.6 million lines (an increase of 15.4% compared to 2002).

In 2003, Maxitel reported operating revenues of Brazilian reais 890 million (256 million), an increase of 17.9% in local currency compared to 2002, due to an increase in traffic; gross operating profit of Brazilian reais 316 million (91 million), an increase of 7.8% in local currency compared to 2002. Operating income was Brazilian reais 62 million (18 million).

TIM Celular. On February 13, 2001, TIM s subsidiaries TIM Sao Paulo and TIM Celular Centro Sul acquired PCS licenses in Brazil respectively in the regions of São Paulo and in the Districto Federal, in the middle/west and south region. On March 13, 2001, TIM Rio Norte acquired PCS licenses in the Northern and in the Rio de Janeiro and Espirito Santo states. On October 18, 2002, the three companies launched GSM services. In December 2002, within the framework of the corporate reorganization process, TIM Sao Paulo merged with the other two companies and, in January 2003, changed its name to TIM Celular.

The company operates mobile network services using GSM technology in the north of Brazil, in the middle/west and south region and in the states of São Paulo, Rio de Janeiro and Espirito Santo and in the Districto Federal.

At the end of 2003, TIM Celular had 2.5 million lines. In 2003, TIM Celular reported operating revenues of Brazilian reais 1,258 million (362 million); a loss in gross operating profit of Brazilian reais 833 million (240 million) compared to a loss of Brazilian reais 472 million in 2002; and an operating loss of Brazilian reais 1,278 million (368 million) compared to a loss of Brazilian reais 521 million in 2002.

Perú

In March 2000, TIM Perù was awarded the third mobile PCS license in the country at a cost of US$180 million. The license has a duration of 20 years, is renewable, and provides for the supply of mobile telecommunications service on the 1900 MHZ frequency band. The license permits TIM Perú to request licenses for supplementary services, including basic and long distance telephone services. These licenses were obtained in March 2001 and October 2001.

The Telecom Italia Group has elected to use GSM technology for its mobile services in Perú consistent with the development of a Latin American platform and GSM roaming worldwide.

At the end of 2003, TIM Perù had 623,000 lines (an increase of 57.7% compared to 2002).

In 2003, TIM Perú reported operating revenues of 502 million Nuevo Soles (128 million), a gross operating profit of 26 million Nuevo Soles (6 million) and an operating loss of 128 million Nuevo Soles (32 million) against an operating loss of 201 million Nuevo Soles (61 million) in 2002.

Venezuela

In December 2000, TIM acquired a 56.6% stake in Digitel, a Venezuelan mobile operator. The amount paid for this acquisition was approximately US$363 million (of which approximately US$107 million was in the form of a capital increase and the balance was in the form of a share purchase). In December 2002, TIM International acquired a further 10% of Digitel s share capital for 32 million. In May 2003 TIM International acquired a further 0.56% of the company shares, consequently, as of December 31, 2003 the TIM group s interest in Digitel increased to 67.12%. Digitel was awarded a 900 MHZ 20-year renewable GSM license in January 1998 and is operating in the Venezuelan Central Region, which, including Caracas and other major cities, is the most important economic region of Venezuela, with 60% of the national GDP.

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In 2002, Digitel changed its network architecture with the choice of Nokia as a main supplier, updated its technologies for prepaid services and launched GPRS and MMS services.

At the end of 2003, Digitel had approximately 1.2 million lines (an increase of 29% compared to the end of 2002).

In 2003, Digitel reported operating revenues of 299 billion Bolivares (148 million), an increase of 14.7% in local currency against operating revenues of 260 billion Bolivares in 2002; gross operating profit of 90 billion Bolivares (45 million) compared to 51 billion Bolivares in 2002; and an operating loss of 20 billion Bolivares (10 million), an improvement of 34.5% against an operating loss of 30 billion Bolivares in 2002.

For further details about pending litigation and other developments relating to Digitel and TIM International, pleaase see Events subsequent to December 31, 2003 and Item 8. Financial Information Legal Proceedings for further details.

Other investments held by TIM International

Czech Republic

The Telecom Italia Group holds a 7.16% interest in C-Mobil B.V., a company which owns a 60.76% interest in T-Mobile CZ (previously known as Radiomobil), a mobile telecommunications operator, which in March 1996 won a GSM license in the Czech Republic.

As of December 31, 2003, T-Mobile CZ had more than 3.9 million customers. T-Mobile CZ had operating revenues of 768 million and gross operating profit of 339 million in 2003.

Turkey

In line with its expansion strategy in the Mediterranean Basin, in April 2000, the Telecom Italia Group was awarded a mobile GSM 1800 license in Turkey. This license was acquired, at a price of US$ 2,525 million, through a special consortium (49% owned by Telecom Italia and 51% by Is Bank, the leading private bank in Turkey, in compliance with restrictions imposed by local laws about foreign investments). The second license was awarded to the fixed network operator (Turk Telekom) at the same time, according to the terms of the bid.

In September 2000, the Telecom Italia Group and Is Bank formed Is TIM, that, under the brand name Aria , launched GSM services on March 21, 2001. According to the agreements with Is Bank, TIM was responsible for the technical and commercial operation of Is TIM. In December 2000, 49% of Is TIM was transferred to TIM International B.V. (now TIM International N.V.).

At the end of 2003, Aria Is TIM had a customer base of approximately 2 million lines and it reported operating revenues of 211,013 billion Turkish lire (121 million) and an operating loss of 759,490 billion Turkish lire (435 million). These results are due to the consequence of the difficulties faced by Aria Is TIM in developing its mobile business, because of the Turkish regulatory scenario. In fact beginning with the award of the license, some measures which should have fostered effective competition and permitted a new entrant to compete against incumbent operators (roaming arrangements in particular), did not effectively take place. These measures are essential in the light of international experience to foster competition and pursuant to applicable legislation in Turkey. Aria Is TIM and its shareholders made repeated and formal efforts to have the situation rectified but was de facto prevented from entering the Turkish mobile telephony market, thereby infringing the terms and conditions of the tender. Aria Is TIM filed a request for arbitration with the International Chamber of Commerce against the authority for telecommunications which, as a result of the joint venture with Turk Telecom described below, has since been discontinued.

From a financial standpoint, at the end of 2002, Telecom Italia, in conjunction with TIM, concluded that the competitive conditions which would permit TIM to earn a return of investment did not exist. Facing this situation Telecom Italia and TIM wrote off their investment in Aria Is TIM in full. The investment held in Aria Is TIM was written down (extraordinary loss of 1,491 million) and a provision was added to the reserve for risk and charges related to Aria Is TIM (850 million) against the guarantees provided by the Telecom Italia Group to financial institutions and suppliers as creditors of Aria Is TIM and the loans to Aria Is TIM by the Telecom Italia Group.

On May 13, 2003, TIM International signed a Term Sheet with Turk Telekom (the fixed line operator) outlining a set of guidelines for the integration of Aria Is TIM and Aycell (the 4th Turkish mobile operator

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wholly owned by Turk Telekom). The agreement aims at obtaining significant operating and financial synergies through the combination of the two companies. On February 19, 2004, the merger of Aria - Is TIM with Aycell was completed after receipt of required regulatory approvals. Turk Telekom and TIM hold a 40% stake in the new company and Is Bank Group holds the remaining 20%. Together the two companies have a joint customer base of about 4.5 million customers representing 15% of the total market, and the ambition of TT&TIM, which will start to operate under the two brands of Aria and Aycell, is to compete for the leading position on the Turkish market.

Financial data of the main subsidiaries/affiliated companies

The following table sets forth operating revenues, gross operating profit and operating income for the main national and international subsidiaries/affiliated companies of the Mobile Business Unit on a stand alone basis. The financial data will not tie directly to consolidated segment data due to intercompany, consolidation and other adjustments.

		National Subsidiaries		Affiliated Companies	
		TIM		IS TIM T.H.A.S.	
		Historical	Pro Forma (1)		
		Millions of Euro		Millions of Euro	Billions of Turkish lire
Gross operating revenues	2003	9,469	8,915	121	211,013
	2002	9,022	6.2	83	141,276
	Change (%)(2)				49.4
Gross operating profit	2003	5,035	4,529	(83)	(144,814)
	2002	4,404	11.2	(122)	(207,609)
	Change (%)(2)				30.2
Operating income	2003	3,863	3,323	(435)	(759,490)
	2002	3,153	16.3	(420)	(715,735)
	Change (%)(2)				(6.1)

(1) Pro forma income statement data are net of effects arising from the incorporation of Blu.
(2) Percentage calculation based on pro forma 2002 compared to historical 2003.

	International Subsidiaries	
	Mobile South America	Other

(million)		Tele Nordeste Celular Participaçoes Group		Tele Celular Sul Participaçoes Group		Maxitel S.A.		TIM Celular S.A.		TIM Perù S.A.C.		Corporacion Digitel C.A.		subsidiaries STET Hellas Telecommunications Group
			Reais		Reais		Reais		Reais		Nuevo Soles		Bolivares	
Gross operating revenues	2003	311	1,080	346	1,202	256	890	362	1,258	128	502	148	298,681	805
	2002	355	984	364	1,010	273	755	39	108	93	308	177	260,378	689
	Change(%)		9.8		19.0		17.9				63.0		14.7	16.8
Gross operating profit	2003	147	509	140	486	91	316	(240)	(833)	6	26	45	90,207	287
	2002	189	523	152	422	106	293	(170)	(472)	(29)	(95)	35	51,355	255
	Change(%)		(2.7)		15.2		7.8		(76.5)				75.7	12.5
Operating income	2003	80	279	71	245	18	62	(368)	(1,278)	(32)	(128)	(10)	(19,702)	166
	2002	98	271	69	192	27	74	(188)	(521)	(61)	(201)	(20)	(30,070)	131
	Change (%)		3.0		27.6		(16.2)				36.3		34.5	26.7

Major 2003 corporate events/scope of consolidation

On March 28, 2003, STET Hellas acquired from IT Telecom S.p.A. the full stake in Telesoft Hellas S.A., a company that developed software for telecommunications, and, as of November 14, 2003, merged it into STET Hellas.

On September 26, 2003, TIMNet.com S.A. changed its name to Blah! S.A., thus completely identifying the name of the company with its commercial trademark.

On September 30, 2003, the merger of TIM Brasil S.A. and Bitel Participaçoes S.A. became effective. The acquiring company took the name of TIM Brasil Serviços e Participaçoes S.A. (in shortened form, TIM Brasil). The transaction is part of the process currently underway to simplify the Group structure.

In December 2003, following the approval of the Boards of Directors of the Brazilian companies, owners of the 80% interest of Blah! S.A. - formerly TIMNet.com S.A. (Tele Nordeste Celular, Tele Celular Sul, Maxitel and TIM Celular), such stake was sold to TIM International N.V., that became the sole owner of Blah! S.A..

Events subsequent to December 31, 2003

TIM s stake in Digitel

On April 19, 2004, TIM International agreed to settle several lawsuits between TIM International and all the other shareholders of Digitel. The lawsuits concerned the covering (which was performed in 2003) of losses for the fiscal year 2002. According to the terms of the settlement, TIM International agreed to acquire the shares held by all the other shareholders (corresponding to 32.88% of Digitel s share capital) for U.S.$110 million. As a consequence of the settlement, TIM International will have total control of the Venezuelan company. The effectiveness of the settlement is subject to certain conditions, the most important of which are: the waiver by all the other shareholders to any further request or lawsuit against TIM/Digitel, and the dismissal of the arbitration proceeding initiated in New York (under the International Chamber of Commerce s rules) between TIM International and Venconsul. The difference between the fair market value of the shares to be acquired and the acquisition price agreed to in the settlement has been covered by a reserve for risks and charges.

Merger of the Tele Nordeste Celular Participações group companies and rationalization of the Brazilian subsidiaries

On January 30, 2004, the extraordinary Shareholders Meeting approved the merger of the operating companies controlled by Tele Nordeste Celular (Telasa Celular, Telpa Celular, Telern Celular, Teleceará Celular and Telepisa Celular) by Telpe Celular. As a result, Telpe Celular s name was changed to TIM Nordeste Telecomunicações S.A..

The objective of the merger of the operating companies by Telpe Celular was to integrate the activities of the six operating companies that pertain to a same business group, taking advantage of synergies, allowing for the expansion of Telpe Celular s operations, reducing expenses relating to maintaining six distinct legal structures and concentrating the liquidity of shares of operating companies controlled by Tele Nordeste Celular.

On May 28, 2004, the Boards of Directors of Tele Celular Sul Participações and Tele Nordeste Celular Participações (both controlled by TIM Brasil) approved the commencement of a transaction for the merger by incorporation of Tele Nordeste Celular Participações into Tele Celular Sul Participações. The shares of both companies are traded on the Sao Paolo Stock Exchange (Bovespa) and on the NYSE (in the form of ADRs, or American Depositary Receipts).

The merger envisages the issue of new shares by Tele Celular Sul Participações which will be assigned, with the same class designation, to the shareholders of Tele Nordeste Celular Participações. The merger will be notified to the Agencia Nacional de Telecomunicaçoes (Anatel) in Brazil and the new shares will need to be registered with the SEC. At the end of the transaction, Tele Celular Sul Participações will be controlled by TIM Brasil and its shares will continue to be listed on both the Bovespa and the NYSE.

Merger of Aria Is Tim

On February 19, 2004, the merger of Aria Is Tim the mobile operator owned by TIM (49%) and Is Bank Group (51%) with Aycell, the GSM operator entirely held by the state owned fixed-line operator Turk Telekom, was completed.

The integration process, which began last May with the execution of an agreement establishing the guidelines for the merger of Aria Is Tim and Aycell, was completed after all the approvals of the relevant Authorities were obtained.

TIM and Turk Telekom own a 40% stake in the new company (TT&TIM) each and Is Bank Group holds 20%.

Today the two companies have a joint customer base of about 4.5 million customers representing 15% of the total market, and the ambition of TT&TIM, which will start to operate under the two brands of Aria and Aycell, is to compete for the leading position on the Turkish market.

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Acquisition of Innovative Services Business Segment

The sale by IT Telecom S.p.A. of its Innovative Services Business Segment to TIM S.p.A. was completed as of April 1, 2004; the activities of this business segment are conducted in the innovative services field, based on IP networks and oriented towards the business and mass-market sectors, and they are related to the development and maintenance of software for telecommunications. The sale price, based on an evaluation by Milestone Advisory House S.p.A., was agreed at 23 million, 551 staff units were also transferred.

Contribution of Specialized Business Software Segment

In March 2004, under Telecom Italia Group s program for information technology, TIM contributed a business segment which develops and maintains software applications in the SAP environment to the company Shared Service Center, a limited liability consortium company. The value of the business segment was determined by an expert appointed by the Milan Courts at 65 thousand.

South America

All the activities conducted by the Latin American subsidiaries (whether controlled by Telecom Italia International or by TIM International) were coordinated by Latin America Operations (LAO) until February 29, 2004 and were developed in accordance with the Telecom Italia Group s overall strategic plan. From February 2003 to February 2004, Latin America Operations reported directly to the CEO Carlo Buora for Wireline telecommunication, and to Marco De Benedetti for Mobile telecommunications. Since March 1, 2004, the Latin America Operations function is no longer operational and the Business Units have been given responsibility for the results of the subsidiaries for which they are accountable in Latin America. In particular, the Wireline and Mobile Business Units have been given responsibility for the results and the day-to-day operations of the wireline and mobile operations, respectively, of such subsidiaries.

As of December 31, 2003, LAO was organized as follows:

LATIN AMERICA OPERATIONS		
Subsidiaries		**Affiliated**
• TIM Brasil Group	• Entel Chile Group	• Telecom Argentina Group
• TIM Perù S.A.C.	• Entel Bolivia Group	
• Corporacion Digitel C.A. (Venezuela)	• Telecom Italia America Latina	

A description of the companies providing mobile services (TIM Brasil group, TIM Perù and Corporacion Digitel) is provided under Mobile Companies Controlled by TIM International Latin America .

International Strategy in Latin America

The Telecom Italia Group s international strategy in Latin America has the following objectives:

- consolidate the Telecom Italia Group s presence in mobile and in the fixed-mobile integrated business;
- maximize return on investments and focus on sustainable growth;
- invest in high-growth market segments, such as wireless, data and broadband, through the creation of a common GSM platform and through the launch of VAS services based on state-of-the-art technologies that provide synergies to the Telecom Italia Group;
- enhance the value of shareholdings, maximizing efficiency and cash cost control particularly on legacy services; and
- strengthen its role of strategic partner in the current operations by increasing the transfer of the Telecom Italia Group s technological expertise and marketing know-how.

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Latin America Companies Controlled by Telecom Italia International

Chile

Telecom Italia International has a 54.76% stake in Entel Chile which was until 1994 the monopoly long distance operator in Chile. During the last ten years the Entel Chile Group has significantly enlarged its activities becoming a full operator maintaining its leadership positioning in the long distance segment while introducing mobile services, through its two PCS licenses acquired in 1998, as well as local, internet and data services.

Since introducing mobile services, Entel Chile has achieved the leading position in wireless telecommunications with a 40.5% market share representing approximately 2,684,000 mobile lines at the end of 2003 (an increase of 17.1% compared to 2002).

Consolidated operating revenues during 2003 were 962 million representing a significant decline (a decrease of 21.3%) against 2002. During this same period the Chilean peso declined in value by 19.8% against the Euro. In local currency terms Entel Chile also recorded a decrease in revenues of 5.8% due to a sharp decline in the wireline segment (a decrease of 15.5%), mainly due to the negative performance of long distance operator Americatel (an affiliate of the Chilean Group in the USA) which has been negatively impacted by the unexpected strengthening of the competitive position of the Competitive Local Exchange Companies (CLECs), and the continuous growth of mobile revenues (an increase of 6.4%).

During the last two years the Company has focused on reducing costs and capital expenditures levels, seeking to improve its margins as well as growth in profitability and cash generation.

The operating profit of 2003 reached 134 million, an increase of 5.7% against 2002 in local currency; return on investments (ROI) reached 10.5% at the consolidated level, and net financial debt was reduced by 22.3%, lowering the debt ratio (net financial debt/net invested capital) to 40% (48% in 2002).

During the second half of 2003, Chile began to show higher Gross Domestic Product (GDP) growth rates implying better demand expectations for 2004 and also taking account of the overall stable political situation. Nevertheless, mobile tariff regulation (January 2003) implies a negative impact on wireless revenues, due to a decrease in access charges to the mobile networks of around 30%, which will be offset only partially by traffic demand elasticity (calls from the fixed network), price increases and growth of mobile VAS revenues.

During 2002, Entel Chile launched a WLL (Wireless Local Loop) business in order to penetrate the growing broadband market. However, during 2003, Entel Chile faced significant competition in broadband from the CATV (Cable TV) operators, as well as the ADSL offer of the incumbent (now Telefonica Chile). The Entel Chile Group within its wireline activities is still considering how to cope appropriately with its lack of local access.

Bolivia

Telecom Italia International holds indirectly a 50% stake in Entel Bolivia, the Bolivian national long distance and international telephony operator, which was acquired in 1995. Local regulations established that until November 2001, when liberalization of the market began, long distance telecommunications services would be provided by Entel Bolivia under a monopoly system. In 2001 complete deregulation of the telecommunication market took place, carrier selection was introduced and local access, previously in the exclusive hands of cooperatives, was liberalized.

During 2003, operating revenues were 151 million, a decrease of 18.8%, primarily attributable to the weakening of the Bolivian currency against the euro, although revenues in local currency increased by 4.1%. Revenue growth was mainly driven by the mobile business (an increase of 23.5%) where the company maintains its strong market leadership (75%), while the wireline business registered a decrease of 10.8% due to the general market contraction related to an unstable political and economic environment during the course of 2003, as well as to aggressive competition.

An efficiency plan applied to both operating and capital expenditures together with a significant reduction of the interconnection costs resulted in important improvements in productivity and profitability. The 2003 gross operating profit was 71 million or 26.6% over 2002 and 47% over revenues.

As of December 31, 2003, Entel Bolivia had 783,000 mobile lines, up 69.5% from the end of 2002, and 49,000 fixed lines subscribers, substantially stable when compared with 2002.

Latin America Affiliated Companies

Nortel Inversora

In December 2003, the France Telecom Group and the Telecom Italia Group contributed their respective stakes in Nortel (corresponding in total to 67.78% of its capital) to a new Argentinean registered holding company, Sofora Telecomunicaciones S.A. which had been organized in September 2003 and was held 50% by the Telecom Italia Group and 50% by the France Telecom Group. On December 19, 2003, France Telecom transferred to the Werthein Group (Argentinean Group) a 48% stake in the Sofora Telecomunicaciones share capital for U.S.$125 million, including a call option on the remaining 2%, exercisable from January 31, 2008 to December 31, 2013. In order to discipline their relationship, Telecom Italia, Telecom Italia International and Werthein Group executed a shareholders agreement. Moreover, Telecom Italia International purchased from Werthein Group two call options for U.S. $60 million. The first one for the purchase of 48% of Sofora Telecomunicaciones share capital which can be exercised within 30 business days after December 31, 2008, and the second one for the purchase of an additional 2% of Sofora Telecomunicaciones share capital, which can be exercised between December 31, 2008 and December 31, 2013.

The current interest of 50% the Telecom Italia Group holds in the Nortel ordinary share capital (through Sofora Telecomunicaciones) is the result of acquiring an initial share of 32.5% in 1990 for approximately U.S.$33 million and a further share of 17.5% in August 1999 for approximately U.S.$265 million.

Nortel currently owns 54.74% of Telecom Argentina, which until October 1999 operated the telecommunications network in the northern part of Argentina (including Buenos Aires) among others, fixed-line and mobile telecommunications operations, international services, data transmission services, value-added services and directories publishing. Since October 1999, the Argentinean market has been progressively liberalized, and as a consequence of this Telecom Argentina has expanded its operations to the entire national territory. In June 1999, Telecom Argentina also expanded its mobile telecommunications services, by acquiring new licenses in the PCS technology, for a total amount of U.S.$327 million.

At the end of 2003, Telecom Argentina had accumulated 3.3 million fixed-line network subscribers. Its subsidiary Telecom Personal (including Nucleo Paraguay) which is a leading company in the wireless segment (both in revenues and customers), accumulated more than 3.1 million mobile lines (81% with prepaid cards), with a market share of 34% in Argentina. The group is moving to GSM technology with an investment of U.S.$26 million during 2003.

In the Internet sector, there were approximately 200,000 subscribers (155,000 access clients and 45,000 broadband clients with a market share of 19%).

During 2003, the Argentine economy recovered partially from the significant economic decline which occurred during 2002. As a result, Telecom Argentina s fixed clients increased by 2% compared to December 2002. The mobile segment recovered strongly during 2003, both in traffic terms (an increase of 21%) and clients (an increase of 15%). However, the partial political economic recovery was due to growth in the international environment (particularly high commodity prices and low interest rates) and not to structural changes in the country. The country remains in default, negotiating with the International Monetary Fund (IMF) and its private creditors. Negotiations with the national government on applicable tariff to fixed telephony is pending.

As a result of the economic recession in February 2002, Telecom Argentina hired Morgan Stanley as financial advisor to explore restructuring alternatives to reduce its outstanding debt. Telecom Argentina defaulted on certain indebtedness in April 2002 and stopped paying interest on its debt in June 2002. As part of its restructuring plan, during 2003, based on a voluntary tender offer that terminated on June 2, 2003, (with a subscription rate of 44%), Telecom Argentina repurchased U.S.$292 million principal amount of its debt using cash of U.S.$161 million at a price of 55% of face value. In addition Telecom Argentina paid the full amount of the interest accrued as of June 24, 2002 and 30% of the interest accrued from June 25, 2002 to December 31, 2002.

On January 9, 2004, Telecom Argentina announced its proposal for a comprehensive restructuring of all of its outstanding unsecured financial debt. Telecom Argentina proposes to implement its proposal pursuant to an Acuerdo Preventivo Extrajudicial , or an out-of-court restructuring agreement governed by Argentine law (APE).

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Under the proposal, Telecom Argentina proposes to restructure all of its outstanding unsecured financial debt by issuing new unsecured notes with new terms and/or by paying cash consideration in accordance with the different options included in the proposal. The proposal has been filed with the relevant authorities in Argentina, USA and Italy in May; once due authorizations and clearance are received, solicitation for creditors consent to the restructuring will start.

In 2003, Telecom Argentina continued to implement a cost and investment optimization process in order to improve cash flow. The use of this strategy is expected to continue for the foreseeable future.

In 2003, the Telecom Argentina group recorded consolidated operating revenues of Argentine Pesos 3,746 million (1,123 million). The gross operating profit was Argentine Pesos 2,218 million (665 million) and the operating income was Argentine Pesos 281 million (84 million).

Financial data of the main subsidiaries/affiliated companies

The following table sets forth operating revenues, gross operating profit and operating income for the main subsidiaries/affiliated companies of the South America Business Unit on a stand alone basis. The financial data will not tie directly to consolidated segment data due to intercompany, consolidation and other adjustments.

		Subsidiaries				Affiliated	
(million)		**Entel Chile Group**		**Entel Bolivia Group**		**Telecom Argentina Group**	
			Pesos		**Bolivians**		**Pesos**
Gross operating revenues	2003	962	750,980	151	1,312	1,123	3,746
	2002	1,223	797,171	186	1,260	1,127	3,983
	Change (%)		(5.8)		4.1		(6.0)
Gross operating profit	2003	336	262,344	71	615	665	2,218
	2002	381	248,256	72	489	684	2,417
	Change (%)		5.7		25.8		(8.2)
Operating income	2003	134	104,289	11	97	84	281
	2002	151	98,678	2	15	1	2
	Change (%)		5.7				

Major 2003 corporate events/scope of consolidation

During 2003, the Telecom Italia Group, through Telecom Italia International (the primary vehicle by which the Telecom Italia Group holds its international wireline and integrated mobile/fixed-line investments), continued pursuing its targets, supporting the growth of its majority owned subsidiaries and focusing on rationalization of other investments.

The following key transactions were finalized during 2003:

- In January 2003, the Telecom Italia Group disposed of its stake (28.57%) held in GLB Servicos Interativos (Globocom) to TVGlobo LTDA for a consideration of U.S.$ 15 million. As a result of such transaction, the Telecom Italia Group realized a net gain of 4 million.

- In September 2003 and December 2003, the reorganization of the share ownership structure of Nortel. See Latin America Affiliated Companies Nortel Inversora.

Events subsequent to December 31, 2003

Effective March 1, 2004, under the plan to consolidate Telecom Italia s presence in Latin America, Latin America Operations was disbanded and Telecom Italia Latam assumed the role of delocalized corporate office at continental level in Latin America.

Internet and Media

During 2003, the Internet and Media Business Unit was significantly reorganized as a result of the spin-off and sale of New SEAT through which Telecom Italia disposed of its directories, directories assistance and business information business segments of the SEAT group. As a result of this disposition the remaining

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businesses of the Internet and Media Business Unit, now held through Telecom Italia Media, provide access and content services to retail and business customers through the Internet, television and telephone.

Starting from August 8, 2003, the Internet and Media Business Unit operates in the following segments: internet services, television, office products and services and business information and professional publishing.

As of December 31, 2003, the Business Unit is organized as follows (the table shows the main companies/consolidated activities):

INTERNET AND MEDIA				
INTERNET	**TV**	**NEWS**	**OFFICE PRODUCTS**	**PROFESSIONAL PUBLISHING**
Tin.it Matrix	Holding Media e Comunicazione Group	TM News (*)	Buffetti Group CiPi (**)	GPP

* Purchased on September 30, 2003.
** Sold on January 29, 2004.

Internet Services

Telecom Italia Media offers a full range of Internet services, consisting of:

- internet access services;
- portal services;
- on-line advertising services; and
- web services.

Internet Access Services

Through Tin.it, Telecom Italia Media provides Internet access services to residential, SOHO and SME Internet users. The SOHO market consists of businesses that use telephone lines to connect to the Internet, as opposed to dedicated lines, and is made up of small businesses, generally with one or two employees, and businesses conducted out of the home. The SME market consists of businesses having between 3 and 50 employees.

Tin.it offers two principal access subscription plans:

- free access (Tin.it Free); and
- premium access (dial-up, ISDN and ADSL access).

At December 31, 2003, Tin.it s subscriber base amounted to approximately 2.5 million active users (defined as users who connect to the Internet at least once every 45 days).

Million	**2001**	**2002**	**2003**
Active users(1)	1.8	2.2	2.5

(1) Active users include Telecom Italia s ADSL Alice subscribers to whom Tin.it provides certain services.

During 2003, Telecom Italia Media enhanced its Tin.it brand and range of products, developing, in particular, the ADSL connection based on usage. This enhancement marked an increase in the customer base (Alice, ADSL of Telecom Italia, +Tin.it).

Portal Services

Telecom Italia Media provides portal services through Matrix, which operates the Virgilio portal.

Virgilio is a leading Italian portal, with approximately 6.6 billion web page views in 2003 and approximately 5.3 billion web page views in 2002, that caters to the Italian speaking community on the Internet.

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Management believes that Virgilio, which has been on-line since July 1996, is one of the most complete Italian portals. It contains a search engine and a websites index, and it centralizes services in various interest areas such as stock quotes, weather forecasts, TV guides, games, chats advertisements and shopping. In order to simplify the use of information, Virgilio offers personalized, interactive services that correspond to the requirements of individual customers.

In 2003, Virgilio launched the new version of Virgilio Ricerca with a significant increase in traffic and turnover. Product innovation is one of the most important basis for future evolution of Virgilio and it represented the primary focus for investment during 2003.

Virgilio Viaggi , the on-line travel agency, was entirely renewed and launched just before summer 2003 with increasing levels of traffic and advertisement.

On-line Advertising Services

Matrix s division *Active Advertising* is a leading on-line advertising agency in Italy and has arrangements with approximately 20 Italian websites to provide advertising services.

Web Services

Telecom Italia Media provides web services through Tin.it and Matrix Communication.

Television

Telecom Italia Media provides television services through Holding Media e Comunicazione S.p.A. which holds the broadcasting licenses for La7 and MTV Italia.

La7 provides news information on a 24-hour basis, and is currently cooperating with the Internet Services business segment to provide on-line news information through the use of video-streaming technology. La7 started broadcasting under an all news format on March 18, 2002.

MTV Italia is a television channel providing music programs on a 24-hour basis. The brand MTV is a well known brand in the music industry and in the television network business. MTV Italia started broadcasting its programs on May 1, 2001.

During 2003, the broadcaster La7 sought to consolidate its editorial image, its brand awareness and its programs. In particular, La7 is now perceived as a high-quality broadcaster and its Auditel audience ratings are now regularly over 2% (1.8% for the same period last year). Over the same period, MTV continued to reign as Italy s premier youth television channel, with increasing revenues (an increase by 25.5% from 51 million in 2002 to 64 million in 2003) and an operating profit, after the operating loss recorded in 2002. Growth in gross advertising sales for television segment (La7 and MTV), increased by approximately 40% compared to 2002.

In late 2003, LA7 and MTV began digital terrestrial television trials in the main cities in Italy. By March 2004, a total of 4,000 households selected by specialist companies took part in trials. In observance of company plans and in compliance with broadcast industry regulations, Telecom Italia Media Group television stations have taken steps to acquire the frequencies and equipment necessary to establish a digital terrestrial broadcast network in compliance with the requisites needed for authorization to set up a digital terrestrial television operator company.

Office Products and Services and Business Information

Through Gruppo Buffetti S.p.A. (Buffetti), during 2003 Telecom Italia Media was a leading distributor of office products and business solutions in Italy.

Professional Publishing

Through GPP, Telecom Italia Media has interests in companies publishing specialized information in the hotel, restaurant and entertainment industry, in electronics, information technology and audiovisual communication and in ceramics, architecture and urban design sectors.

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Financial data of the main subsidiaries

The following table sets forth operating revenues, gross operating profit and operating income for the main subsidiaries of the Internet and Media Business Unit on a stand alone basis. The financial data will not tie directly to consolidated segment data due to intercompany, consolidation and other adjustments.

		Parent Company		National Subsidiaries		
(millions of Euro)		**Telecom Italia Media**		**Matrix**	**Holding Media and Comunicazione Group**	**Buffetti Group**
		Historical(1)	**Pro Forma(1)**			
Gross operating revenues	2003	743	223	36	113	156
	2002	1,152	115	28	88	171
	Change (%)	(35.5)	94.1	28.2	27.8	(8.8)
Gross operating profit	2003	300	20	3	(29)	8
	2002	545	3	(7)	(45)	10
	Change (%)	(45.0)			36.2	(17.3)
Operating income	2003	158	(25)	(5)	(51)	2
	2002	348	(51)	(15)	(64)	4
	Change (%)	(54.7)	51.0	68.2	20.3	(63.8)

(1) In order to allow a better understanding of the results of the business managed by Telecom Italia Media after the SEAT Spin-off, the figures are presented on an historical and pro forma basis.

Major 2003 corporate events/scope of consolidation

On May 9, 2003, the SEAT extraordinary shareholders meeting approved the proposed proportional spin-off of substantially all of the Directories, Directory Assistance and Business Information business segments of SEAT into New SEAT. The spin-off became effective on August 1, 2003. On the same date, the corporate name of old SEAT became Telecom Italia Media S.p.A. . The shares of both companies are listed on the automated screen-based trading system (Mercato Telematico Azionario) of Borsa Italiana. For a further description of these businesses and of the reasons for the spin-off, please see Business Significant Developments during 2003 SEAT Spin-off and Sale .

Events subsequent to December 31, 2003

Sale of CIPI s stake by Telecom Italia Media

On January 29, 2004, Telecom Italia Media sold, as part of the rationalization of its portfolio of activities, its 60% stake in CIPI S.p.A. to Promoinvestments S.r.l., a company owned by the Circo family, already minority shareholder of CIPI S.p.A.. The value of the transaction amounted to 6.5 million and Telecom Italia Media recorded a capital gain of 4.9 million.

Other agreements

On February 3, 2004, the City of Pesaro and La7 Televisioni S.p.A. a company controlled by Telecom Italia Media which operates the La7 TV station signed a memorandum of understanding for the experimentation of land-based digital television (DDT) directed to the development and broadcasting of publicly useful interactive services for the city of Pesaro. The experiment, which involves 100 families, will bring the city s interactive services into the homes of its citizens and will be able to be accessed simply by using the TV remote control.

On February 11, 2004, Telecom Italia Media, Sun Microsystems Italia, a leader in network systems, and CSP Innovation a leader in information communications technology, signed an agreement for the experimentation of innovative services for land-based digital television in the province of Turin.

Agreement for the sale of GPP

On May 13, 2004, Telecom Italia Media reached an agreement with Wise Venture Sgr, the company that manages the Wisequity closed-end equity fund, in relation to the disposal of 100% of GPP S.p.A., the parent company of the publishing groups Quasar s.r.l., JCE S.p.A. and Faenza Editrice S.p.A..

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The disposal of GPP S.p.A. represents yet another step in the process of rationalization of Telecom Italia Media s asset portfolio. Following this transaction, Telecom Italia Media exits the professional publishing sector, which is not considered synergic with its core business.

The disposal is based on the assessment of the overall enterprise value of GPP S.p.A. valued at 14.6 million. The sale will improve the Group s net financial standing by approximately 13.8 million. The transaction is expected to be completed within the first half of 2004.

Information Technology Market

The Information Technology Market Business Unit (IT Market) was created in early 2002 with the aim of focusing the activities previously concentrated in the Information Technology Services Business Unit by type of customer.

The IT Market Business Unit is a full Business Solution Provider for government, banks and enterprise providing consultancy services, system integration, CRM and ERP solutions and web services. Increasingly the IT Market Business Unit is developing technological and commercial partnerships with the leading providers of information technology products and solutions worldwide (Microsoft, Oracle, Sap, FileNET, Siebel).

As of December 31, 2003, IT Market was organized as follows:

Information Technology Market

Finsiel Group:

- Finsiel S.p.A.
- Banksiel S.p.A.
- Insiel S.p.A.
- Tele Sistemi Ferroviari S.p.A.

Webegg Group:

- Webegg S.p.A.
- Software Factory S.p.A.
- Teleap S.p.A.

Eustema S.p.A.

Due to the macro-economic situation, as in 2002, 2003 was marked by continuing weak demand for IT services, with the consequential pressure on pricing for top customers, as well as the acquisition of new orders and new customers at lower prices than in the past. In response to the weak market conditions, action was taken to further improve overall efficiency and to reduce costs, particularly with reference to Finsiel S.p.A. and the major subsidiaries.

Main Subsidiaries

Finsiel Group

The Finsiel group, which covers the whole chain of value of Information Communication Technology or ICT services, is the second-largest Italian supplier of IT solutions and services, and leads the ICT market in the Public Administration sector, with customers in the most important state administrations and in more than 1,000 local governmental organizations and health agencies.

Finsiel provides services in the field of information technology and related activities, including services for local and central government entities. In addition, Finsiel provides management consulting and services related to company automation. Finsiel is the leading Italian firm in the systems integration and information technology consulting market, and one of the largest European companies of this type. Finsiel is the principal supplier of systems integration and information technology consulting to the Italian government and local government authorities, typically under long-term exclusive arrangements.

The Finsiel Group is a business solutions provider for government, banks and businesses.

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Webegg Group

The Webegg group is a multi-functional group with a network of international partners, the corporate purpose of which is to position companies on-line. It operates mainly through the company Telemedia Applicazioni S.p.A., which supplies CRM systems, particularly for Telecom Italia Mobile and for third-party customers, while Software Factory S.p.A. concentrates on developing software exclusively for the banking and insurance sectors. See Events subsequent to December 31, 2003 .

Financial data of the main subsidiaries

The following table sets forth operating revenues, gross operating profit and operating income for the main subsidiaries of the IT Market Business Unit on a stand alone basis. The financial data will not tie directly to consolidated segment data due to intercompany, consolidation and other adjustments.

(millions of Euro)		Finsiel group(*)	Webegg group(*)
Gross operating revenues	2003	777	75
	2002	661	80
	Change (%)	17.5	(6.3)
Gross operating profit	2003	72	10
	2002	73	8
	Change (%)	(1.4)	25.0
Operating income	2003	54	5
	2002	35	2
	Change (%)	54.3	150.0

(*) The 2002 financial data are consistent with the 2003 scope of consolidation.

Major 2003 corporate events/scope of consolidation

During 2003, the main IT Market Business Unit corporate events and changes in the scope of consolidation are the following:

- on January 1, 2003, the Netikos Group (which includes Netikos S.p.A. and Netikos Finland Oy), the Webegg Group (which includes Webegg S.p.A., Domus Academy S.p.A., @Live S.p.A., Winner Project B.V., Software Factory S.p.A. and Telemedia Applicazioni S.p.A.) and Eustema S.p.A. were transferred from the IT Group to the scope of consolidation of the ITM Business Unit.

- On July 23, 2003, (with effects since July 1, 2003), IT Telecom S.p.A., 100% shareholder of Netikos S.p.A., sold the Netikos Group to MyQube S.A. for a sale price of 2 million. As result of this transaction, the 2003 statement of operations includes Netikos only for the first six months.

- On July 31, 2003, Webegg and Telecom Italia signed an agreement for the sale of the 67.33% stake in Domus Academy S.p.A., (with effects since July 1, 2003). As result of this transaction, the 2003 statement of operations includes Domus Academy S.p.A. only for the first six months.

- On July 31, 2003, an agreement between Finsiel S.p.A. and Sogei S.p.A. for the sale of 49% Finsiel share in Sogei IT S.p.A. was signed. On October 9, 2003, after authorization was received from the Antitrust Authority, Finsiel sold its investment in Sogei IT to Sogei, consisting of 25,480 ordinary shares, equal to 49% of share capital, at the price of 1.6 million.

- In October 2003, the extraordinary shareholders meetings of Finsiel S.p.A. and Eis S.p.A. (100%-owned by Finsiel) resolved to merge Eis S.p.A. into Finsiel S.p.A. (with effect from January 1, 2003).

- On November 3, 2003, a preliminary contract for the sale of 22.5% Finsiel stake in Praxis Calcolo S.p.A. was signed. The transaction became effective on November 28, 2003.

- On December 23, 2003, the extraordinary shareholders meeting of @Live S.r.l. resolved to wind up and liquidate the company with effect from December 31, 2003.

- In December 2003, Simest S.p.A. sold its 7.44% share in Finsiel Romania to Finsiel S.p.A.. As a result of this operation, Finsiel S.p.A. currently holds 97.97% of Finsiel Romania.

The following transactions also took place in 2003:

- On October 1, 2003, the Enterprise business area (responsible for planning, implementing and selling IT solutions on the Enterprise Market, and managing applications and facilities on this same market) was transferred from Finsiel to IT Telecom.

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- On October 1, 2003, the Administrative Services Center business area was transferred from Finsiel to Telecom Italia.
- On October 1, 2003, the Desk Top Management business area (operating in distributed workstation management, technical support and hardware maintenance) was transferred from Finsiel and Banksiel to Hewlett Packard.
- On November 1, 2003, the PAL Bologna business area (responsible for UBC service management the Unified Booking Center for the Bologna Metropolitan area, offering applications advice, corrective maintenance and software upgrades, hardware support and peripheral systems management, helpdesk and second level care) was transferred from Finsiel to Webred.

Events subsequent to December 31, 2003

Sale of the Facility Management

On January 1, 2004, the Facility Management of Finsiel S.p.A. was transferred to Emsa Servizi S.p.A..

Information Technology Group

The Information Technology Group (IT Group) Operating Activity is responsible for the information technology activities of the Telecom Italia Group and covers the entire range of information services.

As of December 31, 2003, the IT Group included the following companies:

Information Technology Group

IT Telecom Group

- IT Telecom S.p.A.
- Teco Soft Argentina S.A.
- Telesoft Russia ZAO

EPIClink S.p.A.

As of December 31, 2003, the IT Group was organized as follows:

The Operating Activity is organized into five production divisions:

- **IT Architectures** design and creation of applications and infrastructure architectures, ensuring rationalization and standardization;
- **IT Operations & Infrastructures** design and management of the IT infrastructures required for the functioning of Telecom Italia Group systems and applications and the delivery of investment-based services for the market; the running of IT systems and solutions;
- **Business Support System** - design and development, for the business segment, of the IT systems, solutions and applications for the Business Units of the Telecom Italia Group;
- **OSS & VAS Solutions** design, development and maintenance, for the network segment, of the IT systems, solutions and applications for the Business Units of the Group; development and system integration of hi-tech IT solutions with high added value, supplying technological support to the Business Units of the Telecom Italia Group in the development of innovative services;
- **Operational Planning & Client Management** coordination and support for the operative functions responsible for planning, staffing, operational control and the monitoring of the main projects; preparation of the systems plan.

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In the year 2003, the organization and standardization activities have continued to improve the Group architectural and infrastructure solutions. Such activities were focused on important investment projects such as Business Continuity, Disaster Recovery, Griffon, Data Center Consolidation (Reduction), and also on the convergence and innovation of our IT infrastructures.

Among the main activities in the BSS (Business Support System) area, new projects were begun with the aim of providing Wireline with better tools for business management and replace legacy platforms with new CRM (Customer Relation Manager) platforms, a new platform for credit management and a new platform for acquisition and management of traffic (the completion of the latter is due for June 2004).

In addition, the activities with TIM have continued, particularly with CRM, Charging and Billing, Prepaid and Business Intelligence projects. Also in the OSS area, innovation has continued, while replacing the former legacy environments.

Within the Service Assurance Process the integration of Trouble Ticket Management/Work Force Management systems was started to support claims and trouble management.

Within the Service Provisioning Process, the UNICA/D module was delivered throughout the Italian territory, with the new release of CPC module (to manage respectively the Network and Service Inventory and the Network Configuration of Broadband Services), and the Order Manager Module which completed phase 2 of the project for the new Broadband Management Platform (NPG-BB). As well as helping to improve the quality of service offered to customers, the new platform has made it possible to eliminate a considerable number of legacy systems.

As for VAS solutions, IT Group has improved its support to develop innovative proposals for Wireline and TIM markets.

Major 2003 corporate events/scope of consolidation

- In January 2003, the merger into IT Telecom of its 100% owned subsidiaries (Netsiel S.p.A., Saritel S.p.A., Sodalia S.p.A. and Telesoft S.p.A.), became effective. The merger was carried out to obtain more efficiency and effectiveness in the information technology services rendered to the Group and to focus on innovation, services and products.
- Starting from January 1, 2003, Netikos Group, Webegg Group, TILAB, Loquendo and Eustema are not included in the IT Group Operating Activity. TILAB became part of the Other Activities, Loquendo was transferred to the Wireline Business Unit and the other companies were transferred to the IT Market Business Unit. On the same date EPIClink was included in the IT Group Operating Activity.
- In February 2003, Telecom Italia and Hewlett-Packard reached an agreement in the area of Management Services and Outsourcing with a total value of 225 million. Under the terms of this agreement, HP will supply asset management, help desk, maintenance and workstation management, while IT Telecom will manage Hewlett Packard Italia s operational activities in the SAP environment, housing the systems in its Data Centers. On April 16, 2003, the agreement became effective and, on the same date, a contract for the sale of IT Telecom s Desktop Management services business segment to Hewlett Packard DCS (Distributed Computing Services) was finalized.

- On March 28, 2003, the subsidiary Telesoft Hellas was sold to STET Hellas, with effect from January 1, 2003.

- On June 11, 2003, Sodalia Inc. was sold to third parties, with effect from June 1, 2003.

- On July 23, 2003, IT Telecom sold its entire holding in Netikos S.p.A. to the Belgian company MyQube S.A. for 2 million. The Netikos group was consolidated in the IT Market Business Unit to which it reported functionally. At the same time as the sale, a long-term (2004-2007) commercial agreement was put into place between Telecom Italia, Netikos and MyQube for professional services to be rendered by Netikos to the Telecom Italia Group.

- On July 31, 2003, IT Telecom transferred to Shared Services Center former Pirelli Informatica S.p.A., a software company owned by Pirelli the product division Corporate Solutions (which comprises approximately 270 employees) in exchange for a 45% stake in the capital stock of the company.

- On August 8, 2003, a total of 1,386,455 shares of new SEAT, the company resulting from the proportional partial spin-off of SEAT Pagine Gialle S.p.A., was sold to SILVER S.p.A.. IT Telecom S.p.A. remains the holder of 525,896 shares of the spun-off company which took the name of Telecom Italia Media S.p.A.

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- On October 1, 2003, IT Telecom acquired from Finsiel S.p.A. the Enterprise business segment (253 people) specialized in services and platforms related to Vertical Solutions and Enterprise Re-engineering Management.
- On December 1, 2003, pursuant to the Kings project, approved by Telecom Italia, IT Telecom contributed its Facility Management operations (53 people) to Emsa Servizi.

Events subsequent to December 31, 2003

Sale of the Innovative Services Business Segment to TIM

On April 1, 2004, IT Telecom S.p.A. sold its Innovative Services Business Segment to TIM S.p.A.; the activities of this business segment are conducted in the innovative services field, based on IP networks and oriented towards the business and mass-market sectors, and they are also related to the development and maintenance of software for telecommunications. The transfer s value, based on an independent evaluation, was agreed at 23 million. There has been a staff transfer of 551 units.

Sale of equity stake in Webegg S.p.A.

On June 7, 2004, IT Telecom S.p.A. signed an agreement with Value Partners S.p.A. regarding the sale of a 69.8% equity stake in Webegg S.p.A. for a sale price of 43 million. Finsiel will retain the remaining 30.2% equity interest. The deal provides for reciprocal put and call options for Finsiel and Value Partners S.p.A. on the remaining equity interest held by Finsiel. The transaction will be completed on receipt of necessary approvals from the Antitrust Authority.

Olivetti Tecnost

Olivetti Tecnost and its subsidiaries (the Olivetti Tecnost Group) supply office products and digital printing systems through its Office Products Division, specialized applications for service automation in banking, retail, trade industry applications and gaming and lottery management through its Systems Division. In addition, the Olivetti Tecnost Group operates with the Industrial Operations Division in the development and production of silicon technology (including ink-jet print-heads and MEMS), in document management services and in the mobile phone repairs business.

This Business Unit operates mainly in Europe, Asia and North America.

As of December 31, 2003, the Olivetti Tecnost Business Unit included the following companies:

Olivetti Tecnost Group

Olivetti Tecnost S.p.A.

Olivetti I-Jet S.p.A.

Innovis S.p.A.

Cell-Tel S.p.A.

Wirelab S.p.A.

Olivetti Tecnost International B.V.

(foreign sales companies)

As of December 31, 2003, the Olivetti Tecnost Group was organized as follows:

Office Products Division The Office Products Division has been repositioning its two business lines: the *Professional Line of Business*, which focuses on digital copiers and printers, with an innovative offer of value-added digital products enhanced by loyalty-boosting services; and the *Ink-Jet Communication & SOHO Line of Business*, which develops products based on ink-jet technology such as fax, printers and multifunctional products, as well as calculators and original supplies.

The Office Products Division targets its offer to the business market. The Office Products Division intends to complement its well-established dealer channel with direct sales operations on key markets and development of correlated services.

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Olivetti Tecnost is the leading European vendor of ink-jet fax and supplier to Europe s main telecommunications operators. In addition, it markets ink-jet fax and other products in the SOHO segment through distributors and specialist chain stores.

Systems Division Move to achieve geographical diversification became effective with the acquisition of new orders on foreign markets, particularly in the field of gaming.

Contracts were signed with two lotteries in India, in Tunisia (a pilot test for a game similar to the football pools) and in Peru (football pools) requiring the Systems Division to supply more than 20,000 terminals.

In Italy, during August 2003, the System Division successfully started the Lottomatica network for the new Totocalcio system (football pools) which involved supplying terminals, software and services to adapt the pre-existing collection system.

In the banking sector, there was a generalized recession in the markets of Western countries which slowed down sales and reduced volumes in the first half of the year 2003. Starting from the second half there were signs of a recovery: a significant order was acquired from Abbey-National Bank (UK) to renew its printing equipment (approximately 9,000 printing stations).

Stagnation continued in China, where sales were very low and there was a loss of profit margins as a result of the foreign exchange effect and falling prices. Conversely, there was a significant recovery in other parts of the Asia-Pacific region with increasing volumes.

In the international retail sector, sales (volumes and margins) of the range of PR4 products are in line with forecasts. In Italy, the Shop Automation business of fiscal Cash Registers confirmed the improvement in margins achieved in the first half of 2003. However, announcements about changes to the regulatory framework (the law on the agreement for shop owners) drastically reduced demand in the last part of the year; once the initial uncertainty has passed, there is expected to be a recovery.

South America In 2003, the process to wind-up the companies in the South America Area began.

North and Central America Olivetti Tecnost is present in Mexico and in North America, through the subsidiary Royal Consumer Information Product Inc. under the Royal brand name, focusing on office equipment, accessories and consumer electronic products for the consumer and small business market.

Industrial Operations Industrial re-conversion of the Division continued during the year 2003 with the launch of the company Cell-Tel which operates in the area of mobile phone repairs alongside the company Innovis which is operational in the back-office sector. Furthermore, at the end of July, Wirelab was set up; starting in the third quarter of 2003, the company operates in the sphere of repairing and regenerating fixed telecommunications equipment.

With reference to Olivetti I-JET, development activities continued on MEMS applications in the sector of pressure sensors for automotive applications, and also in the sector of optical components, where Olivetti I-Jet acts mainly as a silicon foundry. Full-scale production also continued for Olivetti I-JET ink-jet print-heads.

Major 2003 corporate events/scope of consolidation

- On January 7, 2003, the contract signed with SMT Vertronic, a Mexican company in the SMT group, for the sale of the industrial assets of the subsidiary Olivetti Tecnost de Mexico became effective. This agreement led to the sale of the factory in Tlaxcala (Mexico) and the hiring of the employees working in the factory (1,266 at December 31, 2002) by SMT Vertronic.

- On February 13, 2003, the agreement with TEL.I.S. in the new mobile phone repair business by way of the investment of TEL.I.S. in the company Cell-Tel S.p.A. became effective.

- On May 12, 2003, the Plans of Merger were voted for the incorporation of the companies Tecnost Sistemi S.p.A., Technoproduzioni S.p.A. and Oliweb S.p.A. with and into Olivetti Tecnost S.p.A.. The Plans of Merger became effective on August 1, 2003.

- In line with the strategy aimed at divesting non-core businesses, the following companies were sold:

  - on May 29, 2003, the Domustech (now Dedita) business segment operating in the security and home automation business was sold to ABB Sace S.p.A. (ABB group);

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- on June 10, 2003, the Domustech (now Dedita) investment in the Aprimatic group operating in the door-automation sector was sold to the URMET group; and

- on July 11, 2003, the investment in Gotoweb S.p.A., (a company operating in ASP Internet services for small- and medium-sized companies) was sold to Comdata S.p.A..

- On July 29, 2003, formation of the company Wirelab S.p.A. (70% Olivetti Tecnost, 30% Tellus S.r.l. Urmet group) destined to carry out repairs of wireline telecommunications equipment in the Canavese area.

- On October 20, 2003, under the plan to reorganize and rationalize back-office operations and administrative area services, the Sales Back End business segment of Olivetti Tecnost S.p.A. (consisting of 24 resources) was sold to the Accenture group, with which an outsourcing contract was signed.

- The process for the wind-up of the companies in the South America Area began: the 2003 financial statements take into account the estimated effects of such process.

Events subsequent to December 31, 2003

Sale of the CRM business segment

Effective January 1, 2004, under the plan to reorganize and rationalize help desk and customer care operations, the CRM business segment of Olivetti Tecnost S.p.A. (consisting of 14 employees) was sold to the Comdata group, with which an outsourcing contract was signed.

The winding up of the following companies was also approved in the first few months of 2004:

- Olivetti de Venezuela C.A. (January 30, 2004);

- Olivetti Peruana S.A. (February 20, 2004);

- Diaspron do Brasil S.A. (March 5, 2004);

- Multidata S.A. Eletronica Industria e Comercio (March 5, 2004); and

- Olitecno S.A. de C.V. (February 17, 2004).

Other Telecom Italia Group Activities

Real Estate and General Services

In February 2003, the Real Estate and General Services Operating Activity was disbanded; all real estate activities and general services were reassigned to the Telecom Italia Purchasing Corporate Function, which continued to be an interface for the various corporate Functions/Business Units to satisfy the needs of the real estate and general services area.

In particular, the activities performed are related to the planning of sites and locations of the Telecom Italia Group, the design and construction of civil works, the maintenance of the properties and technological plants, in addition to providing real estate and general services.

These activities and services were operated through the internal structures of Telecom Italia mainly for the activities conducted on behalf of the Telecom Italia Business Units/Corporate Functions and through the subsidiary Emsa Servizi S.p.A., which, for the most part, geared its activities towards the other companies in the Telecom Italia Group.

In December 2003, the Facility Management business areas of Tim, IT Telecom and Finsiel were transferred to Emsa Servizi S.p.A.: such transactions became effective on December 1, 2003, for Tim and IT Telecom, whereas for Finsiel the transfer became effective on January 1, 2004.

The transfer of such business functions permited Emsa Servizi to improve the quality of its facility management expertise for the benefit of the other companies in the Telecom Italia Group.

International Affairs (the former Foreign Holdings Corporate Function)

In May 2002, the companies and business segments of the Telecom Italia Group which formerly reported to the International Operations (IOP) Operating Activity were transferred to Domestic Wireline and to Foreign Holdings Corporate Function (now International Affairs), while all the companies based in Latin America were subject to the coordination of LAO.

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As of June 18, 2003, the new corporate function, International Affairs, was established and reports directly to the CEO Carlo Buora. On the same date the central function Foreign Holdings was merged into International Affairs.

The corporate function International Affairs guarantees the coordination of the activities managed by Telecom Italia International and ETEC S.A.

During the course of 2003 and the beginning of 2004 the Telecom Italia Group, through Telecom Italia International continued to pursue its targets under the business plan, focusing on reorganizing and rationalizing its international presence. The principal corporate transactions which took place in 2003 were the following:

- On January 20, 2003, Telecom Italia International did not subscribe to the new capital increase in Euskaltel (the regional operator for cable TV and applied telecommunications for the Basque countries) approved by the Shareholders meeting on December 16, 2002. As a consequence, Telecom Italia International s stake fell to 13.85%. On June 12, 2003, the Company entered into an agreement with Bilbao Bizcaia Kutxa (BBK) for the sale of part of its stake in Euskaltel, corresponding to 7.75% of Euskaltel s total share capital. The transaction for a consideration of 34 million, was finalized on October 10, 2003.

- On December 30, 2003, Telecom Italia International received an offer to sell an additional 3.1% stake in Euskaltel for a total amount of 13.6 million. On January 16, 2004, the sale and purchase agreement between Telecom Italia International and Araba Gertu S.A. was signed. On the same date Telecom Italia International sent a notice to the other shareholders of the company offering them to exercise, proquota, their pre-emptive rights on the same terms and conditions agreed with Araba Gertu S.A.. As of February 16, 2004, the pre-emptive right was exercised only by Iberdrola SA.. Furthermore on February 19, 2004 (the Closing date), two separate deeds of sale were signed: the first between Telecom Italia International and Araba Gertu (149,231 shares for a consideration amount of 12.1 million) and the second between Telecom Italia International N.V. and Iberdrola (18,719 shares for a consideration of 1.5 million). Following such a sale Telecom Italia International s stake in Euskaltel decreased to 3.0%.

- On February 20, 2003, Telecom Italia International executed a Share Purchase Agreement, for the sale of its entire participation in Telekom Srbija, corresponding to 29% of the Telekom Srbija share capital for a total consideration of 195 million. The payment of the first tranche of 120 million was completed in June 2003. The shares remain in an escrow account until full payment of the remaining 75 million is made.

- On July 8, 2003, Telecom Italia International N.V. exercised its put option on all of its Mediterranean Broadband Access (MBA) shares (40%) to Forthnet (parent company of MBA) for a consideration equal to 7.04 million which was finalized on October 29, 2003. In parallel, Telecom Italia International, subject to the completion of the sale of MBA s shares as described above on October 29, 2003, subscribed to a reserved capital increase in Forthnet, for a value equal to 7.04 million (corresponding to 7.81% of Forthnet share capital). The Forthnet shares have been listed on the Athens stock exchange.

- In August 2003, Telecom Italia International on the basis of an irrevocable offer, received from Telecom Italia Sparkle, for the purchase of the 100% stake of Intelcom San Marino proceeded to purchase the remaining 30% of the share capital of the subsidiary from third parties for consideration of 4.25 million. The sale of the entire participation of Telecom Italia International in Intelcom San Marino to Telecom Italia Sparkle, was completed as of December 23, 2003 for a consideration of 14.2 million.

- Telecom Italia International, following the agreement reached in June 2002, with OIAG, in the month of November 2002, sold 75,000,000 Telekom Austria shares at a price of 7.45 per share, reducing its investment from 29.78% to 14.78%. Under such agreement, the sale of the remaining part of the shares held by the Telecom Italia Group was permitted from January 1, 2004. Consequently on January 27, 2004 Telecom Italia International sold the remaining 14.78% stake in Telekom Austria for a total gross consideration of 780 million.

- On March 4, 2004, Telecom Italia International signed a Shares Purchase Agreement with AUNA to sell its entire participation in Netco Redes S.A. (30%) for a consideration of 30 million plus interest to be paid in three annual installments starting from December 2006. The closing will take place subject to receiving regulatory approval.

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Cuba

On December 16, 2003, the establishing in Cuba of an integrated TLC operator acting both in the wireline and in the mobile sectors was finalized through the incorporation of the local mobile operators Cubacel and C-Com into Empresa Nacional de Telecommunicaciones de Cuba S.A. (ETEC S.A.). Due to the merger, Telecom Italia International s stake in ETEC S.A. was reduced to 27%. The merger resulted from the agreements signed on October 1, 2003, between all shareholders of the relevant entities in order to set-up the integrated TLC operator. These agreements provide amongst others the granting of a new more extended license to the new entity for rendering fixed line and mobile services up to December 31, 2019. In respect of the new license, a total fee of U.S.$185.18 million payable within one year is to be made by ETEC S.A.. The fee shall be financed by capital increases to be underwritten by each shareholder. Telecom Italia International s share amounts to U.S.$50 million. The first capital increase of U.S.$35.9 million was subscribed by Telecom Italia International on December 16, 2003 for a total amount of U.S.$9.8 million.

On March 4, 2004, the shareholders meeting of the Cuban company voted a further share capital increase, of U.S.$23.8 million, through the issue of 165 new shares with a par value U.S.$144,190 each. Telecom Italia International proportionally subscribed to its share of the capital increase for U.S.$ 6.3 million in exchange for 44 new shares.

On May 20, 2004, the shareholders meeting of ETEC S.A. voted a further share capital increase of U.S.$31,578,000, through the issue of 219 new shares with a par value of U.S.$144,190 each. Telecom Italia International proportionally subscribed to its share of the capital increase of U.S.$8.5 million in exchange for 59 new shares.

In order to fulfill the long-term objectives related to its license, ETEC S.A. increased during 2003 the number of lines from 646,000 in 2002 to 696,000 (an increase of 8%), while the digitalization rate rose to 81.6% from 76% reached in 2002. As a consequence of the merger, ETEC S.A. acquired 43,987 mobile customers. In 2003, ETEC S.A. has maintained the focus on Internet and data transmission commercial development, achieving a 13% growth against 2002 (from approximately U.S.$13.4 million in 2002 to U.S.$15.2 million in 2003). In 2003, total operating revenues, excluding the three months effect of the mobile contribution (U.S.$13.7), were U.S.$310 million compared with U.S.$294 million in 2002, an increase of 5.4%. Gross Operating profit increased from U.S.$202 million in 2002 to U.S.$209 million in 2003 (an increase of 3.5%) and operating income was U.S.$141 million compared with U.S.$139 million in 2002 (an increase of 1.4%). Net income was U.S.$133 million in 2003 compared to U.S.$132 million in 2002 (an increase of 0.8%).

Telecom Italia Lab

The Telecom Italia Lab Operating Activity (TILAB) is responsible for supervising technological innovation within the Telecom Italia Group, in the sector of networks and innovative services. As a result, the activity of TILAB is chiefly oriented towards providing support to the Business Units of the Telecom Italia Group by offering competitive technology and, at the same time, pursuing the objective of improving quality and efficiency and promoting innovation.

As of December 31, 2003, the Operating Activity was organized as follows:

TILAB
Telecom Italia TILab segment

Telsy S.p.A.

The Operating Activity was managed with the following organization:

Innovation Delivery is focused on short-term goal-oriented research activities geared essentially to the Business Units of the Telecom Italia Group.

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Service Innovation and Network Innovation are devoted to medium and long-term research projects with a focus on infrastructures and on the creation of services and the testing of prototypes through innovative platforms, in order to create competitive advantages for the Business Units of the Group.

Telsy, since 1971, has been the leading supplier of information security solutions to the Group, offering off the shelf and customized encryption equipment.

TILAB performs both strategic research and research specifically requested by Group Companies that focuses on projects that are of strategic interest for the individual Business Units and advances the Group s technological leadership. Research is also carried out in specific areas in partnership with Pirelli Labs.

The activities are organized into the main innovative areas of interest to the Group such as:

- Terminal and user interfaces,
- Applications and Services,
- Service control,
- Access, metro and core network, and
- Network operations and management.

Increasing attention to the opportunity of generating competitive advantages and creating value for the Telecom Italia Group was also pursued through the strategic management of the relations between research, Intellectual Property Rights (IPR) and business with the aim of increasing the number of registered patents. In this context, during the year, 68 new patents were filed of which 14 are jointly owned with Pirelli.

The Group spent 204 million, 151 million and 148 million on research and development in 2001, 2002 and 2003, respectively. The Group also receives grants from research and development national and international programs.

In 2003, TILAB s research was based on three macro areas: Broadband Services, Mobile Services, Network Innovation.

The most significant results achieved in these areas in the year 2003 included the following research projects.

Broadband Services

Test of an integrated videocommunication service between fixed (PC, TV) and mobile (3G, WiFi) terminals. Based on network intelligence according to SIP (Section Initiation Protocol) standard a new capability has been developed enabling seamless video communication among terminals connected to different networks and with etherogeneous equipment including television, fixed and mobile subscriber equipment.

Videochat solution that enriches Alice services. The experience in community and chat services and platforms together with experience in video coding and video communication were exploited in the development of a new videochat application deployed in the broadband service portal Alice of the Telecom Italia Wireline Business Unit.

Broadband home service second technical trial. With the aim of gaining original first hand experience with user reaction to new advanced services for the home information and entertainment platform, a trial in Turin and Rome has been established where xDSL access and home WiFi distribution are enabling new applications on PC and television.

Mobile Services

Enhanced SIM based applications and hardware development. These developments will enable the mobile customer to exploit new applications based on the SIM, such as: terminal personalization for TIM with 1 Mbyte of capacity using flash memory; the creation of a Digital Rights Management Platform (DRM) for secure distribution of digital contents based on OMA (Open Mobile Association) standards. SIM Secure, a suite of mobile security solutions.

Enabling Platform and application for Location Based Services. Deployment of an innovative mobile terminal localization platform based on NIMBLE (Non Intrusive Mobile Location Environment) technology and implementation of a first set of location-based services.

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Delivery of new tools for the mobile operator for planning, optimization and management of the mobile network. The experience in radio and network planning, design and monitoring techniques led to the development and delivery of version 9.1 of the radio network planning tool 3 G GUITAR. Based on Jade, an intelligent agent platform developed in TILAB for peer-to peer applications, a platform prototype for quality of service monitoring was developed.

Network Innovation

Development together with Italtel of Telecom Italia Wireline videoconference service interconnected to 3 and FastWeb. The solution was developed on StarSip, a platform for session-based services based on SIP protocol.

Specifications and prototypes for creating service broker functions for Mobile Operators. These results will enable new business models for TIM opening the network to third party service providers.

Product specifications for packet optical router. These studies will enable the evolution of Telecom Italia s optical transport network and its service offer.

Relevant projects have been developed in cooperation with Pirelli Labs, which include:

- *final version of the Access Gateway for residential and SOHO customers.* This solution allows the SOHO customer to configure its home/office network automatically;
- *development of the MAS (Metro Access System) network element based on CWDM (Coarse Wavelength Division Multiplexing) technology, equipped with its element manager system EMMAS (Element Manager Metro Access System).* This activity is related to the network and services management area for metropolitan applications;
- *first live call on TIM UMTS network over RoF (Radio over Fiber) links.* As a result of RoF technology, 3G radio access networks will be realized in urban areas for optimizing radio access capacity. The first RoF modules were provided to Alcatel.

Major 2003 corporate events/scope of consolidation

- Merger by incorporation of the subsidiary Telecom Italia Lab S.p.A. into Telecom Italia S.p.A., agreed on March 18, 2003, effective for accounting and tax purposes as from January 1, 2003.
- The transfer of Loquendo S.p.A., previously included in TILAB, into the Wireline Business Unit.
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Transfer of TILAB s Venture Capital activities to Telecom Italia Merger & Acquisitions Corporate Function (now Corporate Development and Investor Relations).

Other Subsidiaries

Telecom Italia Finance S.A.

Telecom Italia Finance S.A. (TI Finance) organized in the Grand-Duchy of Luxembourg as a Socièté Anonyme, is a 99% owned subsidiary of Telecom Italia. TI Finance provides financial assistance to Telecom Italia as well as companies in which Telecom Italia has a direct or indirect interest such as, among others, providing loans and the granting of guarantees for securities of any kind or form. TI Finance also may borrow in any kind or form and issue bonds or notes.

TI Finance had net income of 333 million for 2003 and a net equity as of December 31, 2003, of 256 million. The results for 2003 are primarily due to the sale of a portion of fixed-rate bonds which were issued by Telecom Italia in 2001 as private placements. With the proceeds of such sale, TI Finance granted several loans to Telecom Italia based on the then applicable market conditions. The sale of the bonds generated a gain of 396 million which is and will be compensated by lower financial revenues up to the end of 2005. On February 20, 2004, Olivetti International S.A. (a 99% Luxembourg-based Telecom Italia subsidiary) was merged into TI Finance. As a consequence of the merger, TI Finance issued 30,000,000 new ordinary shares and the current share paid up capital of TI Finance amounts to 1,162,562,614.74, divided into 118,871,433 shares of 9.78 per share.

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Telecom Italia Capital S.A.

The company is a directly and indirectly wholly-owned subsidiary of Telecom Italia, organized under the laws of Luxembourg, and was established in the year 2000 as the finance vehicle to issue notes in the U.S. market. On October 29, 2003, Telecom Italia Capital issued fixed-rate multi-tranche notes in U.S.$ with a full and unconditional guarantee of Telecom Italia. Details are as follows:

- Series A notes in the principal amount of U.S.$ 1 billion, 4% annual coupon, issue price of 99.953%, maturing November 15, 2008;
- Series B notes in the principal amount of U.S.$ 2 billion, 5.25% coupon, issue price of 99.742%, maturing November 15, 2013;
- Series C notes in the principal amount of U.S.$ 1 billion, 6.375% coupon, issue price of 99.558%, maturing November 15, 2033.

Subsequently, Telecom Italia Capital granted a loan for the same amount of the notes to Telecom Italia.

Saiat S.p.A.

The company, held 100% by Telecom Italia, carries out support services for the Telecom Italia Group, in some finance activities. In particular during 2003, the company continued to provide services under the program for the securitization of the Telecom Italia Group trade accounts receivable.

TI Learning Services S.p.A.

This company operates in the Training sector with the objective of achieving a significant market share in the learning and knowledge management markets.

The Company designs complex and customized training systems that can be used by large numbers of people. Its product range includes more than 2,200 courses for training developed by e.learning as well as in the class room, particularly on topics associated with ICT and Business Management.

The above activity is mainly provided to the Telecom Italia Group.

During the year 2003, TI Learning Services S.p.A., supported by the Board of Directors of Telecom Italia, began a restructuring of its activities. The main guide lines are: head count reduction in order to reduce costs and to introduce a change in management.

Other Investments

Multimedia Services

Stream (now SKY Italia) was formed in 1993 by Telecom Italia with the objective of establishing and promoting a wide range of multimedia services and applications for the Italian and other international markets. Subsequently, Stream focused its activity on the Italian pay television market.

After some changes in the shareholding structure, by the end of 2001 Stream was equally owned by Telecom Italia and News Corporation. On October 1, 2002, Telecom Italia signed an agreement with the News Corporation Group, partner of Telecom Italia in Stream, and Vivendi Universal, shareholder of Tele+ (Stream s main competitor), in order to allow Stream to purchase Tele+ and to subsequently create a single Italian pay-TV company on one platform.

On April 30, 2003, the agreement announced on October 1, 2002 was finalized between Telecom Italia and News Corporation for the creation of Sky Italia, a company that came into being as a result of the merger between Stream and Tele+.

Following this transaction, Telecom Italia sold a 30.1% stake in Stream: 25% to News Publishing Australia Limited and 5.1% to SGH STREAM SUB, Inc..

After this transaction, Telecom Italia holds 19.9% of Sky Italia; the remaining 80.1% is held by News Corporation.

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Competition

Fixed-line Domestic and International Telecommunications Services

Pursuant to the telecommunications regulations approved by Presidential Decree No. 318 of September 19, 1997, which became effective on October 7, 1997 (the Telecommunications Regulations), fixed-line public voice telephony services and the operation of the fixed-line network for the provision of such services was liberalized effective January 1, 1998. Until January 1, 1998, the Telecom Italia Group was the sole provider of fixed-line public voice telephony services, which consist of local, long distance and international telecommunications services, in Italy. In addition to fixed-line public voice telephony services, over the last six years there has been increasing liberalization of all other business areas in which the Telecom Italia Group operates. The operation of telecommunications infrastructure for the provision of all telecommunications services other than fixed-line public voice telephony services was opened to competition by the Telecommunications Regulations and Law No. 249 of July 31, 1997 (the Maccanico Law), during 1997. As a result of the complete liberalization of the market for telecommunications services, the Telecom Italia Group has faced increasingly significant competition since 1998 in the Italian domestic market, including competition from foreign telecommunications operators, particularly with respect to medium-sized and large business customers.

The legal framework for regulation in the telecommunications sector in Italy was completely transformed, as a consequence of the adoption of the Maccanico Law (effective August 1, 1997), the Presidential Decree No 318/97 (the Telecommunications Act) (effective September 22, 1997) and a series of Orders issued by the National Regulatory Authority which have been important to the Telecom Italia Group as it has faced increasing competition. To date the regulatory environment has been characterized by an intensive implementation process in order to complete liberalization. The trend continued in 2003 as additional steps were taken regarding tariff rebalancing, interconnection charges and the further signing of contracts to permit the unbundling of the local loop. See Regulation .

Since the beginning of 1997 about 170 licences have been activated in Italy, although at the end of 203 only 17 OLOs were still actively operating on the market, as the others failed or were involved in merger and acquisition operations. Wireline in its domestic market faces, among others, two national players, Tele2 and Wind, and three other focused competitors: Fastweb (focused on broadband and specific cities), Albacom (focused on business customers) and Tiscali (focused on internet). Only two of these competitors have their own network facilities, Fastweb and Albacom, while the others implement a reseller model utilizing Telecom Italia s network.

In addition, the Italian fixed telecommunications market has been influenced by the development of mobile operators that attract voice traffic through their wide range of Value Added Services and more personalized terminals.

In this competitive environment during 2003 Wireline increased revenues and improved profitability as a result of:

- The increase of its market share on traffic both on Voice-Online (an increase of 0.6% compared to December 31, 2002) and Voice (an increase of 0.5% compared to December 31, 2002), due to the stabilization of its subscriber lines volume, as the unbundling of the local loop has not yet had a material impact, and the successful performance of its winback and loyalty campaign with more than 1.8 million customers acquired and retained from competitors and more than 5.5 million loyalty packages subscribed (21% of total customer base).
- The strong growth achieved in Broadband with 2,200,000 access lines at the end of 2003, of which 160,000 abroad, 1,350,000 more access lines than at the end of 2002.

- The result achieved on Innovative Data Transmission (+42% compared to the end of 2002) and Value Added Services on Data (+30% compared to the end of 2002).

The implementation of a new marketing approach on fixed line services by developing a new mobile-like handset Aladino that enables customers to utilize innovative voice VAS (SMS, MMS, News, Weather and others), the first step towards more Personalized communication and Videocall .

Mobile Telecommunications Services

The Italian Mobile Market. The mobile telephone market continued to grow in Italy in 2003, but at a slower pace (3.6% in 2003 compared to 7% in 2002 and 21% in 2001). By December 31, 2003, the number of cellular phone lines reached 56.8 million, corresponding to a penetration rate of around 99% of the population.

After several years of strong growth, the demand growth curve has reached its inflexion point and the remaining potential market will be smaller than the one already acquired. In addition, the increasing saturation means that new customers to be acquired are likely to result in lower revenues per customer as has been the case in recent years. Competition for mobile telecommunications services remained strong in 2003. Consequently TIM s strategy has been focused on strengthening its leadership with high level valuable customers through innovative offers, CRM actions, quality performance, reinforcement of the core voice business and marketing VAS.

There are three principal competitors to TIM in the Italian mobile market: Vodafone Omnitel, Wind and H3G(3). At December 31, 2003 TIM remained the market leader with a market share of approximately 46% with Vodafone Omnitel, Wind and H3G(3) having market shares of 36.3%, 17.2% and 0.6%, respectively. In 2003, TIM had a 27.3% market share of net additional GSM lines, corresponding to 0.8 million of net lines, compared to 1.6 million for Vodafone Omnitel, 1.2 million for Wind and the remaining 0.4 million attributable to H3G (3).

TIM s statistical data excludes 700,000 silent lines. The Italian market, which has a high penetration of prepaid cards, is characterized by certain customers acquiring multiple lines in order to take advantage of specific/time-limited commercial offers. Once these offers expire these customers tend not to continue the use of such lines which is facilitated by the prepaid nature of the arrangement. As a result, TIM excludes the silent lines in order to provide greater consistency between the number of lines managed by the Company and the development of the business.

The Regulatory Framework

In a scenario of increasing liberalization, the decisions taken by the National Regulatory Authority have greater impact. The most significant measures taken by the National Regulatory Authority were the designation of TIM and Omnitel as providers with considerable market strength in terms of cellular service, interconnection, the definition of new pricing scheduled for fixed-to-mobile communications, and the introduction of mobile number portability.

TIM s role in the New Economy. The opportunities offered by new technologies will accelerate the ICT (Information and Communication Technology) convergence process, linking the two currently fastest growing businesses: mobile communications and the Internet. TIM s strategic choice with respect to this convergence is the open model. TIM will not focus on internet content but, rather, it will create alliances with the best content producers in order to provide its customers with the most innovative and the widest range of opportunities, while guaranteeing customers transaction security.

Traditional Business and Value Added Services. The development of new advanced services will necessarily lead to changes in TIM s revenue structure. Value Added Services have and will continue to account for a rising proportion of revenues compared to those generated by voice traffic. TIM s growth will be increasingly dependent on its ability to develop data traffic and innovative services.

This means the mobile sector is one of the segments with the highest potential growth rates and profitability. Technological developments and data transmission will generate new business models based on the capability of offering information, entertainment and advertising through mobile phones and of executing an increasing number of commercial and banking transactions.

TIM will seek out commercial synergies with web-oriented companies on the market which will increasingly demand mobile services (information and media, on-line banking and trading, geographic positioning information system).

In this regard TIM will leverage on the competitive advantage related to the integration of different technologies and networks (GPRS, EDGE and UMTS) so that the services offered are available regardless of the network being used at any given moment.

EDGE which at present involves only upgrading the GSM/GPRS software and which is complementary to UMTS will permit TIM customers to have prompt access to the main third generation services. The EDGE launch will bring an important competitive advantage for TIM. TIM will be able to offer services in Italy with a network speed similar to that of UMTS (200 kbit/s for EDGE vs 384 kbit/s for UMTS). In fact, due to the availability of dual mode terminals (EDGE/UMTS) that will be marketed with the Turbo TIM brand, TIM customers will be able to use the band they need for a specific service regardless of the network they are using.

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UMTS will be the natural evolution of EDGE: UMTS was launched in May 2004 for corporate clients and will he launched at Christmas 2004 for the mass market when handsets will be available in volumes and the technology will be more reliable.

TIM is the sole operator with a firm commitment to EDGE in addition to UMTS. Currently, only H3G(3) has provided a complete offer for the UMTS technology, while Vodafone Omnitel, consistently with TIM, expects to fully implement UMTS services during 2004.

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REGULATION

Overview

The legal framework for the regulation of the telecommunications sector in Italy has been extensively revised in the last decade. This revision included the liberalization of all telecommunications services including the provision of fixed-line public voice telephony services and the operation of networks to support the provision of such services, which were opened to competition as of January 1, 1998. Most importantly, the legal framework for regulation of the telecommunications sector in Italy has been completely transformed through the establishment of the National Regulatory Authority, and the adoption of the Telecommunications Regulations by the Italian Government pursuant to Law No. 650 of December 23, 1996 (Law 650), and Law No. 189 of July 1, 1997 (Law 189) to implement a number of EU directives in the telecommunications sector, the general objective of which was to create a framework for a fully competitive telecommunications market. Effective August 1, 1997, the former Ministry of Posts and Telecommunications changed its name to the Ministry of Communications pursuant to the Maccanico Law. The Telecommunications Regulations (Presidential Decree No. 318 of September 19, 1997) became effective on October 7, 1997, and have been implemented by specific regulations. The Framework Law in general aimed at:

- ensuring the improvement of competition and efficiency in the telecommunications sector;
- establishing adequate quality standards;
- ensuring access to telecommunications services in a homogeneous manner throughout Italy;
- defining a clear and transparent tariff system based on the price cap method which, pursuant to the Maccanico Law, applied to the Telecom Italia Group s fixed public voice telephony services for up to two years starting on August 1, 1997. The National Regulatory Authority applied the price cap to Telecom Italia fixed public voice telephony from August 1, 1999 to December 31, 2002; and
- protecting consumers and users interests.

The Telecommunications Regulations completed the liberalization of the provision of all telecommunications services and the operation of all telecommunications networks in Italy, effective from October 7, 1997, except for the provision of fixed public voice telephony services and the operation of telecommunications networks to support provision of such services, which were liberalized as of January 1, 1998. Restrictions on other operators providing telecommunications services, other than fixed-line public voice telephony services and the operation of telecommunications networks, had been lifted by several previous measures, including the National Telecommunications Plan referred to in a Ministerial Decree of April 6, 1990 (the NT Plan), Law Decree No. 55 of February 11, 1997 (satellite communications) and Law Decree No. 103 of March 17, 1995 (Decree 103) and its implementing decrees and regulations (data communications, voice telecommunications for closed user groups and Value Added Services).

The Telecommunications Regulations included provisions concerning:

- the granting of general authorizations or individual licenses to provide telecommunications services;

- universal service obligations and the mechanism for funding the net cost of such obligations;
- access deficit contributions;
- special obligations imposed on operators having significant market power, including the determination of interconnection charges using principles of cost orientation;
- numbering, carrier selection and number portability;
- rights of way; and
- the essential requirements that must be complied with in the provision of services and when interconnecting with public telecommunications networks.

The National Regulatory Authority has established detailed regulations governing the telecommunications sector and has monitored their application, while the Ministry of Communications has retained the responsibility for defining telecommunications policy in Italy. See The Telecommunications Regulations and Implementing Regulations.

The activities of Telecom Italia and TIM were subject to the terms and conditions of their public operating concessions (the Public Concessions) which were the basis under which telecommunication services were provided by Telecom Italia and TIM prior to adoption of the Telecommunications Regulations. The Public Concessions were expected to be made consistent with the new regulatory framework by January 1, 1999, as required by the Telecommunications Regulations but the National Regulatory Authority only started the procedures to achieve such amendments at the end of December 1999. See Public Concessions .

Since January 2001, Telecom Italia has been operating pursuant to a license (Order No. 820/00/Cons). See The Telecommunications Regulations and Implementing Regulations .

Other significant telecommunications measures include Ministry of Communications decrees, Presidential decrees and other regulations as well as orders of the National Regulatory Authority issued since its formation.

A new regulatory framework has been introduced in Italy by the incorporation of recently adopted EC Directives, the Framework directive together with three others on Access , Authorization and Universal Service (the Data Protection directive was implemented separately). The new rules have been effective in the national regulatory framework since September 16, 2003. In this connection, Law No. 166 of August 1, 2002, gave the Government a mandate to implement the new directives, and to adopt a code of legal and regulatory measures in the field of telecommunications. Furthermore, the European Commission published Recommendations on important product and services markets in electronic communications, as well as Guidelines for market analysis and the evaluation of significant market power.

The new Electronic Communications Code (the Code) implemented the Directives without substantial changes or departures from the text adopted at European Union level. In implementing the Directives, the Code expressly abolished the former legal framework for regulation of the telecommunications sector in Italy mainly represented by the Telecommunications Regulations, which had been effective since October 7, 1997.

The main characteristics of the Code are as follows:

- redefinition of the concept of significant market power and of the criteria for imposing obligations on certain operators, with the introduction of market analysis;
- the introduction of the term electronic communication services and networks (a broader term which now encompasses the term telecommunications);
- electronic communication services and networks can now be provided pursuant to a general authorization ;
- more flexibility by national regulatory authorities to select which access and interconnection obligations to impose on operators notified as having significant market power in a relevant market; and
- redefinition of certain measures relating to retail price regulation and extension of number portability to mobile operators.

Moreover, the Directives (and other EU-related regulatory interpretations and recommendations) as implemented by the Code provide for guidelines on market analysis and calculation of significant market power and identify 18 markets at retail and wholesale level where such analyses and identification shall be conducted. According to the Code, the Italian National Regulatory Authority will have to conduct a new evaluation of the operators having significant market power and propose applicable remedies. Within the authority allowed by EU law, the Code also provides for the following:

- allows the trading of the rights of use of frequencies among operators, offering the same type of services;
- excludes from the category of universal service (and its related obligations), the provision of directory information services;
- provides for specific and more defined rules aimed at reducing the burden of current legislation and local regulations which discipline the installation of networks;
- redefines the assignment of roles and responsibilities among the Italian Ministry of Communications and the National Regulatory Authority mainly by assigning to the Ministry of Communications the task of supervising the authorization process and compliance with the universal service obligations and to the national regulatory authority the task of conducting market analyses and proposing remedies.

The Code also introduces a new definition of and specific references to broadband services , encouraging their development also at regional level. See EU Telecommunications Law and Regulation The 1999 Review.

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The National Regulatory Authority (AGCOM)

The National Regulatory Authority consists of a President that has been appointed by the Italian Government through a Presidential decree, a Committee for Infrastructures and Networks, a Committee for Products and Services and the Council. Each of the Committees members is selected by the Italian Parliament (four by the Senate and four by the Chamber of Deputies) and appointed through a Presidential decree. Each of the Committees and the Council is responsible for establishing regulations for their specific areas.

The Committee for Infrastructures and Networks is responsible for, among other things, allocating radio frequencies relating to telecommunications services; defining objective and transparent criteria for establishing tariffs for interconnection and network access; regulating relationships among telecommunications companies; settling disputes regarding interconnection; and defining the scope of the universal service obligation and the operators subject to it, together with criteria for calculating and sharing its costs.

The Committee for Products and Services is responsible for, among other things, regulating product quality and conformity with EU directives governing the relationship between companies controlling fixed or mobile telecommunications networks and telecommunications service providers.

The Council is responsible for adopting regulations establishing criteria for issuing licenses for the telecommunications sector and for TV and radio activities (including cable and satellite broadcasting).

The National Regulatory Authority is responsible for:

- market analysis as defined by the Code;
- preparation of regulations in the telecommunications field;
- establishment of the criteria to be followed by operators in determining tariffs;
- monitoring operators to ensure their compliance with such tariff criteria;
- ensuring, where appropriate, accounting separation between different activities carried out by the same operator;
- monitoring of the performance of services to ensure compliance with contracts and qualitative levels of service;
- issuance of directives regarding quality of services;
- examination of complaints filed by users and customers in relation to quality of services and the level of tariffs;

- control of steps taken by operators to ensure equal treatment of their customers and verifying periodically the quality of the service provided;
- control of operators compliance with the general principles issued by the Italian Government and the National Regulatory Authority in relation to public services.

The National Regulatory Authority has been operational since June 1998.

The National Regulatory Authority has investigative powers, as well as the authority to impose sanctions on operators who do not comply with their directives and resolutions. In addition, the National Regulatory Authority is entitled to propose to the Ministry of Communications the revocation and/or suspension of general authorizations and individual licenses in the event of repeated violations by the holder. The Maccanico Law also permits the National Regulatory Authority to limit access to networks for security reasons.

The Code and Implementing Regulations

The principal provisions contained in the Code, which affect the provision of telecommunications services by the Telecom Italia Group and its competitors in Italy relate to:

- universal service obligations;
- obligations imposed on operators having significant market power, in particular with respect to interconnection agreements and accounting policies;
- numbering (carrier selection, preselection, and number portability);

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- rights of way;
- authorizations; and
- introduction of new broadband services.

Universal Service Obligations

The universal service obligations include the provision of fixed-line public voice telephony service, publication of telephone directories, public payphones, free emergency call services and special services for disabled or disadvantaged people. To date Telecom Italia is the only operator subject to the universal service obligations, although similar obligations could be imposed on other operators. In such an event such other operators will be required to provide all or part of the services included in the universal service obligations on all or part of the national territory, under reasonable and non-discriminatory conditions. The net costs for the provision of the universal service is calculated on a long run forward-looking incremental cost basis. The telecommunications operators providing fixed-line public voice telephony service or mobile and personal communications services are required, under certain circumstances, to contribute to such costs.

Telecom Italia submitted the net cost of providing universal service for the first time for the year 1998. The National Regulatory Authority concluded that for 1998 the costs of such service were not an unfair burden for Telecom Italia. The National Regulatory Authority appointed an independent advisor to audit the 1999 net costs submitted by Telecom Italia. On August 1, 2000, the National Regulatory Authority recognized a net cost for the provision of the universal service in the year 1999 of 62.4 million. The operators obliged to contribute to finance such net cost were: (a) Telecom Italia (57.1%); (b) TIM (28.1%); (c) Omnitel (13.8%), and (d) Infostrada (1%).

With Order No. 8/00/CIR Telecom Italia was requested to provide an assessment on the net cost foreseen for the year 2001, together with information regarding areas and customers estimated as not profitable, in order to allow the National Regulatory Authority to launch a public consultation aimed at determining the guidelines for the provision of the universal service on a competitive basis. On January 31, 2001, pursuant to the same Order, Telecom Italia filed its evaluation for the year 2001. On July 12, 2001, the National Regulatory Authority opened a public consultation in order to assess the possibility of using a bidding procedure for the assignment to operators, other than Telecom Italia, of all or part of the obligations relating to the universal service. The outcome of the consultation was published on January 17, 2002. No decision has been taken by the National Regulatory Authority.

In connection with the net cost for the year 2000 submitted by Telecom Italia, the National Regulatory Authority recognized a net cost of 58.9 million, of which Telecom Italia contributes 48.3%. OLOs obliged to contribute to finance such net cost are: TIM (31.4%); Omnitel (18.9%), and Infostrada (1.4%).

Regarding the net cost of 1999 and 2000, reimbursements have not yet been fully paid to Telecom Italia by the other operators, as some of them have filed a claim in the Administrative Court.

With respect to 1999, on January 27, 2002, the Administrative Court issued a decision in favor of the OLOs, based only on procedural matters. Consequently, the procedure for the evaluation of the net cost for 1999 was re-opened by the National Regulatory Authority. With Order No. 5/03/CIR the National Regulatory Authority issued a final decision confirming its Order No. 8/00/CIR. However the Italian Supreme Administrative Court, by Decision No. 7257/03 of November 2003, decided to re-open the case. The National Regulatory Authority will intervene again during 2004 in order to definitively assess the matter.

Decision from the Court on costs of 2000 is still pending.

In December 2001, the National Regulatory Authority published rules designed to grant to low income and to disabled customers certain reductions of the monthly rental fee for voice telephony services.

Telecom Italia was confirmed by the Code as the operator with the obligation to supply the Universal Service under the conditions laid down in the regulations.

The National Regulatory Authority approved the net cost sustained by Telecom Italia to provide the Universal Service in 2001 of 40.52 million, to which Telecom Italia itself is to contribute 42.68% (17.29 million), the remaining cost being funded by OLOs (TIM, Vodafone, WIND, Infostrada).

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As far as 2002 is concerned, the National Regulatory Authority is evaluating the net cost presented by Telecom Italia of 158 million. A final decision should be issued by June 2004.

Special Status of Operators Having Significant Market Power

In the old regulatory regime telecommunications operators operating fixed-line or mobile networks, or offering fixed public voice telephony services, leased lines or international circuits, were subject to special obligations with respect to interconnection and accounting policies if they had Significant Market Power (SMP). An operator was presumed to have Significant Market Power if its share of the relevant market was greater than 25%, although the National Regulatory Authority might determine that an operator having a market share greater than 25% did not have Significant Market Power, in view of the operator s ability to influence market conditions and its access to financial resources, or that an operator with a market share lower than 25% had such power.

Starting from August 2003, with the introduction of the new European Framework, criteria for the identification of Significant Market Power have changed: the European Commission, with its Recommendation C(2003)497, identified 18 separate markets; the National Regulatory Authority will have to carry out a separate Market Analysis in each market, in order to identify:

- the level of competition in each market;
- the need to indicate one or more operators as having Significant Market Power;
- the appropriate remedies, i.e. the rules to apply, if the case, to ensure appropriate competition.

In April 1998, Telecom Italia was identified as an operator having Significant Market Power in the markets of fixed telecommunications networks, fixed-line public voice telephony services, leased lines and interconnection services. Telecom Italia was the sole operator identified as having Significant Market Power for the above-mentioned markets. In April 1998, TIM was identified as having Significant Market Power in the market of mobile telecommunications services. See EU Telecommunications Law and Regulation The 1999 Review .

With order 197/99 the National Regulatory Authority in September 1999 also determined that TIM and Omnitel had Significant Market Power for mobile telecommunications services and for domestic interconnections. The National Regulatory Authority reviews and evaluates Significant Market Power operators every year. In 2001, the National Regulatory Authority started a market analysis to identify the operators with Significant Market Power in the year 2000. In addition, on August 7, 2002, the National Regulatory Authority started a procedure to identify telecommunications organizations with Significant Market Power for 2001.

The National Regulatory Authority concluded its inquiry with the aim of identifying the operators with Significant Market Power in the Internet access market (Resolution No. 219/02/CONS sent to Telecom Italia on July 31, 2002) and the SMP 2000 inquiry (Resolution No. 350/02/CONS).

Significant Market Power Internet

In its approval of the measure granting equal status to ISPs and OLOs (Law No. 59/2002), the Parliament ruled that, within two months of the law coming into effect (by June 26, 2002), the National Regulatory Authority would update the list of operators with Significant Market Power in the Internet access market.

In Resolution No. 132/02/CONS of April 24, 2002, the National Regulatory Authority commenced the inquiry by conducting a public consultation with the aim of Updating the list of operators with significant market power on the Internet access market [..] which concluded with Resolution No. 219/02/CONS. This Resolution identified Telecom Italia and Wind as operators with Significant Market Power in the market of calls terminating on the Internet using dial-up technology, and also identified Telecom Italia alone in the final market of switched Internet access services from the fixed network. The Resolution, which became effective immediately, referred to Presidential Decree No. 318/97 for the remedies (publication of interconnection price lists, separate accounting, cost orientation, etc.) which the two operators are bound to respect.

Significant Market Power 2000

In Resolution No. 350/02/CONS the National Regulatory Authority confirmed for the year 2000 that the following operators had Significant Market Power:

1) Telecom Italia in the markets of public fixed telephone networks and services, leased line systems, and the national interconnection market;

2) TIM in the markets of public mobile and national interconnection communications systems (termination);

3) Vodafone Omnitel in the markets of public mobile and national interconnection communications systems (termination).

As far as the named operators are concerned, this special status automatically imposed a series of extra legal obligations over and above those which all telecommunications operators are normally expected to fulfill: cost orientation of interconnection prices (and also of retail/leased lines for Telecom Italia), transparency, non-discrimination, and, only for Telecom Italia, separate accounting.

Telecom Italia was designated as an operator with Significant Market Power in the interconnection market, despite having reduced its market share in 2000 to approximately 11% (based on revenues).

Significant Market Power 2001

An inquiry was begun by the National Regulatory Authority on August 7, 2002. An official decision was taken on May 7, 2003, and published in Resolution No. 160/03/CONS of June 3, 2003. The Resolution confirmed for the year 2001 Telecom Italia as having Significant Market Power in the market of public fixed telephone networks and services, leased line systems, and the national interconnection market, as well as TIM and Vodafone Omnitel in the markets of public mobile and national interconnection (termination).

Under the new European regulatory framework, the National Regulatory Authority is in charge of carrying out market analyses. In order to do this, the National Regulatory Authority separated the most important markets according to current laws (Presidential Decree No. 318/97 and Law No. 59/02) into the 18 markets identified by the recommendation of the European Commission, and has entrusted a large part of the above-mentioned analyses to external consultants.

During 2003, the National Regulatory Authority should have conducted the market analyses in order to propose applicable remedies by means of public consultation. However, the National Regulatory Authority only stated the criteria for conducting the market analyses. As the National Regulatory Authority has not yet conducted the market analysis in the identified markets to determine significant market power it is not possible for Telecom Italia to determine the overall impact on its business of the new regulatory regime.

Finally, on March 20, 2002, the National Regulatory Authority began an inquiry into Enel/Wind to verify whether, according to Article 9, sub-section 2 of Presidential Decree No. 318/97, it is necessary to adopt separate accounting directives with regard to Wind, and to impose restrictions ex ante regarding the use of infrastructures associated with special and exclusive rights, including access to information about the users of electricity.

Interconnection

Telecommunications operators providing fixed-line public voice telephony services, mobile telecommunications services or leased line systems and having Significant Market Power are required to negotiate and enter into interconnection agreements at the request of other operators wishing to provide telecommunications services, to apply non- discriminatory terms and to communicate copies of their interconnection agreements to the National Regulatory Authority. Public fixed network operators and leased line service providers having Significant Market Power are required to publish a Reference Interconnection Offer (RIO).

On April 18, 2002, Telecom Italia published the RIO 2002 for Interconnection and Unbundling 2002. The offer was successively integrated with Partial Circuits and FRIACO services (April 30, 2002), with PVC (Permanent Virtual Channel) ADSL and HDSL services (June 14, 2002), and with billing services (July 4, 2002).

With Order No. 2/03/CIR of February 27, 2003, the National Regulatory Authority asked Telecom Italia to integrate the RIO with other services (e.g. interconnection links at 34 and 155 mbps rates) and to modify the economic conditions of traffic conveyance services (origination, termination and transit) and other services such as number portability and Partial Circuits. Consequently, Telecom Italia published a new RIO 2002 on March 27, 2003.

On the same date of Order No. 2/03/CIR, the National Regulatory Authority published Order No. 3/03/CIR, which (on the basis of the previous Order No. 152/02/CONS) introduces a network cap , a mechanism for defining in advance the rules for pricing RIO services according to the RPI (Retail Price Index) and productivity factors. The network cap applies for the period 2003-2006. Order No. 152/02/CONS also established non discrimination criteria in interconnection and wholesale market between Telecom Italia and the other licensed operators:

- same conditions to other licensed operators as applied to its retail units;
- further obligations of accounting separation;
- functional separation between network and retail units; and
- price squeeze tests for retail offers.

In compliance with Order No. 3/03/CIR, Telecom Italia submitted the RIO 2003 on April 11, 2003, which has been evaluated and approved by National Regulatory Authority with Order No. 11/03/CIR.

On October 31, 2003, Telecom Italia published the RIO 2004 which has been evaluated and approved by the National Regulatory Authority with Order No. 3/04/CIR.

Local Loop Unbundling

With Order No. 2/00/CIR issued on March 16, 2000, the National Regulatory Authority published the general guidelines regarding the services that must be offered by Telecom Italia on an unbundled basis: twisted copper pairs; fiber optics; access extension (lines between switches), and digital transmission channels (i.e., digital circuits between the local office of Telecom Italia and the operator s point of presence) and the related economic pricing criteria, based on fully distributed historical costs. The Order allows other operators to have direct access to end users (customers) by leasing the network components from Telecom Italia (full unbundling) as well as leasing only the high bandwidth (shared access).

Telecom Italia appealed this Order to the Regional Administrative Court (TAR Lazio), in particular with respect to the inclusion of fiber optic in the mandatory offer and the costing criteria. On May 12, 2000, Telecom Italia put forward a Reference Offer for Local Loop Unbundling, for approval by the National Regulatory Authority. The National Regulatory Authority finally issued Orders 13/00/CIR and 14/00/CIR, respectively on December 30, 2000 and in January 2001. The former regards the technical and procedural aspects of the provisioning of local loop unbundling and co-location. The latter sets the rates for the unbundled services.

Telecom Italia published a revised Reference Offer for 2000 on January 31, 2001.

During 2001, in line with the suggestions made by the National Regulatory Authority, special areas were made available in exchanges to accommodate other operators with the aim of unbundling local loops. By December 31, 2001 Telecom Italia handed over equipped technological areas to operators in 748 exchanges. In addition, following Resolution No. 24/01/CIR, on December 12, 2001, Telecom Italia presented its rate plan to the National Regulatory Authority for shared access and sub loop (shared access to the local network and access to line boxes).

On April 18, 2002, Telecom Italia published the Reference Offer of Local Loop Unbundling for 2002, with price reductions for copper pair. On March 2002, around 17,400 unbundled lines were in place, 27 licensed operators requested co-location, 1,043 local switches for co-location were requested by licensed operators and 919 sites were ready for co-location.

On June 24, 2002, Telecom Italia presented to the National Regulatory Authority a Virtual Unbundling offer, which offers carrier preselection, inclusive of the payment for the unbundling charge wherever it is temporarily impossible to offer co-location. On September 16, 2002, following a number of meetings with the National Regulatory Authority, Telecom Italia further reduced the price of some unbundling services:

- shared access: the monthly subscription rate was reduced from euro 4.34 to euro 2.80; the activation charge was reduced from euro 94.36 to euro 81.00;
- full unbundling: the monthly subscription rate for the ADSL pair was reduced from euro 12.60 to euro 11.10;
- the fee for qualification of the ADSL pair was reduced from euro 39.51 to euro 10.37.

On February 27, 2003, with Order No. 2/03/CIR, the National Regulatory Authority approved Telecom Italia s Reference Offer for 2002 (RIO 2002), after hearing the opinions expressed by the Antitrust Authority and

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the European Commission, and after Telecom Italia s submission to the National Regulatory Authority of its regulatory accounting for 2001, which took place on December 20, 2002. The RIO 2002 applied to other local operators for the use of Telecom Italia s network, and provided criteria for changing the charges of the RIO 2002 starting in 2003 for the next four years (the so-called network cap).

Order No. 02/03/CIR confirmed the monthly rental fees of LLU and set a reduction of activation fees. As regards co-location services, the Order asked the application of internal Telecom Italia costs (approximately a decrease of 40%) to the square-meter costs for co-location paid by OLOs. Furthermore the integration of the offer with the coming services is required.

As regards RIO 2003, Order No. 03/03/CIR of February, 27 2003, asked Telecom Italia to set the monthly rental fee on the basis of the following criteria: a) the best European tariff, b) the anticipation of efficiency on operational costs, c) the non discrimination principle and d) on the basis of the cost structure of access network assets. In the RO 2003, approved by Order No. 11/03/CIR, Telecom Italia published the price for the monthly rental fee for LLU, fixing it at 8.30, which represented the best price in the EU Countries (the incumbent Danish operator price). Order No. 11/03/CIR included additions and changes, particularly regarding the application of the network-cap mechanism, introduced with Order No. 03/03/CIR, for the offer of certain interconnection lines, and for co-sharing, local loop unbundling, partial lines and permanent virtual lines services.

Due to the delay in fixing the cap for the LLU service by the National Regulatory Authority, Telecom Italia published the RIO 2004 on October 31, 2003, maintaining the same level of price for LLU service (8.30/month) as the RO 2003 (even though the incumbent Danish operator price for LLU has now increased to 8.60).

Leased lines

According to Order No. 304/03/CONS issued on August 5, 2003, by the National Regulatory Authority, Telecom Italia published a new retail and wholesale leased line offer that has been approved with Order No. 440/03/CONS on January 29, 2004.

In respect of the previous offer (approved by Order No. 711/00/CONS) the new one introduces a price reduction of between 5.25% and 7% for the retail offer and of 12% for the wholesale offer.

Mobile termination rate

According to the GSM Concessions (as defined below) of December 1994, mobile network operators were responsible for fixing tariffs for calls originated on the fixed network and terminated on mobile networks. Such regulatory framework has been modified by DPR 318/97 establishing, as a new principle, that the originating operator is responsible for fixing the retail tariff. This principle has been reaffirmed by the National Regulatory Authority with Order No. 85/98. Since issuing this order the National Regulatory Authority has started an assessment of termination rates charged by mobile network operators and with Order No. 338/99 it set 19.0 eurocents/min, the maximum average termination price. The National Regulatory Authority has deemed it necessary to issue new regulations and on February 5, 2003, issued Order No. 47/03 setting new maximum values for the termination rates applied by mobile operators (TIM and Vodafone Omnitel) for calls originated on third fixed networks. The ceilings for mobile termination charges have been established at 14.95 eurocents/min, as from June 1, 2003. For 2004 and 2005 the National Regulatory Authority has envisaged a mechanism (so called network cap) for the planned reduction of termination costs of fixed-mobile which would be introduced along with the improvements and fine-tuning of the regulatory accounting system based on incremental costs and the review of the obligations following the implementation of the new European regulatory framework. The National Regulatory Authority believes that, within this framework, a planned reduction of a maximum of 10% per year minus inflation in 2004/2005 would be reasonable; no decision has been taken yet.

Accounting Policies

Operators having Significant Market Power are required to have an accounting system showing their costs in a transparent manner. Upon request, such operators must provide the National Regulatory Authority with a description of their cost accounting system to verify compliance with the provisions of the electronic telecommunications regulatory framework. Moreover, operators of fixed public networks and mobile networks and providers of fixed public voice telephony services, mobile telecommunications services and leased line services with significant market power must keep a separate accounting system distinguishing between the activities related to the building and operation of public telecommunications networks, the activities related to the provision of telecommunication services, the interconnection offering and the universal service provision.

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The National Regulatory Authority chose KPMG as the independent advisor for the auditing of the accounting separation reports. In accordance with the Telecommunication Regulations, on September 4, 2000, Telecom Italia submitted the Regulatory Accounting Reports for the year ended December 31, 1999 to the National Regulatory Authority. On September 14, 2001, the Regulatory Accounting Reports for the year ended December 31, 2000 were also submitted to the National Regulatory Authority.

Due to a delay in the appointment of the independent advisor, the results of the audit on 1999 and reports were published only on November 6, 2002, with Order No. 337/02/CONS. The results of audit on 2000 Reports were published in March 2003 with the Order No. 48/03/CONS.

On June 17, 2002, the National Regulatory Authority issued Order 152/02 CONS which requires Telecom Italia to provide more detailed accounting reports on a current cost basis (fully allocated costs); the cost basis previously adopted was the historical one. In compliance with Order No. 152/02 CONS in December 2002, Telecom Italia submitted the Regulatory Accounting Reports for the year 2001 the auditing of which is in progress. During 2001 the National Regulatory Authority issued an order which raised the allowed return on capital employed WACC (weighted average cost of capital) for regulatory purposes from 12.5% to 13.5% before taxes.

TIM cost accounting policy

According to Order No. 197/99 TIM and Vodafone Omnitel have been notified as a Significant Market Power operator in the national interconnection market and must provide a cost oriented fixed-mobile termination rate.

On the basis of Order No. 338/99 TIM was required to implement cost accounting report in order to calculate a fixed-mobile termination rate. In accordance with Order No. 340/00, in 2001 TIM produced a cost accounting system based on Fully Allocated Historical Cost Data for the year 1999 (positive certification was issued by the advisor of the National Regulatory Authority at the end of 2002). It also introduced an accounting system based on a FAC-CC model (Fully Allocated Cost on a Current Cost basis), as an intermediate step towards the adoption of long-run incremental costs to determine the fixed mobile rates. In December 2001 the National Regulatory Authority adopted Order No. 485/01 requiring the SMP operators to prepare historical accounts for the year 2000.

With Order No. 399/02, the National Regulatory Authority requested both historical cost data and current cost data for the year 2001; it also required a long run incremental cost orientation for the year 2002 as the last step for cost orientation. Subsequently, with Order No. 47/03/CONS, the National Regulatory Authority decided to implement a three-year Network Cap mechanism (2003-2005) to be applied to the termination rate, in order to grant a gradual reduction of this price. The application of the mechanism for the years 2004 and 2005 will be subject to a new decision, after the completion of the incremental cost modeling, and after the evidence forthcoming from the Market Analyses, under the new Regulatory Framework.

Numbering

In accordance with the Telecommunications Regulations and by the issuance of various Orders the National Regulatory Authority issued regulations related to Number Portability and Carrier Preselection as described below.

Number Portability (NP)

Since February 2000, following the National Regulatory Authority Order No. 4/99/CIR and 7/00/CIR, which is consistent with EU Directive 98/61/CE, SPP (Service Provider Portability) in fixed networks was introduced, including non-geographic numbers (Premium Rates, Freephone Numbers, Splitting Charges).

SPP allows an end user to retain his number independent of the organization providing service, in the case of geographic numbers at a specific location (same Local Area) and in the case of other than geographic numbers at any location. Implementation of SPP is related to negotiations and technical implementation timing among operators. Telecom Italia upgraded its network and operational systems to be in a position to offer NP consistent with the requirements of the regulations. NP for non-geographic numbers started in May 2000. NP for geographic numbers has been implemented, as well as its synchronization with the unbundling of the local loop.

NP for mobile services was established during 2001 and commenced in April 2002.

On March 28, 2002, the National Regulatory Authority issued Order No. 7/02/CIR: established that by November 30, 2002, the National Regulatory Authority would have determined the price of Mobile NP (per number costs) that should be equal to the one-off price that the operator receiving the customer/recipient must

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pay to the operator giving the customer/donor the price. Mobile NP would have been applied starting January 1, 2003. Per cost number should not be higher than the price applied to fixed-line services as established by Order No. 10/00/CIR at 10.02. In January 2003, The National Regulatory Authority issued a new Order No. 13/02/CIR setting a cap price for the portability charge. This charge can not be higher than the price established for Number Portability between fixed operators.

Carrier Preselection (CPS)

Carrier selection (call by call) has been operational since the end of 1998 for long distance (national and international) and fixed mobile calls. Carrier selection for local calls has been available since January 2000.

Since February 2000, in accordance with Order No. 3/99/CIR and No. 4/00/CIR, which introduced new obligations for the provision of Carrier Preselection (i.e., timing, minimum daily number of user activations), customers can make inter-district, international calls and calls to mobile networks using a pre-selected carrier as an alternative to Telecom Italia, without dialing the identifying code required. Since July 2000 customers have also been able to make local calls (within the same district) with a pre-selected operator.

On April 18, 2003, the National Regulatory Authority sent notice to Telecom Italia of Resolution No. 4/03/CIR concerning the Integration of measures with regard to CPS: standards relating to the disconnection of the service . The Order, adopted at the end of the preliminary proceedings which began on November 28, 2002, defines common measures relating to the disconnection of the CPS service, describing in detail the modes and time-scales involved in the disconnection of CPS services, to safeguard users, and stating precise obligations with regard to transparency for operators of the services.

Rights of Way

The Telecommunications Regulations prohibit public authorities from discriminating in the granting of rights of way for the installation of public telecommunications infrastructures. The National Regulatory Authority and the local public authorities can promote the sharing of such structures and rights of way. If the access to such rights of way cannot be granted to a new operator, the National Regulatory Authority and the local public authorities can allow the access to existing infrastructure. The parties involved agree on the commercial terms of the sharing of the existing infrastructure.

Decree Law No. 198 of September 4, 2002, establishes fundamental principles with regard to the installation and alteration of TLC infrastructures that are regarded as strategic, and fixes precise terms for the issue of authorizations, abrogating the procedure of environmental impact assessment (VIA) and limiting the financial responsibility of companies to expenses associated with installation operations, digging and occupation of public property. Law No. 166 of August 1, 2002, also defined the new standards relating to the installation, access and sharing of multi-service cables and of cable ducts that need to be built following construction and maintenance work on civil works.

The regulation of the rights of way is exhaustively treated in the new Code.

Public Concessions

The Telecommunications Regulations provided that by January 1, 1999, the Public Concessions were to be modified to make them consistent with the new regulatory framework, on the initiative of the National Regulatory Authority, with the aim of bringing the Public Concessions into line with the Telecommunications Regulations. All special or exclusive rights held by Telecom Italia under the former monopoly system, and not compatible with the introduction of competition, were to be considered abolished.

The National Regulatory Authority opened an inquiry on December 15, 1999, with the aim of bringing the Public Concessions into line with the new regulatory framework, modifying the content of the Public Concessions and eliminating the special and exclusive rights and obligations which were in conflict with the Telecommunications Regulations, such as approval by the Ministry of Communications of the long term and technical plans of Telecom Italia, the installation and operating of public telephone facilities in specific areas of the country, and the development of services in small centers.

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At the end of its inquiry the National Regulatory Authority issued three individual licenses and a general authorization to Telecom Italia formally notified on January 19, 2001:

- An individual license for the installation and provision of public telecommunications networks, and for the provision to the public of voice telephone services (modification of the concessions and associated agreements formerly granted to SIP, Iritel and Italcable).

- An individual license for the installation and operation of a network of coastal stations with the aim of providing mobile maritime services via Inmarsat satellite (modification of the concession and associated agreement formerly granted to Iritel).

- An individual license for the plant and operation of radio-electric boarder stations, and the supply of mobile maritime services and mobile services via satellite through Inmarsat terminals (modification of the concession and associated agreement formerly granted to Sirm).

- Authorization for the supply of satellite network and communications services (modification of the concession and associated agreement formerly belonging to Telespazio).

Each individual license included a list of specific charges, drawn up on the basis of the indications given by the ministerial Decree of November 25, 1997, containing Provisions for the issue of individual licenses in the telecommunications sector .

The licenses and authorizations issued to Telecom Italia have the same expiry date as the Public Concessions (2012, according to Article 14 of Law No. 359/92, containing Urgent measures for the rehabilitation of public finances).

Pursuant to Law No. 448 of December 23, 1998, a new fee was instituted from January 1, 1999, to take the place of the license fee payable under the previous regulatory regime. The amount of the operating fee was based on a sliding scale (2.5% for 2001, 2.0% for 2002 and 1.5% for 2003). The Ministerial Decree of March 21, 2000 established that the fee should only be applied to revenues from installation activities and the supply of public telecommunications networks, local telephone service and mobile and personal service.

Under its Public Concession, Telecom Italia had the right to provide all mobile public telecommunications services, regardless of the technologies used. These rights were transferred to TIM as a consequence of the TIM Demerger. In accordance with the Presidential Decree No. 211 of August 1, 2002, the duration of TIM s GSM concession is 20 years, commencing on February 1, 1995 (before such decree the duration was 15 years).

The Telecommunications Regulations provided that by January 1, 1999, the existing GSM concessions (the GSM Concessions) (Omnitel, now Vodafone Omnitel, also was granted a GSM Concession) were to be modified to make them consistent with the new regulatory framework. In March 2001 the GSM Concessions were transformed into individual licenses.

TIM is also a holder of an individual license for radio mobile analogical (TACS) public service, for radio mobile paging public service and for the installation of their relative networks. The term of validity for the license corresponds to that of the original concession (2012).

According to Resolution 286/02/CONS, issued by the National Regulatory Authority on September 25, 2002, all TACS frequencies are to be released and returned to the government, which would then reallocate them on GSM.

The entire reallocation and rationalization process of the GSM 900 MHz frequency band will take place over three time periods until expiry of the TACS system users scheduled for December 31, 2005. With Order No. 54/04/CONS, the National Regulatory Authority launched a public consultation on the procedures to assign new rights of use on GSM frequencies.

With the publication of the Code licenses have been automatically transformed into general authorizations (with individual usage rights for frequencies).

Licensed Operators

In October 2003, the number of operators licensed for the provision of both fixed voice telephony service and building public telecommunications networks and for mobile and satellite services granted by the Ministry of Communications and the National Regulatory Authority was about 160.

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In the segment of mobile telecommunications services, one license was granted to the third national mobile operator (DCS-1800, GSM) Wind, which started on March 1, 1999, and another license (only for DCS-1800) was granted to the fourth national operator Blu, which started on May 16, 2000. Wind is the sole Italian telecommunications operator that was granted both a mobile and a fixed license at the time it started its operations. Fixed licenses have also been awarded to TIM (February 2001) and Vodafone Omnitel. Mobile telecommunications services based on the DCS-1800 technology are also provided by the two GSM operators, TIM and Vodafone Omnitel.

The Italian government awarded five UMTS licenses in Italy in December 2000. TIM, together with Vodafone Omnitel N.V., WIND S.p.A., Andala S.p.A. (now H3G S.p.A.) and IPSE S.p.A., were awarded licenses to provide the third generation mobile services. TIM committed to pay 2,417 million for its license, with 2,066 million paid in December 2000 and 117 million paid in November 2001 and November 2002. The remaining 117 million were paid during 2003.

In 2002, Blu, the fourth operator, was acquired by TIM, with its customers transferred to Wind.

On August 1, 2002, TIM was granted individual licenses for the point multi-point system WLL on a frequency band of 27.5-29.5 GHz and a width of 112 MHz.

In accordance with Presidential Decree No. 211 of August 1, 2002, the duration of all individual licenses is now 20 years (before such decree the duration was 15 years). Transition towards the third generation will be gradual with an extensive launch of the service expected in 2004.

XDSL/ATM Broadband

In December 1999, Telecom Italia received temporary authorization from the National Regulatory Authority for the wholesale offering of ADSL/ATM access service to Other Licensed Operators and Internet Service Providers. In February 2000, Telecom Italia started the always on retail offering for fast internet access. The ADSL 640 wholesale offer has been partially modified by the National Regulatory Authority with order 217/00/CONS issued in April 2000. In February 2001, the National Regulatory Authority approved the Permanent Virtual Circuit (ADSL up to 2 Mbit/s and HDSL up to 155 Mbit/s technologies) offer as presented by Telecom Italia and authorized Telecom Italia to offer XDSL retail services branded as RING and FULL BUSINESS COMPANY from April 2001. At the end of 2003, ADSL 640 and XDSL wholesale services were available in 2,120 towns for about 80% of total lines on a national basis.

On April 15, 2003, the National Regulatory Authority with Order No. 6/03/CIR approved the Telecom Italia wholesale x-DSL offer for intermediate services which operators must acquire from Telecom Italia in order to supply ADSL to the public, unless they have their own infrastructures or do not use unbundling. The new range of services includes price reductions for ADSL access, the introduction of longer time-scales for starting to market new wholesale services based on the retail-minus principle, and the integration of an operators Service Level Agreement with regard to the disconnection of services.

On August 6, 2003, some Internet Service Providers filed a complaint to the European Commission claiming the abuse of dominant position of Telecom Italia in the market of broadband Internet access when bundling it with the provision of exclusive content for its clients.

Tariff and Pricing Policy

Overview

Telecom Italia operates in both domestic and international markets. Its pricing policy is established in accordance with existing regulations for regulated services, and in accordance with market and competitive factors.

Fixed Network. Management believes that it is essential for Telecom Italia to have the flexibility to price its telecommunications services selectively in order to counter increased competition.

With Order No. 171/99 the National Regulatory Authority described the rules to be applied by Telecom Italia in setting the tariffs for the services offered. The National Regulatory Authority distinguished two kinds of tariffs. The first required prior approval by the National Regulatory Authority and applied to:

- services under a price-cap obligation (RPI-X): the X is differentiated according to different levels of competition in the provision of the various telecommunications services (such as installation, connection charge, local voice calls, long distance voice calls, international voice calls);

- services under cost-orientation and accounting separation obligations: Interconnection, Special Access and Leased Lines, due to the Significant Market Power of Telecom Italia in the provision of these services; and
- services to be kept affordable , on the basis of the regulation concerning the universal service obligation.

The second category of tariffs required only a prior communication to the National Regulatory Authority itself and applied to so-called value added services for which a high level of competition exists.

In a new Order (No. 289/03/CONS) the National Regulatory Authority described the rules to be applied by Telecom Italia in setting tariffs for the services offered for the years 2003-2006 introducing a safeguard cap with the aim of maintaining price stability.

The new safeguard cap system provides for 3 different caps as described below:

- Access services, such as installation and connection charge: RPI-0 as well as a sub-price cap for residential subscription charges of RPI-RPI;
- Traffic services, such as local voice calls, long distance voice calls, fixed-mobile voice calls: RPI-RPI;
- Fixed/mobile services, limited to the fixed call segment belonging to Telecom Italia (the Retention segment): RPI-6%.

In Order No. 304/03/CONS of August 5, 2003, the National Regulatory Authority approved the criteria for the preparation of new rate plans for retail and wholesale leased lines. In particular, the Order involves the re-formulation of Telecom Italia s retail rate plans with a reduction of expenditure of at least 5.25% for direct national lines and 7% for digital 2-Mbit/s lines. As far as wholesale rate plans are concerned, terminations co-shared with a Telecom Italia exchange are to be introduced, along with all the extra services, including RPV-D, diversity of routing and the link of protected access. Furthermore, items of cost must be reduced by at least 12% compared to the prices of the retail rate plans. Finally, the Order involves the re-formulation of the Service Level Agreements of certain conditions relating to the supply of retail and wholesale services.

In Resolution No. 440/03/CONS of December 17, 2003, the National Regulatory Authority confirmed the new rate plans for Telecom Italia s retail and wholesale leased lines, published on October 30, 2003.

EU Telecommunications Law and Regulation

Italy is a member of the EU and, as such, is required to implement the directives issued by the EU. Although directives must be incorporated into domestic legislation to be fully effective, a directive or certain provisions of a directive may take effect automatically in a Member State on the prescribed deadline if it is sufficiently clear and specific, even if it is not formally adopted by such Member State by the prescribed deadline. If a directive is not formally implemented by the prescribed deadline, the only remedy available for an interested party is to seek damages against the Member State. Italy is also the addressee of various EU resolutions, recommendations and communications which are not legally binding, although politically important. The European Commission began opening the telecommunications market to competition with the adoption of directives in the late 1980s and early 1990s which beginning in 1990, opened to competition telecommunication services, other than fixed public voice telephony services, opening the market for value added services. Subsequent directives liberalized the market for satellite services, alternative infrastructure and mobile services and infrastructure. These liberalization measures culminated with the opening of competition in 1998 of public voice telephony and public network infrastructure. These directives were also accompanied by directives relating to open networks, setting out a body of principles for access to public telecommunications networks and services.

The 1999 Review

It was intended that the European 1998 regulatory package be reviewed by January 1, 2000. The Commission started a number of studies on the following subjects: (i) remaining barriers in the EU-wide telecommunications market; (ii) assessment of the interconnection situation in the EU; (iii) fixed-mobile convergence/integration; (iv) consumer demand; (v) quality of telecommunication services and consumer protection; (vi) need for a European regulator; and (vii) universal service obligations.

As a result of the above-mentioned studies, the Commission proposed the following five Directives:

- a common regulatory framework for electronic communications networks and services (Framework Directive);

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- the authorization of electronic communications networks and services (Authorization Directive);
- access to, and interconnection of, electronic communications networks and associated facilities (Access Directive);
- universal service and users rights relating to electronic communications networks and services (Universal Service Directive); and
- the processing of personal data and the protection of privacy in the electronic communications sector (Personal Data Directive).

The Framework, Authorization, Access and Universal service Directives were adopted in March 2002 and published in the Official Journal on April 24, 2002. Member States had to adopt these Directives into their own laws by July 24, 2003. In Italy these Directives became effective as of September 16, 2003 through the adoption of the Code.

Framework Directive. In an important change described by the Commission as rolling back regulation , the Directive redefines the concept of Significant Market Power and the threshold for imposing obligations on certain operators. The directive amends the current definition of Significant Market Power based on a 25% or more share of the relevant market.

In the Directive, the notion of SMP is based on the concept of dominant position, calculated in a manner consistent with competition law practice. Significant Market Power implies the application of rules in accordance with the conditions imposed by the other Directives.

Authorization Directive. The Authorization Directive provides for electronic communications services and networks to be provided under general authorization. Licenses will no longer be required and specific rights of use would be granted, separately from authorizations, for the assignment of radio frequencies and numbers.

A notification will require only the following elements:

- a declaration of the intention to start operation;
- contact information of the company requesting the authorization; and/or
- a short description of the service provided.

Upon notification the company can start to operate a network and provide services, provided that it has the right to use radio frequency and numbers if needed. No information should be required prior to, or as a condition for, market access. Nonetheless, Member States could require some justified information (listed in the proposal) from undertakings.

Access Directive. The Access Directive represents a significant departure from the previous Interconnection Directive 97/33/EC which sets out common obligations to be followed by Significant Market Power operators in all Member States.

Under the directive, national regulatory Authority will have flexibility to select which access and interconnection obligations to impose on operators notified as having Significant Market Power in relevant markets. A maximum list of obligations is contained in the directive. The proposed operators with rights and obligations to interconnect are essentially the same as those defined in the current ONP Interconnection Directive.

National regulatory Authority will carry out an analysis of the competitiveness of a designated list of relevant product and service markets and identify which operators (if any) have Significant Market Power on any of the particular markets. A national regulatory authority will be able to impose price controls, including obligations for cost orientation of prices and obligations concerning cost accounting systems, for the provision of specific types of interconnection and/or access services.

National regulatory Authority will also be able to impose obligations for transparency, non-discrimination, and accounting separation on Significant Market Power operators in relation to interconnection and/or network access. These obligations are carried over from the current regulatory framework.

Universal Service Directive. The Universal Service Directive replaces the existing directive on voice telephony and universal services. The Directive also contains rules on number portability, carrier selection and carrier pre-selection which are currently in the Interconnection Directive. The directive also covers the provision of leased lines and other mandatory services as well as a number of issues concerning users rights, such as contracts, tariff transparency and information and quality of service.

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In general, the existing requirements for the provision of universal service, voice telephony facilities and leased lines will remain in place, at least for the time being. The principal changes are described below.

In an important section on retail price regulation (up to now only covered in national law), it is proposed that, when an operator has Significant Market Power in the provision of access to, and use of, public telephone services, the national regulatory authority must:

- determine appropriate mechanisms for retail price control, such as price caps or specific price floors and ceilings;
- ensure that the Significant Market Power operator sets prices at normal commercial levels;
- notify to the Commission the names of organizations subject to retail price control; and
- retail price control mechanisms should not be applied where effective competition exists.

The directive also provides for the extension of the requirement for number portability to mobile operators.

Data Protection Directive

In July 2000, the Commission published a draft proposal for a Directive for data protection on the Electronic Communications sector. It aimed at replacing directive 97/66 of 1997 on the processing of personal data and the protection of privacy in the telecommunications sector by updating and adapting it to market and technological development.

On July 12, 2002, Directive 2002/58/CE was adopted on the treatment of personal information and on the safeguarding of privacy in the electronic communications sector. The new directive abrogates and replaces the above-mentioned directive 97/66.

The main changes are the extension of scope and technological neutrality. The principle of technological neutrality implies that consumers and users should get the same level of protection regardless of the technology used. Telecommunications services and networks would be replaced by electronic communications services and networks in line with the proposed common Framework Directive.

The scope of the new directive is to include networks used for radio and television broadcasting and cable TV networks, irrespective of the type of information conveyed (these were excluded from Directive 97/66/EC) but would exclude content of broadcasting transmissions.

Guidelines on Market Analysis

In March 2001, the Commission published Draft Guidelines on market analysis and the calculation of Significant Market Power. The Commission called for public comments and an exchange of views among the interested authorities and different market operators. The Guidelines set out the principles for use by national regulatory authorities in the analysis of effective competition, when determining whether an operator has significant market power. Operators having significant market power may be subject to obligations under other Directives in the regulatory package. The guidelines were adopted in July 2002.

On June 17, 2002, the Commission issued the draft of the Recommendation on the list of markets to which the new framework will be applied and a working document, for opening the public consultation on the Recommendation in accordance with Art. 15(1) of the Framework Directive. The Recommendation was adopted in February 2003.

Recommendation on relevant markets

Article 15(1) of the Framework Directive requires the Commission to adopt a Recommendation on relevant product and service markets. The Recommendation aims at identifying markets for which competition law remedies may be insufficient to effectively redress possible market failures.

The Recommendation was adopted on February 11, 2003 and identifies 18 relevant markets at retail and wholesale level. The range of different network structures and technologies deployed across the EU means that in some cases national regulatory agencies must decide the precise geographical boundaries between, or elements within, particular product and service markets identified in the Recommendation. National regulatory authorities may identify markets that differ from those of the Recommendation, provided they act in accordance with Article 7 of the Framework Directive.

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Recommendation on remedies

The recommendation is under preparation by the Commission. The purpose of this recommendation will be to indicate to the respective national regulatory authorities which remedies have to be applied in accordance with the principle of proportionality in order to achieve the objectives set out in the Framework directive. An ERG (European Regulators Group) common position was adopted in April 2004.

Competition Law

Telecom Italia is subject to Law No. 287 of October 10, 1990 (Law 287), the Italian competition law of general application, to the substantive rules of the Maccanico Law (Law 249) and to the competition rules of the EU. Law 287 forbids:

- agreements (including resolutions and concerted practices) aimed at fixing prices, limiting production or access to markets and technological developments, sharing of markets, applying different conditions for the same services to the detriment of competitors, and subjecting contracts to the acceptance of conditions that, according to their nature and common practice, are not linked to the object of the contract;
- abuses of dominant position (including practices aimed at fixing prices, limiting production or access to markets and technological developments, applying different contractual conditions for the same services to the detriment of competitors, as well as subjecting contracts to the acceptance of conditions that, according to their nature and common practice, are not linked to the object of the contract); and
- concentrations of enterprises (i.e., mergers, acquisitions of controlling interests and concentrative joint ventures) which would result in the creation or strengthening of a dominant position. All concentrations in relation to which the combined overall turnover, in Italy, of the companies involved is higher than 377 million or the turnover of the company being acquired is, in Italy, higher than 37 million, must receive a prior authorization from the Antitrust Authority. These thresholds are adjusted every year to take account of inflation. Failure to file prior notification of a concentration to the Antitrust Authority will result in a fine from 1% to 10% of the turnover of the parties involved in the concentration, or higher in the case of fines for violation of a prohibition of a concentration.

Law 287 is administered by the Antitrust Authority which, either on its initiative or following a complaint submitted by any interested party (the Interested Party), has the power to investigate and ascertain compliance with Law 287. When the Antitrust Authority finds prima facie evidence that Law 287 has been violated, the parties involved (including the Interested Party) are notified of the opening of a formal investigation. The party under investigation (the Investigated Party) and the Interested Parties shall then have the right to be heard and to file written arguments with the Antitrust Authority. Pending the investigation, the Antitrust Authority may also require the parties involved and third parties to disclose information or to submit documents that it considers useful for the investigation. In addition, the Antitrust Authority may appoint experts and carry out direct inspections at the Investigated Party s premises in order to examine and seize relevant documents.

If at the conclusion of the investigation the Antitrust Authority determines that Law 287 has been violated, it orders the Investigated Party to cure the relevant violation and, in the case of serious violations, imposes fines up to 10% of the turnover. Any failure to comply is sanctioned with an additional fine up to 10% of the turnover of the Investigated Party.

With respect to competition matters, the decisions of the Antitrust Authority are considered administrative acts and may be appealed before the TAR of Lazio, based in Rome, for violation of law, abuse of power and lack of jurisdiction. The TAR may either reject the appeal or declare the Antitrust Authority s decision null and void. The TAR, upon request of the complainant, may also suspend the enforcement of the decision of the Antitrust Authority. The TAR s judgments may be further appealed before the State Council, whose decision is final.

The Antitrust Authority has no powers other than those indicated above. It may not issue provisional injunctions or impose liquidated damages for abuses of dominant positions. For these remedies, Law 287 confers special jurisdiction on the Court of Appeal that has jurisdiction over the relevant case.

In addition to Law 287, the Maccanico Law confers upon the National Regulatory Authority the power to enforce provisions aimed at ensuring pluralism in the communications sectors, including radio and television broadcasting activities.

Moreover, the competition rules of the EU (EU Competition Law) also have a direct effect in Italy. The main principles of EU Competition Law are contained in Articles 81 and 82 of the Treaty of Rome. Article 81 prohibits agreements or concerted practices between undertakings that may affect trade between Member States and has the object or effect of restricting competition within the EU. Article 82 prohibits any abuse of a dominant position within a substantial part of the EU that may affect trade between Member States. These rules are primarily enforced by the European Commission, which cooperates with the national competition authorities, and through the national courts. The Antitrust Authority has the power to apply Article 81(1) and Article 82, following its own procedures and imposing, if necessary, the fines provided for under Law 287. In September 1991, general guidelines were published by the European Commission on the application of EU Competition Law in the telecommunications sector. In August 1998, the European Commission published a notice updating the 1991 guidelines. These guidelines outline the EU s approach to common competition issues.

On December 11, 1996, the Commission adopted a Communication on the application of the competition rules to access agreements in the telecommunications sector. The purpose of this notice is:

- to set out access principles stemming from EU law in order to create more market certainty;
- to define and clarify the relationship between competition law and sector specific regulation; and
- to explain how competition rules will be applied in a consistent way across the converging sectors. On October 3, 1997, the EU adopted a further communication on the definition of the relevant market for the purpose of EU competition law. The aim of this notice is to provide guidance as to how the Commission applies the concept of relevant product and geographic market in its ongoing enforcement of EU competition law.

In April 1999, the Commission adopted a White Paper on modernization of the rules implementing Articles 81 and 82 of the EC Treaty, which examined various options for reforming the system and proposed the adoption of fundamentally different enforcement system called a direct applicable exception system. Such system is based on the direct applicability of the exception rule of Article 81.3, implying that the Commission and national competition authorities and courts would apply Art. 81.3 in all proceedings in which they are called upon to apply Art. 81.1, which is already directly applicable.

On December 16, 2002, the EU Council approved the Regulation No. 01/2003 (OJ L 1 01/04/2003) On the implementation of the rules on competition laid down in articles 81 and 82 of the Treaty . The Council Regulation provides, inter alia, for the abolition of the Commission s exclusivity in the application of art. 81.3; a system of legal exception and evaluation ex post of the agreements; an effective decentralization of the enforcement of EU competition rules; and the strengthening of Commission s investigation powers. This regulation has replaced Regulation 17/62. The new Regulation simplifies the way in which the EC Treaty s antitrust rules are enforced in the European Union. Most importantly, the new Regulation abolishes the practice of notifying business agreements to the Commission, therefore reducing bureaucracy and legal costs for companies. The simplified system of the new Regulation is designed to facilitate the effective enforcement of the antitrust rules in the EU comprising more than 15 Member States. The new regulation allows national courts and competition authorities to directly apply Article 81(3) without prior involvement of the Commission.

Under the Regulation, where the trend of trade between Member States, the rigidity of prices or other circumstances suggest that competition may be restricted or distorted within the common market, the Commission may conduct an inquiry into a particular sector or into a particular type of agreements across various sectors. The Commission may request the undertakings or associations concerned to supply all the information necessary for giving effect to Arts. 81 and 82 of the Treaty and may carry out any inspections necessary for that purpose.

On December 11, 2001, the European Commission issued a Green paper on the Review of Council Regulation (EEC) No 4064/89, concerning mergers with community dimensions. The Commission seeks to launch a wide ranging debate on the functioning of the EU merger control regime based on the experience gained during the last 10 years. On December 11, 2002, the Commission published a proposal for a Council Regulation on the control of concentrations between undertakings. The proposal tackles jurisdictional issues (such as the notion of concentration and the community dimension), substantive issues (such as the concept of dominance) and Procedural issues (such as the timing of notifications, the suspension of proceedings, etc.).

During 2003, the Commission published the Best Practices on the conduct of EC merger control proceedings , in order to provide guidance for interested parties on the day-to-day conduct of EC merger control proceedings and foster and build upon a spirit of cooperation and better understanding between DG Competition and the legal and business community. The Commission finds it is the appropriate time to review the Regulation, to ensure effective, efficient, fair and transparent control of concentrations at the most appropriate level.

On February 5, 2004, the Commission also published Guidelines on horizontal mergers which address, inter alia, the issue of oligopolies and collective dominance.

GLOSSARY OF SELECTED TELECOMMUNICATIONS TERMS

The following explanations are not intended as technical definitions, but to assist the general reader to understand certain terms as used in this Annual Report.

Access charge: Amount paid per minute charged by the national operators for the use of their network by operators of other networks. Also, known as an interconnection charge .

ADSL (Asymmetric Digital Subscriber Line): A modem technology, converts existing twisted-pair telephone lines into access paths for multimedia and high-speed data communications. ADSL can transmit up to 6 Mbps to a subscriber, and as much as 832 Kbps or more in both directions. Such rates expand existing access capacity by a factor of 50 or more without new cabling.

Analog: A transmission or switching which is not digital, e.g., the representation of voice, video or other modulated electrical audio signals which are not in digital form.

Analog network: A network using analog technology with circuit switching, capable of connecting one user with all the others, but with limited transmission capacity.

ASTN (Automatically Switched Transport Network): Emerging architectural standard for switched intelligent optical network in order to manage the automatic signalling and routing of connection, auto-discovery and meshed optical network protection.

ATM (Asynchronous Transfer Mode): A broadband switching technology that permits the use of one network for different kinds of information (e.g., voice, data and video).

Backbone: A primary shared communication path that serves multiple networks and may facilitate communications between different protocols.

Broadband services: Services characterized by a transmission speed of 2 Mbit/s or more. According to international standards, these services are divided into two categories: (i) Interactive services, including videotelephone/videoconferencing (both point-to-point and multipoint); videomonitoring; interconnection of local networks; file transfer; CAD; highspeed fax; e-mail for moving images or mixed documents; broadband videotex; Video on demand; retrieval of sound programs or fixed and moving images; and (ii) Broadcast services, such as sound programs, television programs (including high-definition TV and pay TV) and selective document acquisition.

Broadcast: Simultaneous transmission of information to all nodes and terminal equipment of a network.

BSS (Business Support System): The system used by network operators to manage business operations such as billing, sales management, customer-service management and customer databases. A type of Operations Support System OSS.

Business Packet: The Italian packet-switching data network.

Carrier: Traditionally, the carrier is the company that makes the physical lines available.

CATV (Cable television): Cable or fiber-based distribution of TV programs.

Cellular: A technique used in mobile radio technology to use the same spectrum several times in one network. Low power radio transmitters are used to cover a cell (i.e., a limited area) so that the frequencies in use can be reused without interference for other parts of the network.

Channel: The portion of a communications system that connects a source to one or more destinations. Also called circuit, line, link or path.

Closed User Group: A group of telecommunications users that share a longstanding economic interest. This definition has arisen in a regulatory context; it permits the partial liberalization of some telecommunications services.

Coaxial cable: A type of electrical cable in which a central conductor covered by an insulator is then surrounded with a cylindrical conducting sheath whose axis coincides with that of the central conductor, hence the term coaxial .

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Corporate Network: A network, which could be a virtual private network, provided by a corporation for its own use and possibly for that of other corporations. The network s features are tailor-made to address the specific need of the client. It is separate from the network provided by the national telecommunications carrier, but it may be connected to the latter for the use of selected facilities.

CPS (Carrier Pre-selection): It permits a customer to pre-select another operator as an alternative to Telecom Italia without dialing an identifying code.

Data Network Access Point: Unit of measurement used in data network business.

DCS 1800 (Digital Communication System): A derivative of the GSM cellular mobile telephone standard. 1800 refers to the frequency used of 1800 MHz. DCS 1800 is the European PCN standard.

Digital: A mode of representing a physical variable such as speech using digits 0 and 1 only which vary in relation to the variable being represented. The digits are transmitted in binary form as a series of pulses. Digital networks are rapidly replacing the older analog ones. They allow for higher capacity and higher flexibility through the use of computer-related technology for the transmission and manipulation of telephone calls. Digital systems offer lower noise interference and can incorporate encryption as a protection for external interference.

Digital Terrestrial TV: Digital Terrestrial Television Broadcasting is a new type of broadcasting technology that provides a more effective way of transmitting television services using a digital system rather than the existing analogue system.

District traffic: Long distance telephone calls within the same area code.

DSL Network (Digital Subscriber Line Network): A network built on existing telephone lines with DSL technology devices which use sophisticated modulation schemes to pack data onto copper wires for connections from a telephone switching station to a home or office.

EDGE (Enhanced Data for GSM Evolution): A prototype in the evolution of data communications within existing GSM standards.

Exchange: See Switch.

Frame Relay: A data transmission service using fast protocols based on direct use of transmission lines.

Gateway: A connection between the LANs and WANs of one or more suppliers. Can also mean the access nodes to international networks of various kinds.

GPRS (General Packet Radio Service): This is the data service for GSM and is the European standard digital cellular service.

GPS (Global Positioning System): A constellation of satellites, orbiting the Earth two times a day, that is able to pinpoint precisely where a certain object is on Earth.

GRX (GPRS Roaming eXchange for Mobile Operator): The GRX service allows Mobile Operators to interconnect GPRS networks around the world and offer global GPRS roaming coverage.

GSM (Global System for Mobile Communications): A standard for mobile cellular telephony used in Europe, Asia, South Africa and Australia, based on digital transmission and cellular network architecture with roaming.

GSM TIM Card: A prepaid, rechargeable card which permits the TIM mobile customer to make outgoing calls up to the limit of the card and receive an unlimited number of calls.

HDSL (High-bit-rate Digital Subscriber Line): Technology which allows the provisioning of local loop circuits at higher speeds and lowers cost than through conventional means.

IN (Intelligent Network): Network architecture that centralizes processing of calls and billing information for calls.

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Interactive: The user can change some aspect of the program received.

Internet: The world s best-known data network. Initially used by the U.S. Department of Defense, the Internet now provides an interface for networks based on different technologies (LANs, WANs, data networks, etc.), but which use the TCP/IP protocol platform.

IP (Internet Protocol): A standard describing the software that keeps track of the Internet s addresses for different nodes, routes outgoing messages and recognizes incoming messages.

IP/MPLS (Internet Protocol/Multi Protocol Labeling Switching): A packet switching protocol to optimize network behaviours of mapping Layer3 (IP) end-to-end data flow to Layer2 traffic between adjacent network nodes.

ISDN (Integrated Services Digital Network): A system in which several services (e.g., speech and data) may be simultaneously transmitted end to end in digital form.

ISPs (Internet Service Provider): Vendor who provides access to the internet and world wide web.

ITU (International Telecommunication Union): The worldwide policy, spectrum regulation and standardization body in telecommunications operating under the auspices of the United Nations.

LAN (Local Area Network): A private network that covers a local geographic area and provides public telecommunications services as well as interconnection between personal computers.

MAS (Metro Access System): A network element based on CWDM (Course Wavelength Division Multiplexing) technology.

MEMS (Micro-Electro-Mechanical Systems): MEMS are miniaturized devices ranging in size from a few micrometers to a few millimeters, which execute one or more monitoring, processing or actuation functions by deploying a combination of electronic, mechanical, optical, chemical or biological components integrated on a usually silicon hybrid circuit.

MMS (Mobile Multimedia Services): Represent an evolution of the SMS and the EMS service using various mono-medial elements (text, design, photos, video-clips and audio), which are synchronized and combined allowing them to be packed together and sent to GSM-GPRS platforms.

Modem: Modulator/Demodulator. A device that modulates digital data to allow their transmission on analog channels, generally consisting of telephone lines.

MPLS (Multi Protocol Label Switching): A packet switching protocol to optimize network behaviors of mapping Layer3 end-to-end data flow to Layer2 traffic between adjacent network nodes.

MS SPRING: A form of traffic protection mechanism for the equipment.

MSP: The name of a general purpose programmable switch made by Redcom Laboratories.

Multimedia: A service involving two or more communications media (e.g., voice, video, text, etc.) and hybrid products created through their interaction.

Network: An interconnected collection of elements. In a telephone network, these consist of switches connected to each other and to customer equipment. The transmission equipment may be based on fibre optic or metallic cable or point to point radio connections.

NNI (Network Node Interface): The interface between two public network pieces of equipment.

NNI Agreements (Network Node Interface Agreements): Contractual agreements for the interface between two public network pieces of equipment.

Nodes: Topological network junction, commonly a switching center or station.

OLOs (Other Licensed Operators): Companies other than the incumbent operator which operate telecoms systems in a national market.

ONP (Open Network Provision): Principles and conditions laid down by the EU for access to and usage of public telecommunications networks and services. A network architecture that permits telecommunications services to be offered on facilities of public operators and for equipment to be connected to such networks.

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Optical fiber: A transmission medium which permits extremely high capacities. It consists of a thin strand of glass that provides a pathway along which waves of light can travel for telecommunications purposes.

OSS (Operations Support System): Methods and procedures (mechanized or not) which directly support the daily operation of the telecommunications infrastructure.

Outsourcing: Hiring outsiders to perform various telecommunications services, which may include planning, construction, hosting of a network or specific equipment belonging to a company, and, ultimately, the management of entire telecommunications systems. Value-added applications may also be provided in various sectors.

PABX (Private Automatic Branch Exchange): Telephone switchboard for private use, but linked to the national telephone network.

Packet-Switched Services: Data services based on parceling or breaking the data stream into packets and switching the individual packets. Information transmitted (whether voice or data) is segmented into cells of a standardized length, which are then transmitted independently of one another, allowing maximization of available capacity and usage of a single transmission path for multiple communications. The cells are then reassembled upon reaching their destination.

Pay-Per-View: A system by which the viewer pays to see a single program (such as a sporting event, film or concert) at the moment at which it is transmitted or broadcast.

Pay TV: Paid-for TV channels. To receive Pay TV or Pay-Per-View programs, a decoder must be connected to the television set, connected to a conditional access system.

PCN (Personal Communications Network): PCN is a cellular telephony network designed to have the high capacity required to support a mass market service.

PCS: Personal communications services.

Penetration: The measurement of the take-up of services. As of any date, the penetration is calculated by dividing the number of subscribers by the population to which the service is available and multiplying the quotient by 100 on such a date.

Platform: The total input, including hardware, software, operating equipment and procedures, for producing (production platform) or managing (management platform) a particular service (service platform).

POTS (Plain Old Telephone Service): The basic telephony service supplying standard, single-line telephones, fixed-line services and access to public voice telephony network.

PSTN (Public Switched Telephone Network): The public telephone network delivering the basic telephone service and, in certain circumstances, more advanced services.

Roaming: A function that enables wireless subscribers to use the service on networks of operators other than the one with which they signed their initial contract.

RoF (Radio over Fiber): A technology to feed antennas with digital/analogue signals over optical fiber.

Satellite services: Satellites are used, among other things, for links with countries that cannot be reached by cable or to provide an alternative to cable and to form closed user networks.

SDH Standard (Synchronous Digital Hierarchy): The European standard for high-speed digital transmission.

SDSL (Symmetrical Digital Subscriber Line): also known as HDSL.

Service Provider: The party that provides end users and content providers with a range of services, including a proprietary, exclusive or third-party service center.

SGT (Transit exchange interconnection level for telephone traffic): Transit Exchange for telephone traffic carriage, routing and transmission.

SGU (Local exchange interconnection level for telephone traffic): Local Exchange for telephone traffic carriage, routing and transmission.

SME: Refers to the small- and medium-size enterprise market which consists of businesses having between 3 and 50 employees.

SNCP: A form of traffic protection mechanism for the equipment.

SOHO: Refers to the small office/home office market which consists of businesses that use telephone lines to connect to the Internet, as opposed to dedicated lines, and is made up of small businesses, generally with one or two employees, and businesses conducted out of the home.

SPP (Service Provider Portability): A faculty that allows an end user to retain the same directory number after changing from one service provider to another.

Switch: These are used to set up and route telephone calls either to the number called or to the next switch among the path. They may also record information for billing and control purposes.

Switched Transit Traffic: Consists of calls placed between two other countries that are routed through the Italian fixed network.

Synchronous: Type of data transmission in which there is permanent synchronization between the transmitter and the receiver.

TACS (Total Access Communication System): An analog cellular network using the 900 MHz band based on a European standard also used in the UK, Ireland, Austria and Spain. Features include handover and available add-on services include answering, call notification, call transfer, differentiation of business and private calls, authorization code for outgoing international calls and itemized billing.

UMTS (Universal Mobile Telecommunication System): Third generation mobile communication system.

Universal service: The obligation to supply basic service to all users throughout the national territory at reasonable prices.

VAS (Value Added Services): Value Added Services provide a higher level of functionality than the basic transmission services offered by a telecommunications network for the transfer of information among its terminals, which include wired or wireless switched-circuit analog voice communications; direct unrestricted digital point-to-point service at 9,600 bit/s; packet switching (virtual call); direct broadband analog transmission of TV signals, and supplementary services, such as closed user groups; call waiting; collect calls; call forwarding, and identification of number called. Value Added Services performed by the network, the terminals or the specialized centers include message handling services (MHS) (which can be used, among other things, for commercial documents in predetermined formats); electronic directories listing users, network addressees and terminals; e-mail; fax; teletex; videotex and videotelephone.

Value Added Services could include also value added voice telephony services such as Freephone or Premium Rate Services.

VAN (Value-added Network): A type of public network that leases basic transmission facilities from a common carrier, adds features that enhance the service and provides the improved communications capability to end users. Automatic alternate routing network management and error correction are examples of the value added.

Videotex: A service pursuant to an ITU standard, permitting remote access to database by telephone.

VPN (Virtual Private Network): A network designed for a business or government agency, using the infrastructures of a carrier and providing customized services, which operates in such a manner as to appear dedicated to the user thereof.

WAN (Wide Area Network): A private network that covers a wide geographic area using public telecommunications services.

WAP (Wireless Application Protocol): A Technology which allows access to Internet using mobile radio sets, even without the use of a computer.

WI FI: Is a service for wireless internet connection and high speed access.

WLL (Wireless Local Loop): The means of configuring a local loop without the use of wiring.

XSDL (x(generic) Digital Subscriber Line): A generic term for DSL equipment, services and technologies which provide extremely high bandwidth over the twisted-pair lines that run from a phone company s central office to a home or office.

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DESCRIPTION OF PROPERTY

General

As of December 31, 2003, the Telecom Italia Group owned approximately 6,800 buildings located throughout Italy. Specialized buildings for telecommunications services account for the majority of properties both in number and book value. They house mainly exchange equipment and transmission equipment, and are used as part of the Telecom Italia Group s continuing telecommunications operations. General purpose properties consist chiefly of offices, depots and computer centers.

The principal categories of the Telecom Italia Group s equipment are exchanges and transmission equipment, cable networks, base stations for cellular networks and equipment for radio communications, most of which are located throughout Italy. The Telecom Italia Group also has numerous computer installations which are primarily located at the headquarters of the Telecom Italia Group s significant subsidiaries.

At December 31, 2003, telecommunications installations, including local and domestic long distance networks and radio transmission equipment, represented approximately 78% of the fixed assets of the Telecom Italia Group, land and buildings represented 10%, plant under construction, advances to suppliers and stock for fixed assets represented 9%, and furniture, office equipment and other equipment, technical installations and machinery comprised the remaining 3%.

As of December 31, 2003, the total amount of liens, mortgages and pledges on real property owned by the Telecom Italia Group was 149 million. Such liens, mortgages and pledges do not represent major encumbrances on fixed assets and on the material plans to expand or construct new facilities.

An important element of Telecom Italia s restructuring plan was to realize value on its extensive real estate portfolio.

In November 2000, Telecom Italia established a partnership with Beni Stabili, a leading Italian real estate operator, and Lehman Brothers to manage a significant portion of Telecom Italia s real estate portfolio.

Telecom Italia contributed a going concern including an important portion of its real estate portfolio to IM.SER and subsequently sold 45% of this company to Beni Stabili and 15% to Lehman Brothers.

The real estate portfolio originally held by IM.SER consisted of 581 properties, totaling 3.7 million square meters and was composed of two parts, the Real Estate Investment Portfolio and the Real Estate Trading Portfolio :

- Real Estate Investment Portfolio , consisting of 386 properties totaling approximately 2.4 million square meters, located throughout Italy. All the properties, including buildings that contain telecommunications equipment, were leased to Old Telecom Italia at the end of 2000 under long-term lease contracts (21 plus 6 years) at market rates; and

- Real Estate Trading Portfolio , consisting of 195 properties totaling approximately 1.3 million square meters, located throughout Italy. Of these properties, the majority have been leased at market rates to Old Telecom Italia under contracts allowing for early termination in favor of Telecom Italia.

In May 2001, IM.SER contributed its Real Estate Trading Portfolio to Telemaco Immobiliare, a newly formed company. Following such contribution, IM.SER sold the shares of Telemaco Immobiliare to its shareholders. The shareholders of Telemaco Immobiliare at that time were Beni Stabili with a 45% stake, Telecom Italia with a 40% stake and Lehman Brothers with a 15% stake.

On May 16, 2001, Beni Stabili exercised an option to buy the Lehman Brothers stake in IM.SER, resulting in Beni Stabili holding a 60% stake in IM.SER and Old Telecom Italia a 40% stake.

During 2002 some additional real estate related transactions were completed:

Tiglio Project

Pursuant to a framework agreement signed in May 2002, between the Pirelli, Olivetti-Telecom Italia Groups and The Morgan Stanley Real Estate Funds (through MSMC Italy Holding B.V. and POPOY Holding B.V.) certain real estate properties as well as the entities that provide real estate services to the same companies or to their subsidiaries were transferred to two new vehicle companies set up for this purpose (Tiglio I S.r.l. and Tiglio II S.r.l.).

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Among the preliminary transactions for the concentration of the real estate assets in Tiglio I and Tiglio II, on October 24, 2002, the non-proportional partial spin-off of IM.SER (60% Beni Stabili and 40% Telecom Italia) was effected by which the relative real estate assets were contributed to the company IM.SER 60 (98% Beni Stabili group and 2% Telecom Italia) and to the company EMSA Immobiliare (100% controlled by Telecom Italia) in proportion to the stakes held in IM.SER, respectively, by Beni Stabili and Telecom Italia.

Following this transaction, which came after the completion of the securitization of IM.SER 60 s debt, and also to the effect of certain fixed asset acquisitions by companies in the Seat Pagine Gialle group, EMSA Immobiliare had a portfolio of 169 real estate properties.

On October 29, 2002, having satisfied the necessary conditions, a series of acts were finalized whereby the first stage of the Tiglio Project was concluded including the following:

- the subscription, simultaneously with all the other participants, to a capital increase by Tiglio I for cash, with the consequent stake in the company equaling 36.85% (in addition, at Old Telecom Italia Group level, to the 2.1% subscribed to by Seat Pagine Gialle), in proportion to the value of the assets transferred by Old Telecom Italia (and by Seat Pagine Gialle) to Tiglio I to the total assets that were taken over by the latter company;
- the subscription to a capital increase by Tiglio II paid for in kind by the contribution of Old Telecom Italia s Asset Management business segment with the consequent stake in the company equaling 49.47%;
- the sale of the investment in EMSA Immobiliare to OMS2 (100% controlled by Tiglio I);
- the sale directly and through the subsidiary Saiat of the investment in Telimm S.r.l. to the company MSMC Immobiliare Holding (entirely controlled by Tiglio I).

With reference to the part of the Tiglio Project regarding the optimization of the service activities, in November 2002, Telecom Italia sold its Property Management , Project Management and Agency businesses to the Pirelli & C. Real Estate group.

The above mentioned transactions gave rise to a total gross capital gain for the Telecom Italia Group of 234 million.

Finally, as agreed between the parties, December 24, 2002, marked the completion of the merger by absorption, in Tiglio I and Tiglio II, of the real estate investment holdings owned by them falling under Tiglio Project and already 100% controlled, directly or indirectly so that the corporate structure of the two subjects could be optimized, in view of the successive actions to leverage the assets on the market.

In particular the second phase of the Tiglio Project consists of the change of asset ownership, through awarding it to real estate funds, or through realization of transfer operations. The real property was divided into several categories (office, industrial portfolio, trading portfolio, etc.), in order to optimize Tiglio I and Tiglio II shareholders profit, also in the light of real estate funds market features.

In November 2003, Pirelli & C. Real Estate Sgr S.p.A. and Tiglio I drew up the contribution act to TECLA FONDO UFFICI Closed Investment Fund , in which Tiglio I contributed with 65 buildings, for a total market value of about 926 million, plus 25 million in cash.

On March 1, 2004, TECLA FONDO UFFICI was successfully placed on the market.

Sale of IMMSI

On November 22, 2002, Old Telecom Italia sold its stake in IMMSI to the company Omniapartecipazioni. The sale price was 68 million, with a gross gain of 1 million for the Telecom Italia Group.

Sale of Telemaco Immobiliare

On August 1, 2002, Telecom Italia sold its 40% interest in Telemaco Immobiliare to Mirtus, an indirect subsidiary of the American real estate fund Whitehall promoted by the Goldman Sachs group.

On October 31, 2002, Telemaco Immobiliare exercised a put option towards Telegono (a company held 40% by Telecom Italia, 45% by the Beni Stabili group and 15% by Lehman Brothers) on 28 real estate properties

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it owned based on agreements formalized in the Sale and Purchase Agreement of July 31, 2002 between Mirtus and the three sellers of the company. For purposes of the acquisition of such assets, Telegono signed a loan agreement that will be extinguished partly by the consideration from the sale in progress of such properties.

On December 20, 2002, the final sale price was fixed relating to Telecom Italia s investment in Telemaco Immobiliare to the company Mirtus. The net proceeds were 192 million for the Old Telecom Italia Group with a gross gain of 110 million.

Ortensia Project

On December 24, 2002, Telecom Italia and the other shareholders of Tiglio I (MSMC Italy Holding BV, Olivetti, Seat Pagine Gialle and Pirelli) and Tiglio II (POPOY Holding B.V.) formalized a binding agreement with the company Marzotto which became effective on March 4, 2003, to set up a common vehicle company (Ortensia s.r.l. , following called Aree Urbane s.r.l.) for the land owned by Tiglio I and Tiglio II together with the portfolio of areas owned, directly and indirectly, by Marzotto. The agreement calls for the deal to be finalized in 2003 through the spin-off of the land owned by Tiglio I and Tiglio II and other assets and liabilities related thereto to a company in which Marzotto, at the end of December 2002, on the basis of formalized agreements, had contributed a business segment inclusive of the land earmarked for the initiative.

On July 21, 2003, the definitive spin-off agreements of Tiglio I and Tiglio II in Aree Urbane s.r.l. were formalized between the shareholders: after this operation, Telecom Italia owns 31.65% of the share capital of Aree Urbane s.r.l. and Telecom Italia Media owns 0.97 %.

Dedalo Project

In January 2003, the procedures were completed for the early purchase of 12 property units (representing about 300,000 square meters) from Teleleasing S.p.A. that are used by Telecom Italia S.p.A. and other Telecom Italia Group companies under lease contracts. The deal involved a total financial payment of approximately 369 million for the entire Old Telecom Italia Group.

Following a binding offer by the Beny Steinmetz Group through its subsidiary FMP, on June 20, 2003 Telecom Italia formalized an agreement with Lastra Holding B.V. (FMP Group) for the transfer of most of the early purchased property units, with a sale price of 355 million; Telecom Italia agreed to sign lease agreements on the same units to guarantee their utilization.

On June 30, 2003, all property units which were the object of the binding offer were transferred into a vehicle company, FMP Italy, former Ireos S.p.A. 100% owned by Telecom Italia. On July 21, 2003, the entire FMP Italy stake was transferred from Telecom Italia to Lastra Holding B.V. for 45,000. On the same date, Telecom Italia, TIM and Atesia received the purchase price for the property units from FMP Italy.

Integration of the Facility Management Activities Owned by Olivetti and by Pirelli & C. Real Estate

In accordance with the agreements regarding the Tiglio Project, the Facility Management activities owned by Olivetti Multiservices and by Pirelli & C. RE Facility Management were integrated in the first half of 2003. The deal involved the transfer of 809,946 Pirelli & C. Real Estate treasury shares (just under 2% of share capital) to Olivetti which contributed the above activities concentrated in a specific company known as OMS Facility.

The transaction also calls for a possible differential to be determined on December 31, 2005 based upon the price performance of Pirelli & C. Real Estate shares.

Fintecna Project

In the beginning of December 2003, Telecom Italia formalized a lease agreement on some property units of Fintecna S.p.A.: in this agreement Telecom Italia also can exercise an option to buy all property units during the first half of 2004, for a total amount of 72 million, whereas Fintecna S.p.A can exercise an option to sell to Telecom Italia the same units during the second half of 2004 for the same amount.

On December 22, 2003, Fintecna S.p.A. accepted the agreement. On April 1, 2004, Telecom Italia exercised its right to buy all the property units. The parties are currently carrying out the activities which will lead to the acquisition of such property units by around June 30, 2004.

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Item 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read in conjunction with the Consolidated Financial Statements included elsewhere in this Annual Report. Such financial statements have been prepared in accordance with Italian GAAP, which differ in certain material respects from U.S. GAAP. For a discussion of the principal differences between Italian GAAP and U.S. GAAP as they relate to Telecom Italia, see Note 27 of Notes to the Consolidated Financial Statements included elsewhere herein.

General Factors Affecting the Telecom Italia Group s Business

The European and the Italian market for telecommunications services.

In 2003, the Western European telecommunications market grew by 4%; in 2004 a growth of approximately 4.3% is expected, despite an expected decrease in revenues in the fixed voice telecommunication sector (source: 2004 Eito). Eito, or European Information Technology Observatory, is a non profit organization sponsored by telecommunications companies (including Telecom Italia) and supported by the EU and the OECD which provides reports on the information and communications technology industry in Europe.

In 2003, the Italian telecommunications services market grew by 5.0% (source: 2004 Eito). 34% of total market revenues was generated by fixed line telephone services, 52% by wireless telephone services and 14% by data and internet/on line services (source: 2004 Eito). This contrasts with 38.3%, 49.2% and 12.5%, respectively, in 2002.

As in previous years, the growth in demand for telecommunications services continues to be driven by mobile telephone services and by the development of Internet and data services. With over 54 million subscriber lines at the end of 2003, Italy is one of the European countries with the highest penetration and number of subscribers (only Germany with 64 million subscriber lines has a higher number of mobile users) (source: 2004 Eito). Italy is among the first European countries where commercial offers are presently available for third generation or 3G services. The new entrant (H3G) launched UMTS services in March 2003. TIM s strategy consists of integrating GPRS, EDGE and UMTS networks so that any of the services can be utilized regardless of the network being used at any particular time.

The transition towards the third generation is progressive. By making the most of the potential offered by 2.5G technology TIM was able to introduce in 2003 services similar to those available under UMTS such as mobile TV. The EDGE launch will bring an important competitive advantage for TIM in that it will be able to offer throughout Italy services with a network speed similar to that of UMTS (200 kbit/s for EDGE vs 384 kbit/s for UMTS). UMTS is the natural evolution of EDGE and will be launched in June 2004 for corporates and at Christmas 2004 for the mass market when handsets will be available in volumes and the technology will be more reliable.

In 2003, approximately 25 million people in Italy used the internet (source: 2004 Eito). Internet usage growth has been sustained by increased penetration of broadband services, led by the commercial success of ADSL, with over 2,000,000 installed subscriber lines at the end of the year.

Over the next two years, the Italian telecommunications market is expected to grow in line with the Western European average, with an average yearly growth rate of 4.4% (source: 2004 Eito). The performance of broadband and value added services is expected to continue to be strong. Overall market evolution in Wireline will be restricted by a slight decrease in voice traffic value driven by volume declines due primarily to substitution of mobile for fixed and price erosion which will only partially be offset by increase in access fees (source: 2004 Eito). Growth in mobile telecommunications will be driven by the uptake for new value added services, which are expected to grow at a rate of 30% over the next three years.

Competition

The Telecom Italia Group faces domestic competition in all of its businesses. See Item 4. Information on the Telecom Italia Group Business Updated Business Plan and Strategy and Item 4. Information on the Telecom Italia Group Business Units Competition . Management expects further consolidation among suppliers of telecommunication services, especially at the national level.

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On the technological side, innovation will be aimed at offering broadband services with faster connections in the fixed line market and in the development of seamless solutions for the wireless market. The incumbent operators will focus their strategic plans on the introduction of new broadband value added services, on the defense of their domestic core businesses, and on the strengthening of their financial position through debt control.

Competition remains a significant factor in how our businesses develop. Competitive pressure in the Italian market continued during 2003 as reflected in:

- further pressure on tariffs;
- 3G mobile operator H3G launched its commercial offer in March 2003;
- further development of broadband service offers based on fiber optic and ADSL; and
- gradual development of local loop unbundling and shared access with approximately 500,000 lines handed over to OLOs.

Regulatory Environment

The regulatory environment in which the Telecom Italia Group operates has been significantly altered due to changes in laws and regulations at both the Italian and EU levels and the establishment of the National Regulatory Authority in 1998, which since that time, has been principally responsible for implementing telecommunications regulations. The recent adoption of the Code for electronic communications (effective since September 2003) implementing EU directives is expected to have a significant impact on the regulatory regime in Italy and the rest of Europe.

The implementation in 2003 of the EU directives, is meant to increase the use of competition law and decrease the sector specific regulation in the electronic communications sector. See Item 4. Information on the Telecom Italia Group Business Units Competition and Item 4. Information on the Telecom Italia Group Business Regulation . As the National Regulatory Authority has not yet conducted the market analysis in the identified markets to determine significant market power it is not yet possible to determine the overall impact on our business of the new regulatory regime.

Tariff Rebalancing

We commenced rebalancing our tariffs in 1991 and made various adjustments until 1997. Since December 1998, the National Regulatory Authority has been responsible for tariff regulation. On July 28, 1999, the National Regulatory Authority introduced a price cap mechanism designed to promote productivity and efficiency for us, as the incumbent operator in markets with a low level of competition. The price cap was applied until December 31, 2002 to a whole basket of public voice telephone services composed of activation fees, basic subscriber charges, local and long distance calls and international tariffs.

On July 23, 2003, the National Regulatory Authority introduced a new price cap mechanism, also referred to as a safeguard cap , which is intended to control the maximum prices we may charge for voice services for the four year period 2003-2006. Such price caps cover:

- basic subscriber charges and other access charges RPI (Retail Price Index) + 0%, as well as a sub-price cap for residential subscription charges of RPI RPI;
- local and out-of-district calls with a cap equal to RPI-RPI; and
- fixed to mobile traffic with a cap equal to RPI-6%.

The basket of public voice telephone services includes one-off fees, monthly fees, domestic and fixed to mobile standard tariffs.

Consistent with the new price-cap mechanism, Telecom Italia continued to simplify its pricing structure during the course of 2003. The general effect of the new price cap formulas for 2003 provided for an increase of 2.3% (an increase of 100 million per year) in Telecom Italia s access service charges (i.e. monthly subscription fees) and an overall stability in Telecom Italia s domestic traffic charges (due to an increase in local traffic expenditure of approximately 37 million offset by a similar reduction in long distance traffic). The changes in tariffs implemented in year 2003 increased business monthly subscription fees by 6.5%.

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Out of the framework of the price cap mechanism, in compliance with the 47/03/CONS regulation (which has defined the new termination charge for the notified mobile operators and the value of retention for Telecom Italia), on June 1, 2003, new and lower prices of fixed-to-mobile calls became effective with an overall downgrading adjustment effect (on an annual basis) as follows:

- total customer expenditure fell by approximately 275 million (-11.7%), of which:
  - decline in termination charge of approximately 193 million (-10.9%)
  - decline in retention of approximately 82 million (-14.3%).

In particular:

- the termination charge represents the cost that Telecom Italia incurs for terminating the traffic generated by its wireline customers on the networks of mobile operators; the rate per minute is fixed by the mobile operators; and
- retention represents the difference between the amount paid by the customer and the amount due to the mobile operators for termination: the rate per minute for retention by Telecom Italia is fixed by the National Regulatory Authority (Order No. 47/03 CONS).

Greater pricing flexibility has been important to Telecom Italia s ability to remain competitive, particularly with respect to international telecommunications services for which there has been the greatest competition, and it remains an essential element of Telecom Italia s strategy to be able to price services selectively in order to respond to competition by lowering prices on selected services.

See Item 4. Information on the Telecom Italia Group Business The Organizational Structure , Item 4. Information on the Telecom Italia Group Business Units Wireline Traffic and Tariffs , Item 4. Information on the Telecom Italia Group International Traffic and Item 4. Information on the Telecom Italia Group Regulation Tariff and Pricing Policy .

Specific Factors which Impacted Results of Operations Over the 2001-2003 Period

Divestitures and Cost Reduction Plan

Following the acquisition of the controlling interest in Old Telecom Italia by Olivetti in 1999, Olivetti embarked on a series of initiatives designed to reduce overall corporate costs and to reduce acquisition related indebtedness, predominantly through the divestiture of non-core assets. This program was continued by Olimpia after it acquired it s stake in Olivetti in 2001.

As a result, since September 2001 approximately 10 billion of fixed assets and non-core financial assets have been divested. The disposal of assets has followed our previously discussed Industrial Plan. In general, investments in fixed line, non-telecommunication and non-strategic entities in Europe have been disposed of, allowing us to focus on the Italian market and to invest in new technologies and emerging areas of Europe, such as ADSL and broadband. The disposed of assets encompass both previously consolidated operators, such as 9Télécom of France and Seat Pagine Gialle, and equity investees. Mobile asset development in South America and the Mediterranean Basin have been increased in line with our industrial plan, and non-core assets in those regions have been disposed of, such as our previous equity investment in Globo.com. Further detailed information of all disposals and when they occurred can be found in Note 1 of the Notes to the Consolidated Financial Statements included elsewhere herein.

As part of the ongoing review of operations, we have under consideration other assets for disposal. The disposal of any operations and investments in the future will be broadly in line with our previously announced strategy.

The results achieved through efficiency gains and the disposals plan have strongly impacted Telecom Italia Group s net financial debt (see Item 3. Key Information Selected Financial and Statistical Information for a reconciliation of gross debt to net financial debt over the past three years). From September 2001, the date on which the new management took over responsibility for the running of the Telecom Italia Group, to December 31, 2003 net financial debt decreased by approximately 10 billion (from 43.4 billion to 33.3 billion). The macroeconomic components which determined this reduction were cash flows generated by operations, divestitures of fixed assets and long-term financial investments for approximately 10 billion and distributions to shareholders (dividends, withdrawals and the tender offers by Olivetti on Old Telecom Italia shares) for approximately 10 billion.

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Provisions and Write-downs and Gains on Disposal of Equity Investments, tangible and intangible assets of non recurring nature

The operations of 2001 and 2002 were disproportionately impacted by the ongoing disposal program of non-core assets, as mentioned above, and the ongoing review of operations that occurs throughout the year.

Starting in 2001, with the change in management through Olimpia, we undertook a significant review of all operations, including the assessment of each operations long-term viability within the Telecom Italia Group framework and the related fair value of that operation. The review conducted in 2001 indicated that, due to the acquisition of many of these assets in prior years at relatively high valuations, that the valuations of these assets as of the end of 2001 could no longer be supported by market fundamentals. The provisions and write-downs of goodwill and equity investees were consistent with the strategic guidelines of the Industrial Plan. The following table outlines the extent of which asset impairments, generally related to goodwill and other intangible asset write-offs, occurred:

	Year ended December 31,		
	2001	2002	2003
	(millions of euro)		
Provisions and write-downs of goodwill and equity investments	(2,984)	(6,584)	(879)
Gains on the disposal of equity investments, tangible and intangible assets	465	2,553	105

In 2001, as part of the overall operating review undertaken by management, the write-downs affected several operating units, including 9Télécom, Maxitel, Tele Celular Sul, Tele Nordeste Celular, Med-1, Entel Bolivia, Entel Chile, TIM Brazil and certain companies within the SEAT group. In 2002, provisions were taken for the equity investment in Turkey (Aria Is Tim), Seat Pagine Gialle and Digitel. The Seat Pagine Gialle provision included the accrual of 1,942 million to account for the fact that, upon the disposal of SEAT, we would be required to buy out the put and call arrangements with JP Morgan and take possession of the underlying SEAT shares. In 2003, additional significant impairments were taken for the goodwill of Telecom Italia Media, Entel Chile, Digitel, and EPIClink, and the fixed assets of the LAN network. In all cases, we obtained fair value assessments from either leading investment banks or other highly reputable valuation experts. Such valuations are based on various information, including short and long-term business plans, general local market conditions, market prices and market multiples.

In 2003, gains on the disposals of equity investments and other tangible and intangible assets amounted to 105 million. In 2002, this amount was 2,553 million, mostly related to the disposal of the Spanish equity investment Auna (1,245 million), the equity investment in Bouygues Decaux Télécom (484 million), the equity investment in Austrian mobile operator Mobilkom (115 million) and the disposal of the interest in real estate company Telemaco Immobiliare (110 million), the transfer of selected real estate assets to Tiglio I and II (a total of 219 million) and other minor disposals.

In 2001, which marked the beginning of the disposal program of the new management team, a total of 465 million in gains were recognized, including the transfer of all holdings in satellite sector investments to Mirror International, with a gain of 170 million being recognized, 94 million on the 30% sale of Mediterranean Nautilus, the sale of Globespan Virata Corp for 43 million and other minor investments.

Significant Trends Impacting Our Core Businesses

As described above under General Factors affecting the Telecom Italia Group s Business , management has identified the following key trends that have, and will continue to have, an impact in our two main business areas.

Wireline

- Slowly decreasing voice traffic volumes, due in part to fixed to mobile substitution;
- continuing pricing pressure due to price caps, regulatory constraints and competition;
- introduction of new value added services, including video communication, contributing to a stabilization in voice revenues;
- continuing growth in the number of unbundled lines in Italy, due to a favorable regime (particularly LLU price compared to line rental) for OLOs;

- migration of Internet users from Dial-up to broadband;
- significant broadband and data revenue growth;
- growth in revenues from content and value added services provided on the Internet; and
- growth in broadband services in selected European metropolitan areas, targeted by Telecom Italia for their growth prospects.

Mobile

- Continuing intense competition;
- stable customer base;
- significant growth in value added services driven by the introduction of new technologies/new handsets and by increased customer demand; and
- growth in targeted international markets, particularly Brazil.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with Italian GAAP. Our reported financial condition and results of operations are sensitive to the accounting methods, assumptions and estimates that underlie the preparation of financial statements. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing our financial statements. We believe the following critical accounting policies involve the most significant judgments and estimates used in the preparation of our consolidated financial statements.

We are also required to select accounting principles for the annual reporting of our U.S. GAAP results. Included in the following discussion are the U.S. GAAP principles we have identified that have the potential to generate significant differences from Italian GAAP and for which management is required to make substantial estimates and assumptions.

Revenue recognition

Our primary revenue streams consist of fixed line telecommunication services, mobile telecommunication services, the sale of products including primarily telecommunication (both fixed and mobile) equipment and office products, IT software and services, advertising services, and internet access and related services.

Revenues related to fixed line and mobile telecommunication services, principally network access, long distance, local and wireless airtime usage, are recognized when the services are provided based on the actual minutes of traffic provided and the contracted fee schedule with the customer. Certain revenues derived from telecommunication services, such as installation and activation fees are recognized at the date of installation or activation. Revenues billed in advance are deferred and recognized at the date the related service is provided.

Under U.S. GAAP, we defer recognition of non-refundable connection fees and other initial fees and recognize these over the estimated customer relationship period. We also defer the associated direct expenses over the estimated customer relationship period in an amount equal to or less than the amount of deferred revenues. If the length of the estimated customer relationship period increases or decreases, the amounts of deferred revenue and deferred expense is adjusted over the revised estimated life.

Revenues from the sale of products, including telecommunication equipment and office products, are recognized when title transfers to the customer, which is either at the date the products are shipped or when the products are delivered and accepted by the customer.

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IT services and software revenues are recognized at the date the related services are provided.

Advertising revenue from on-line services is recorded on the date the on-line advertisement is posted to the related web site. Advertising revenue from television is recorded on the date at which the advertisement is shown. Revenues from Internet access and related services primarily represent subscription services, which are recognized over the subscription period on a straight-line basis.

In connection with recording revenue, estimates and assumptions are required in determining the expected conversion of the revenue streams to cash collected. The reserve estimation process requires that management make assumptions based on historical results, future expectations, the economic and competitive environment and changes in the credit worthiness of the Telecom Italia Group s customers, and other relevant factors. If these assumptions prove to be incorrect, Telecom Italia s actual conversion rate of recorded revenue to cash may be lower than expected and we would be required to increase our allowance for doubtful accounts.

Accounting for long-lived assets

Property, plant and equipment and purchased intangible assets other than goodwill are recorded at acquisition cost. If such assets are acquired in a business combination, the purchase price is allocated to the estimated fair value of the acquired property, plant and equipment and intangible assets. Property, plant and equipment and intangible assets are depreciated or amortized on a straight-line basis over their estimated useful lives.

Property, plant and equipment are valued at acquisition or construction cost, less accumulated depreciation. Construction costs include directly allocable costs, an appropriate allocation of material and production overhead and interest accruing during the construction related to debt specifically associated with the related construction project.

Accounting for long-lived assets and intangible assets involves the use of estimates for determining the fair value at the acquisition date for assets acquired in a business combination, and the useful lives of the assets over which the costs of acquiring these assets are charged to the statement of operations. The useful lives of long-lived assets are subject to such variables as technological feasibility, obsolescence, changes in consumer demand and strategic management decisions.

When an impairment in the value of assets occurs, nonscheduled write-downs are made. We assess the impairment of identifiable intangibles and long-lived assets whenever there is reason to believe that the carrying value may exceed the fair value and where a permanent impairment in value is anticipated. The determination of impairments of long-lived and intangible assets involves the use of estimates, which include but are not limited to the cause, the expected timing and the amount of the impairment. Impairment is based on a broad measure of factors. In evaluating assets for impairment, we typically consider, among other things, technological obsolescence, discontinuance of services, changes in market prices, significant negative industry or economic trends, significant underperformance relative to expected historical or projected future operating results and other changes in circumstances that may indicate impairment. All of these assessments require the application of management judgment to the facts and circumstances existing at the time.

To assess impairment of property, plant and equipment and amortizing intangible assets for purpose of U.S. GAAP, we use the guidance outlined in SFAS 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. If, based on the preceding discussion, management has concluded that impairment indicators exist, we will initially review for possible impairment by assessing the undiscounted cash flows expected to be derived from the asset or group of assets, comparing the lowest level of total expected undiscounted cash flow to the carrying value. If the carrying value of the asset or the group of assets exceeds the sum of the undiscounted cash flows, impairment is considered to exist. An impairment charge is assessed by comparing the assets fair value to the carrying value. Fair value can be calculated by a number of different approaches, including discounted cash flow, comparables, market valuations or quoted market prices. The process and steps required to assess the possible impairments of assets, including the identification of possible impairment indicators, assessing undiscounted cash flows, selecting the appropriate discount rate, the calculation of the weighted average cost of capital and the discounts or premiums inherent in market prices requires a substantial amount of management discretion and judgment. If actual results differ from these estimates, or if the Telecom Italia Group adjusts these estimates in future periods, operating results could be significantly affected.

Acquisition accounting

We have entered into certain acquisitions and in the future may make additional acquisitions. We generally account for these acquisitions based on the form of the transaction. Cash exchanged for assets or shares is

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accounted for at its face value. However, other consideration, such as the fair value of shares exchanged (either Telecom Italia shares or other shares of Telecom Italia Group companies used to effect an acquisition) are generally not accounted for in Italian GAAP. In general, the Company uses carry over basis of the assets acquired and liabilities assumed and allocates the difference between the purchase price paid and the carry over basis to the intangible asset goodwill.

The development of a purchase price, and the subsequent allocation of that purchase price to the fair value of the assets acquired and liabilities assumed, is critical due to the long term impact on the statement of operations. To the extent that other assets (for example, fixed assets or trademarks) are identified that are amortizable over a shorter life than goodwill (for which the major part is 20 years), the allocation of that fair value through the purchase price allocation is fundamental to the statement of operations.

For purposes of our U.S. GAAP reporting, we are required to perform a purchase price allocation under SFAS 141, *Business Combinations*. As part of that allocation, it is necessary to develop a purchase price, which under U.S. GAAP requires that all consideration, including the fair value of exchanged shares, be valued. This purchase price, which is generally higher than that arrived at for the same acquisition using Italian GAAP, is then allocated to the fair value of the assets acquired and liabilities assumed. The allocation requires that all assets and liabilities, including those not reflected in the final financial statements of the acquired entity, be valued. This valuation approach requires that significant estimates be made. For example, in the valuation of intangible assets such as a customer list, estimates and judgment are required for the amount of expected future profitability of customers, the expected churn rates, the discount rate used to present value the earnings and the expected economic life of the asset. All of these factors, which are developed in conjunction with the guidance and input of professional third party evaluation experts, require judgment and estimates. A change in any of these estimates or judgments could change the amount to be allocated to a particular intangible or tangible asset. The resulting change in the purchase price allocation to non-goodwill assets or liabilities has a direct impact on the final amount of the purchase price that cannot be allocated to a particular asset (i.e., goodwill). Under U.S. GAAP, this allocation takes on significant meaning, as under existing U.S. GAAP (see also Valuation of Goodwill below), the asset goodwill is no longer a wasting asset. Therefore, as goodwill is no longer amortized on a periodic basis, the cumulative estimates and judgments made in

- the definition of the purchase price,
- the identification of the assets acquired and liabilities assumed in the acquisition;
- the valuation of these assets and liabilities in the purchase price allocation; and
- the assessment of whether selected assets have an indefinite life or are amortizing;

has a significant impact on both the level of total goodwill and the statement of operations.

Goodwill

Goodwill resulting from business combinations is amortized on a straight-line basis over its estimated useful life.

The determination of goodwill is dependent on the allocation of the purchase price to the tangible and intangible assets acquired and liabilities assumed. Such allocation is often based on judgmental factors and estimates of fair values for assets that may not have a readily determinable market value. In addition, the useful life assigned to goodwill is an estimate based on the judgment of management at the time of acquisition. The estimated useful life is subject to adjustment if facts and circumstances indicate that the assets economic life has been affected by other variables, including technological feasibility, competitive factors and contractual rights. During 2003, management re-assessed the goodwill that originated from the original 1999 acquisition of Old Telecom Italia. That assessment was undertaken based on the input of independent third party professionals and the valuations undertaken as part of the Merger. Based on the re-assessment, we concluded that the remaining goodwill of Old Telecom Italia, which was originally established with a life of 20 years, should be reset as of 2003 to 20 years. The effect of this change in estimate was to reduce goodwill amortization expense in 2003 by 227 million.

Nonscheduled write-downs are provided when an impairment in the value of goodwill occurs. We review on a regular basis the performance of our subsidiaries. When there is reason to believe that the goodwill arising from the acquisition of a business is impaired and that the impairment is of a permanent nature, we compare the carrying amount of that subsidiary or business to its fair value. The determination of the fair value of a subsidiary involves extensive use of estimates. Methods commonly used by us for valuations include discounted cash flow methods, comparable market multiples and quoted stock market prices, if available. Factors affecting estimated fair values typically include discount rates, future cash flows, growth rates, weighted average cost of capital, market prices and control premiums. These estimates, including the methodologies used, are important in determining fair value and ultimately the amount of any goodwill impairment.

As of January 1, 2002, we adopted the requirements of SFAS 142, *Goodwill and Other Intangible Assets,* and as a result we ceased amortization of goodwill and indefinite lived intangible assets for U.S. GAAP purposes. The requirements of SFAS 142 include that goodwill be tested for impairment at least annually (and between annual tests when certain triggering events occur) using a two-step methodology. The first step screens for potential impairment at the reporting unit level, while the second step measures the impairment, if any. Under U.S. GAAP, the quoted market price of an asset or other valuation techniques, including discounted cash flow, comparables, etc., are acceptable valuation methodologies to assess fair value. The selection of the various assumptions that are necessary to arrive at the fair value of a reporting unit, including the assumptions used in the underlying business plans, require substantial management judgment and discretion. If actual results differ from these estimates, or if we adjust these estimates in future periods, operating results could be significantly affected.

Deferred taxes

We are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves a jurisdiction-by-jurisdiction estimation of actual current tax exposure and the assessment of the temporary differences resulting from differing treatment of items, such as accruals and amortization, among others, for tax and financial reporting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. We must assess in the course of our tax planning process the ability of Telecom Italia and its subsidiaries to obtain the benefit of deferred tax assets based on expected future taxable income and available tax planning strategies. If in management s judgment, the deferred tax assets recorded will not be recovered, a valuation allowance is recorded to reduce the deferred tax asset.

Significant management judgment is required in determining our provision for income taxes, deferred tax assets, deferred tax liabilities and valuation allowances to reflect the potential inability to fully recover deferred tax assets. In our Italian GAAP financial statements the analysis is based on the estimates of taxable income in the jurisdictions in which we operate and the period over which the deferred tax assets and liabilities will be recoverable. If actual results differ from these estimates, or we adjust these estimates in future periods, we may need to establish an additional valuation allowance which could adversely affect our financial position and results of operations.

Under U.S. GAAP, we assess the recoverability of tax assets based on the criteria of more likely than not , that is, a probability of recoverability just over 50%. The probability assessment requires significant judgment regarding the timing of future book and tax reversals, which could be materially different from the actual results.

Accrued liabilities

We exercise considerable judgment in recording our accrued liabilities and our exposure to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation as well as other contingent liabilities.

Judgment is necessary in assessing the likelihood that a pending claim or a liability will arise and to quantify the possible range of the final settlement. In case the occurrence of a contingency or potential liability is more likely than not, we accrue an amount for contingent liabilities that represents management s estimate at that date. Because of the inherent uncertainties in the foregoing evaluation process, actual losses may be different from the original estimated amount accrued.

For purposes of U.S. GAAP, we apply the guidance outlined in SFAS 5, *Accounting for Contingencies*. Under SFAS 5 a loss contingency is considered to exist when a future use of assets to settle a liability or claim is considered probable and can be reasonably estimated. The necessary estimates used by management rely on the analysis of internal specialists, attorneys, actuaries or other external specialists as considered necessary. A revision of the original estimates may significantly affect future operating results.

Financing, acquisition and lease transactions

We have entered into several financing, acquisition and lease transactions that have resulted in material off balance sheet accounting treatment. These transactions include the sale and the subsequent lease of certain real

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estate assets, the sale of a portion of our equity interest in certain satellite sector entities, and the sale of trade accounts receivable under a securitization program.

We have acquired several companies using the shares of listed subsidiaries as a form of currency, often in conjunction with a mix of cash. For purposes of acquisition accounting, no economic value is ascribed to the shares exchanged, therefore the recorded value of the acquired company does not reflect the value of the underlying shares given up. For purposes of U.S. GAAP, the shares of the subsidiaries used to acquire a target are fair valued as part of the purchase price, generally based on the quoted market price of the shares at the date of the announcement. As there is an economic value ascribed to these shares, the total investment in the acquired company is generally larger, including the associated goodwill, on a U.S. GAAP basis. From 2002, as part of the adoption of SFAS 142, this goodwill is no longer amortized, but rather becomes subject to the fair value impairment tests as previously described.

The sale and the subsequent lease of certain real estate assets, the sale of a portion of our equity interest in certain satellite sector entities, and the sale of accounts receivable under securitization programs have been recorded as sale transactions and gains or losses were recognized for the differences between the fair value of the consideration received and the carrying value of the real estate assets, investments, and receivables sold. The real estate assets sold continue to be used in the ordinary course of our operations and are accounted for as operating leases. Management has substantial flexibility in structuring transactions to effect the recognition of assets, liabilities, gains and losses. For purposes of U.S. GAAP, the sale of the real estate portfolio s were not considered to be sales as we maintained a continuing interest in the properties, therefore no gains were recognized and the assets remain on the balance sheet, with the cash received treated as a secured borrowing. Similarly, the securitization of certain equity stakes in the satellite sector with a special purpose entity resulted in that structured entity also being fully consolidated in our U.S. GAAP results.

However, we have deconsolidated the qualified special purpose entity related to the accounts receivable securitization program initiated in 2001.

In general, U.S. GAAP requires a substance over form approach to structured transactions, including real estate, leases, securitizations and other structured finance transactions. For purposes of U.S. GAAP, for entities created or modified after January 31, 2003, we adopted the financial reporting guidelines of FIN No. 46 (revised December 2003), Consolidation of Variable Interest Entities (FIN 46-R). Consolidation will no longer be determined solely on the majority of voting interests approach, but instead on identifying the primary beneficiary of the variable interest entity. The assessment of which party has the primary benefit will require management to assess each transaction in which it currently holds such financial interests, assessing the probability of expected residual returns and expected losses to arrive at a final decision regarding consolidation.

Derivatives

We enter into several different types of derivative contracts in order to adjust and manage the various cash flows associated with foreign currency and interest rate exposures. For purposes of Italian GAAP, the changes in the fair value of the derivative contract are not accounted for in the statement of operations until the contract has expired. The notional amount of the contracts open at the end of the fiscal year is disclosed. For purposes of U.S. GAAP, we have used the guidance established in SFAS 133, *Accounting for Derivative Instruments and Hedging Activities* . Under U.S. GAAP, we recognize the change in the fair value of the derivative contract in the calculation of net income or loss for the period. The assessment of the fair value of a derivative contract requires the use of quoted market prices, banker price quotations, price quotations for similar instruments traded in different markets and, where applicable, pricing models. Pricing models and their underlying assumptions impact the amount and timing of unrealized gains and losses recognized. As a result, we are required to rely on these pricing models when external fair values are unavailable. The estimates regarding future prices requires estimating several factors, including interest rates, currency values and cash flows. Prices realized in the future will differ from the estimates, therefore producing different financial results.

Adoption of International Accounting Standards

In accordance with the recommendations of the CESR (Committee of European Securities Regulators) published on December 30, 2003 and containing guidelines for companies listed within the EU regarding the transition to IAS/IFRS, (the benchmark regulatory framework) and process of adoption of international accounting standards within the Telecom Italia Group are illustrated below.

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The principal phases which characterized the process of accounting harmonization within the EU are:

- the adoption of Regulation No. 1606 issued by the European Parliament and by the Council of the European Union in July 2002 which provides for the mandatory application of IAS/IFRS, beginning from 2005, for the consolidated financial statements of companies listed in regulated markets of the EU;
- the European Commission s adoption of Regulation No. 1725 dated September 29, 2003, which approved the international accounting standards, and related interpretations, existing at September 14, 2002; IAS 32 and 39, relating to the disclosure and measurement of financial instruments, respectively, and the related interpretations (SIC 5, 16 and 17) were excluded from that approval process as they were in the process of being revised by the IASB;
- the issue, by Italian legislators, of the 2003 EU Law (Law No. 306 dated October 31, 2003) which in Art. 25 provides, moreover, for the obligation of listed companies to draw up not only the consolidated financial statements in accordance with IAS/IFRS (already provided by EU Regulation No. 1606/2002) but also their annual separate financial statements.

Concurrently, the IASB planned a series of projects directed at the implementation of the International Accounting Standards adopted by the EU, including the regulation of transactions not presently covered by IFRS. Certain of these projects have already been concluded whereas others are being completed and/or are at the inception stage.

During 2003, we commenced a specific project relating to the implementation of international accounting standards through the establishment of a dedicated working group which involved the principal companies of the Telecom Italia Group. In particular, an analysis was carried out to identify the principal differences between Italian accounting principles and IAS/IFRS, and to quantify, on the basis of the differences identified, the most significant impacts on the our consolidated financial statements.

The objectives of the project were the following:

- identification of the principal differences between Italian accounting principles and IAS/IFRS, including those for the preparation of the initial opening financial statements (January 1, 2004, the transition date) and quantification of the relative impacts;
- implementation of administrative processes and company information systems to permit the preparation of financial statements and interim accounts in accordance with IAS/IFRS.

In compliance with IAS 1, financial statements in accordance with IAS/IFRS should include, in terms of comparative disclosures, the year previous to the current year. The financial statements as at December 31, 2005 will be the first annual accounts we present in accordance with international accounting standards and, accordingly, will include, for comparative purposes, the financial statements as at December 31, 2004 in accordance with IAS/IFRS.

The analysis conducted thus far has identified certain differences between Italian accounting principles and IAS/IFRS (assuming the endorsement of all the existing Exposure Drafts and excluding the impacts deriving from the first application of international accounting standards), of which the principal differences are described below:

- *goodwill*: goodwill will no longer be amortized annually in the statement of operations but will be subject to a valuation, carried out at least annually, in order to identify any impairment in value (impairment test);

- *treasury stock*: in accordance with IAS/IFRS, treasury stock may not be recorded as an asset and should be cancelled together with the corresponding reserve; furthermore, the amount of treasury stock should be recorded as a reduction of shareholders equity;

- *principles of consolidation*: the possibility of excluding companies that are not significant in size, companies in liquidation and those with dissimilar activities from the scope of consolidation has been eliminated; the shares of consolidated subsidiaries recorded as current assets would be subject to consolidation;

- *stock options*: IFRS 2 classifies stock options within the category of equity settled share-based-payment transactions or rather goods or services received by an entity as consideration for equity instruments of the entity ; in particular, based on this standard, stock options must be valued at their fair value at the time granted (grant date), recording the cost in the statement of operations with an increase in shareholders equity;

- *employee termination indemnities (TFR)*: Italian accounting principles require recognition only of the liability for employee termination indemnities (TFR) on the basis of the nominal liability matured to the end of a reporting period; under IAS/IFRS, TFR fall under the category of defined benefit plans subject to actuarial valuation requiring that the present value of the benefit, payable upon termination of employment, that employees have matured up to the balance sheet date, be recorded;

- *compound financial instruments*: in accordance with IAS 32, the value of compound financial instruments (e.g. convertible notes) should be allocated between financial liabilities and equity instruments (shares, quotas, share purchase options and other equity instruments);

- *derivative financial instruments*: in accordance with IAS/IFRS, all derivatives should be reflected in the financial statements at their fair value. The method of accounting for derivative financial instruments varies based on their characteristics (hedging instruments and non-hedging instruments);

- *asset retirement obligations*: as required by IAS 37, the Telecom Italia Group will record liabilities to be incurred, at the time fixed assets are abandoned, through a legal or constructive obligation assumed upon purchase, construction and development of installations. The liabilities will be recorded at market value, in the period in which they arise, as an accrual, with an offset to the fixed assets to which they refer. Recognition in the statement of operations occurs through the depreciation of the related asset over its estimated useful life;

- *extraordinary items*: there are no extraordinary items under IAS/IFRS;

- *departure from accounting principles envisaged by special laws*: for IAS/IFRS, the accounting treatment of any article or transaction does not take into consideration the effects of special laws or tax laws (e.g. Law No. 58/92).

In relation to the differences identified, projects have been initiated to define the operating procedures for the relative quantification for each company.

Moreover, other differences in accounting principles have been identified, which are being further analyzed, principally relating to provisions for risks, revenue recognition, contract work in process, capitalization of interest, deferred taxes, acquisitions and the recording of dividends in the separate financial statements.

Results of Operations

Reorganization of Business

At the beginning of 2001 we reorganized our businesses into business units and began reporting our results by business unit during 2001. Following the acquisition by Olimpia of its interest in Telecom Italia (formerly Olivetti), and a new management and a new Board of Directors taking control, we implemented a further restructuring plan. This plan included further divestitures of assets, particularly non-strategic international assets. In addition, during 2002 we reorganized our IT and international operations business units and we have continued to reorganize certain of our operations during 2003.

Our businesses are managed and organized on the basis of the following Business Units and the segment disclosure which follows is based on these Business Units.

Wireline. The Wireline Business Unit operates on a national level as the consolidated market leader in wireline telephone and data services and call centers, for final (retail) customers and other (wholesale) providers. On an international level, Wireline develops fiber optic networks for wholesale customers, mainly in Europe and South America.

Mobile. This business unit includes national and international mobile telecommunications businesses which are managed by TIM. Beginning in 2001 international mobile operations were consolidated and managed by TIM, through TIM International. International mobile operations are concentrated in Latin America and in the Mediterranean Basin.

South America. All the activities conducted by the Latin American subsidiaries (whether controlled by Telecom Italia International or by TIM International) were coordinated by Latin America Operations (LAO) until

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February 29, 2004 and were developed in accordance with our overall strategic plan. In particular, from February 2003 to February 2004, Latin America Operations reported directly to the CEO Carlo Buora for Wireline telecommunication, and to Marco De Benedetti for Mobile telecommunication. Since March 1, 2004, the Latin America Operations function is no longer operational and the Business Units Wireline and Mobile have been charged with responsibility for the results of the subsidiaries for which they are accountable in Latin America.

Internet and Media. Starting from August 8, 2003, after the proportional spin-off and sale of substantially all of the directories, directories assistance and business information segments, the Internet and Media Business Unit operates in the following segments:

- Internet. Management of access services (ISP), with Tin.it, management and development of portals (Virgilio with Matrix), and web services, where it occupies a leadership position in the Italian market;
- Television. La7 and MTV, both in the sectors of production and broadcasting of publishing content through the use of television transmission networks entrusted under concession and in the marketing of advertising space in TV programming;
- Office Products and Services. Through the distribution of products, services and solutions for the office through the Buffetti retail network; and
- Professional Publishing in the sector of specialized technical publishing.

Information Technology Market. The IT Market Business Unit was created in 2002 with the aim of focusing the activities previously concentrated in the Information Technology Services Business Unit by type of customer. The IT Market Business Unit is responsible for organizing the information technology activities of the Group, that are marketed to third parties, in particular, central and local governmental administrations moving towards decentralization and e-government, as well as banks and businesses. The IT Market Business Unit provides consultancy services, system integration, CRM and ERP solutions and web services. It is a full business solution provider for government, banks and enterprise.

Information Technology Group. The IT Group Business Unit was created in 2002 to rationalize the activities previously carried out in the Information Technology Services Business Unit. The Business Unit is responsible for organizing technological innovation and service information technology activities within the Telecom Italia Group and covers the entire range of information services, pursuing objectives to reposition its activities to higher value-added products.

Olivetti Tecnost. Olivetti Tecnost and its subsidiaries (the Olivetti Tecnost Group) offer office products and digital printing systems (Office Products Division), specialized application for service automation in banking, retail, trade industry applications, gaming and lottery management (Systems Division). In addition, the group cooperates with the Industrial Operations Division in the development and production of silicon technology (ink-jet print-heads and MEMS), in document management services and mobile phone repairs. The principal geographic markets of this Business Unit are Europe, Asia and North America.

For a complete description of these Business Units, see Item 4. Information on the Telecom Italia Group Business Units . For purposes of the following discussion selected financial data of each Business Unit has been provided for 2001, 2002 and 2003, consistent with the structure of each Business Unit at December 31, 2003.

Results of Operations for the Three Years Ended December 31, 2003

Change in scope of consolidation and Currency Exchange Rates

Our results of operations fully consolidate all Italian and foreign subsidiaries (other than subsidiaries not material to us) in which we hold, directly or indirectly, more than 50% of the voting stock or has dominant influence (effective control).

Other entities in which we hold, directly or indirectly, between 20% and 50% of the voting rights, including jointly controlled companies, are accounted for under the equity method. These include a number of our international investments. The equity in the earnings of such entities (i.e.: our proportional share in the profits or losses of these entities) is included in financial expense. See Note 22 of Notes to the Consolidated Financial Statements included elsewhere herein.

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The following main changes in the scope of consolidation took place during the three year period (2003, 2002 and 2001):

- some investments were disposed of in 2003 and in particular the New SEAT group following the proportional spin-off of the directories and almost all of the directory assistance and business information business segments of SEAT into New SEAT, a newly incorporated company which assumed the current name of Seat Pagine Gialle S.p.A. ; such sale occurred on August 8, 2003 and therefore the activities disposed of were consolidated in the results of operations only for the first seven months of 2003;

- some investments were disposed of in 2002 and were consolidated in the results of operations as follows: the 9Télécom group for the period from January 1, 2002 to June 30, 2002; the former Satellite Business Unit (the Telespazio group) for the period from January 1, 2002 to September 30, 2002 and the company Sogei for the period from January 1, 2002 to June 30, 2002.

Throughout the discussion which follows we use the term organic growth . Organic growth means that the percentage changes provided assume that on a year to year comparison basis the effects of changes in the scope of consolidation are excluded and exchange rates are calculated on a constant currency basis. Constant currency means that the difference in exchange rates between years are eliminated by using the same exchange rate in the later year as in the prior year. Management believes that providing this information enables the reader to better understand the actual operating changes which are impacting the consolidated and business segment results of operations.

Overview of 2003 Results of Operations

As part of our 2003-2005 Industrial Plan we established certain key targets:

- Strengthen our core Italian domestic activities

- Exploit growth opportunities

- Improve cost efficiency

In 2003 we largely met these targets on the basis of some of the key measures we use in monitoring our performance.

With respect to the strengthening of our core Italian domestic activities such key targets were evidenced by:

• Wireline voice market share	plus 0.6 percentage points compared to 2002
• Mobile average revenue per user (ARPU)	plus 1% compared to 2002
• Mobile usage	plus 5.5% compared to 2002

In each case the above reflected a reversal in trends of the prior two years where we had been losing voice market share and the trends in mobile ARPU and usage had also been declining. These improvements must be considered against significant continuing competitive pressures and regulatory developments which have put additional pressure on pricing and pricing strategies which negatively impacted revenue growth in 2003.

In both our core domestic and international markets our strategy has been to focus our investment and significant management time on exploiting growth opportunities. In the domestic market this means our focus has been on value added services and internationally on markets which we consider to have the most potential for growth mobile telecommunications in selected markets, particularly in Latin America, and broadband in selective European markets. We also met certain key performance targets in 2003 as measured by the following:

• *Domestic Value added services*	
• broadband domestic lines	plus 140% over year end 2002
• wireline innovative data services revenues	plus 42.1% compared to 2002
• mobile VAS revenues	plus 36.7% compared to 2002
• *Internationally*	
• Latin America	plus 3.5 million mobile lines
• Europe	selective broadband investments in France and Germany made in 2003

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As discussed under Item 4. Information on the Telecom Italia Group Business Updated Business Plan and Strategy , we have established certain targets under our 2004-2006 Industrial Plan including compound annual revenue growth over the period in excess of 5% and compound annual growth in operating income greater than 10%, in each case assuming no changes in the scope of consolidation and exchange rate impacts. Our ability to achieve these targets will be dependent on maintaining our existing competitive position and successfully growing our revenues with value added services and in our targeted international markets. See Item 3. Key Information Risk Factors . To achieve these goals our capital expenditures will be focused on investments in innovative, value added services and our targeted international investments. See Liquidity and Capital Resources Capital expenditures under the Business Plan . We anticipate that our revenue mix will, as a result, change over time, as the continuing competitive pressures in our core voice markets persist (wireline and mobile), with revenues from domestic innovative services and international expected to reach approximately 38% of total revenues by 2006 compared with 27% in 2003. This is consistent with the trends we have seen in 2003 compared to 2002.

Telecommunications (TLC) License Fee

The impact of certain decisions regarding the TLC License fee had a material one time impact on our 2003 results of operations. After the ruling by the Court of Justice of the European Community stating that the telecommunications license fee established by Italian Law 448/1998, Art. 20, is contrary to EU law, the Telecom Italia Group stopped recording the license fee for 2003 and the financial charges accrued in 2003 on the amount payable for the license fees recorded in previous years. In addition, the statement of income in 2003 benefitted from the reversal of payables and reserves for risks and charges of 1,465 million for the years 2000, 2001 and 2002. Such amount, net of the tax effect of 562 million, contributed to the improvement in net income before minority interests for the year of 903 million.

Moreover, in anticipation of the final ruling by the administrative judge and the subsequent executive order, income has not been credited for the telecommunication license fee of 546 million (362 million by Telecom Italia and 184 million by TIM) paid by the respective companies for the year 1999.

The following table sets forth our Italian GAAP statement of operations for the years ended December 31, 2001, 2002 and 2003.

	2001	2002	2003
		(millions of Euro)	
Operating revenues	32,016	31,408	30,850
Other income	476	504	345
Total revenues	32,492	31,912	31,195
Cost of materials	2,640	2,315	2,081
Salaries and social security contributions	4,919	4,737	4,303
Depreciation and amortization	7,612	7,227	6,779
Other external charges	12,687	12,188	11,934
Changes in inventories	92	62	114
Capitalized internal construction costs	(583)	(675)	(805)
Total operating expenses	27,367	25,854	24,406
Operating income	5,125	6,058	6,789

Financial income	1,446	1,569	992
Financial expense	(6,559)	(4,647)	(3,256)
of which write-downs and equity in losses in affiliated and other companies, net	*(1,771)*	*(487)*	*(91)*
Other income and (expense), net	(3,109)	(5,496)	(1,083)
Income (loss) before income taxes and minority interests	(3,097)	(2,516)	3,442
Income taxes	(579)	2,210	(1,014)
Net income (loss) before minority interests	(3,676)	(306)	2,428
Minority interest	586	(467)	(1,236)
Net income (loss)	(3,090)	(773)	1,192

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Business Unit Financial Data

We operate predominantly in Italy and our core business is focused on domestic and international telecommunications services.

The table below sets forth the gross operating revenues, gross operating profit, operating income and other date for our Business Units, for the last three years:

		Wireline (1)(3)	Mobile	South America (4)	Internet and Media(5)	IT Market (3)	IT Group (3)	Olivetti Tecnost	Sub-total	Other activities and eliminations (3)(6)	Consolidated Total
		(millions of Euro, except number of employees)									
Gross operating revenues	2003	17,216	11,782	1,126	1,297	891	1,100	655	34,067	(3,217)	30,850
	2002(2)	17,047	10,867	1,409	1,991	1,039	996	914	34,263	(2,855)	31,408
	2001(2)	17,174	10,250	1,534	1,957	1,322	1,039	1,097	34,373	(2,357)	32,016
Gross operating profit(7)	2003	8,255	5,502	400	322	84	96	40	14,699	(419)	14,280
	2002(2)	7,951	5,039	450	593	114	98	59	14,304	(289)	14,015
	2001(2)	7,730	4,760	527	444	181	198	27	13,867	(212)	13,655
Operating income	2003	4,969	3,786	137	63	58	(36)	2	8,979	(2,190)	6,789
	2002(2)	4,677	3,358	146	232	64	(40)	4	8,441	(2,383)	6,058
	2001(2)	4,338	3,136	187	31	133	51	(26)	7,850	(2,725)	5,125
Capital expenditures	2003	2,302	1,957	130	102	30	174	20	4,715	179	4,894
	2002(2)	2,475	1,715	216	81	39	149	35	4,710	191	4,901
	2001(2)	2,842	3,151	406	175	33	139	62	6,808	423	7,231
Number of employees at the year end	2003	50,766	18,888	5,049	2,029	4,827	4,107	2,395	88,061	5,126	93,187
	2002(2)	53,935	18,702	5,461	7,715	5,506	5,039	4,527	100,885	5,735	106,620
	2001(2)	58,112	16,721	5,746	9,264	7,454	5,127	4,896	107,320	8,700	116,020

(1) As of June 16, 2003, Domestic Wireline changed its name to Wireline.

(2) The data relating to 2002 and 2001 have been reclassified and presented consistent with the 2003 presentation.

(3) Starting from January 1, 2003, the Netikos group, the Webegg group, the TILab, Loquendo and Eustema are no longer consolidated by the IT Group Operating Activity. BBNed is no longer included in Other Activities. The TILab moved to Other activities and Loquendo and BBNed became part of Wireline, whereas the other companies moved to the IT Market Business Unit.

(4) The data refer to Entel Chile group, Entel Bolivia group, the company Telecom Italia America Latina and the business segment South America of Telecom Italia. See Recent Developments Telecom Italia Group Results for the First Quarter Ended March 31, 2004 compared to March 31, 2003 .

(5) New SEAT, the beneficiary company of the spin-off from Seat Pagine Gialle which took place on August 1, 2003, was sold on August 8, 2003. As a result of this, the 2003 figures include the results of operations for the first seven months of New SEAT Group, as well as the results of operations for the entire year of the remaining part of Seat Pagine Gialle which was renamed Telecom Italia Media following the spin-off.

(6) The data include the operations of the International Affairs Corporate Function, the TILab, the former Business Unit Satellite Services (the Telespazio group) which was disposed of during the fourth quarter of 2002 and consolidated in the statement of operations only for the first nine months of 2002 -, the 9Télécom group sold in the third quarter of 2002 and for which only the statement of operation data was consolidated for the first six months of 2002 -, as well as the finance companies, the centralized group services and the staff functions. See Recent Developments Telecom Italia Group Results for the First Quarter Ended March 31, 2004 compared to March 31, 2003 .

(7) Gross Operating Profit is a non-GAAP financial measure. The following table reconciles operating income to the calculation of Gross Operating Profit by showing the Statement of Operation items included in calculating Gross Operating Profit on a consolidated basis.

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	Year ended December 31,		
	2001	2002	2003
	(millions of Euro)		
Operating income	5,125	6,058	6,789
Depreciation and Amortization	7,612	7,227	6,779
Other external charges:			
• Provision for bad debts	448	546	471
• Write-downs of fixed assets and intangibles	17	58	6
• Provision for risks	389	114	70
• Other provisions and operating charges	431	466	485
Other income (excluding operating grants, reimbursements for personnel costs and costs of external services rendered)	(367)	(454)	(320)
Gross Operating Profit	**13,655**	**14,015**	**14,280**

Year ended December 31, 2003 compared with Year Ended December 31, 2002.

Consolidated Operating Revenues

Our consolidated operating revenues decreased by 1.8% in 2003 compared to 2002. Organic growth was 5.3% (1,545 million), excluding the negative effect of changes in exchange rates (728 million, of which   641 million was attributable to the Latin American telecommunication companies) and the effect of the change in the scope of consolidation (1,375 million, of which   797 million related to the sale of New SEAT from the Internet and Media Business Unit).

Organic growth in revenues was due largely to the following:

- a significant increase in the revenues of the Mobile Business Unit, which were driven by the domestic market (voice traffic and value-added services) and by the Brazilian market;
- an increase in the revenues of the Wireline Business Unit, which was due to growth in income from basic subscription charges, especially for ADSL, and from the sales of telephone equipment, which more than compensated for the drop in traffic in the retail segment. The decline in retail traffic was offset in part by an increase in the wholesale area; and
- a reduction in the sales of the Olivetti Tecnost Business Unit.

The table below sets forth, for the periods indicated, gross operating revenues and consolidated operating revenues by Business Unit and the percentage contribution of such Business Unit to our consolidated operating revenues.

	Year ended December 31,					
	2002(1)			2003		
	Gross Operating Revenues(2)	Consolidated Operating Revenues(3)	% of Consolidated Operating Revenues	Gross Operating Revenues(2)	Consolidated Operating Revenues(3)	% of Consolidated Operating Revenues
	(millions of Euro, except percentages)					
Wireline(4)(5)	17,047	15,112	48.1%	17,216	15,364	49.8%
Mobile	10,867	10,595	33.7%	11,782	11,562	37.5%
South America(6)	1,409	1,369	4.4%	1,126	1,104	3.6%
Internet and Media(7)	1,991	1,900	6.0%	1,297	1,122	3.6%
IT Market(5)	1,039	926	2.9%	891	804	2.6%
IT Group(5)	996	59	0.2%	1,100	41	0.1%
Olivetti Tecnost	914	906	2.9%	655	637	2.1%
Other activities(5)(8)	1,574	541	1.8%	1,126	216	0.7%
Total operating revenues	**35,837**	**31,408**	**100.0%**	**35,193**	**30,850**	**100.0%**

(1) The data relating to 2002 has been reclassified and presented consistent with the 2003 presentation.

(2) Gross operating revenues are total revenues of the various business units of the Telecom Italia Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(3) Consolidated operating revenues are revenues recorded by each business area on a consolidated basis after elimination of intercompany sales.

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(4) As of June 16, 2003, Domestic Wireline changed its name to Wireline.
(5) Starting from January 1, 2003, the Netikos group, the Webegg group, TILab, Loquendo and Eustema are no longer consolidated by the IT Group Operating Activity. BBNed is no longer included in Other Activities. The TILab moved to Other activities and Loquendo and BBNed became part of Wireline, whereas the other companies moved to the IT Market Business Unit.
(6) The data refer to Entel Chile group, Entel Bolivia group, the company Telecom Italia America Latina and the business segment South America of Telecom Italia.
(7) New SEAT, the beneficiary company of the spin-off from Seat Pagine Gialle which took place on August 1, 2003, was sold on August 8, 2003. As a result of this, the 2003 figures include the results of operations for the first seven months of New SEAT Group, as well as the results of operations for the entire year of the remaining part of Seat Pagine Gialle that was renamed Telecom Italia Media following the spin-off.
(8) The data include the operations of the International Affairs Corporate Function, the TILab, the former Business Unit Satellite Services (the Telespazio group) which was disposed of during the fourth quarter of 2002 and consolidated in the statement of operations only for the first nine months of 2002 -, the 9Télécom group sold in the third quarter of 2002 and for which only the statement of operation data was consolidated for the first six months of 2002 -, as well as the financial companies, the centralized group services and the staff functions.

The table below sets forth, for the periods indicated, consolidated operating revenues by geographic area and the percentage of total consolidated operating revenues:

Geographic Area	Year ended December 31, 2002		2003	
	(millions of Euro, except percentages)			
Italy	25,029	79.7%	24,811	80.5%
Rest of Europe	2,665	8.5%	2,478	8.0%
North America	452	1.4%	589	1.9%
Central and South America	2,805	8.9%	2,566	8.3%
Australia, Africa and Asia	457	1.5%	406	1.3%
Total consolidated operating revenues	**31,408**	**100.0%**	**30,850**	**100.0%**

Operating Expenses

The table below sets forth, for the periods indicated, total consolidated operating expenses by major components and expressed as a percentage of total consolidated operating revenues.

	Year ended December 31, 2002		2003	
	(millions of Euro, except percentages)			
Cost of materials	2,315	7.4%	2,081	6.7%
Other external charges	12,188	38.8%	11,934	38.7%
Personnel costs (salaries and social security contributions)	4,737	15.1%	4,303	13.9%
Changes in inventories	62	0.2%	114	0.4%

Capitalized internal construction costs	(675)	(2.2)%	(805)	(2.6)%
Depreciation and amortization	7,227	23.0%	6,779	22.0%
Total operating expenses	**25,854**	**82.3%**	**24,406**	**79.1%**

Our operating expenses decreased by 1,448 million or 5.6% in 2003 compared to 2002. The decrease was attributable to the lower cost of materials, the elimination of the TLC license fee (included in other external charges), personnel costs, depreciation of fixed assets and amortization of intangible assets (including goodwill).

As a percentage of our operating revenues, operating expenses represented 82.3% and 79.1% in 2002 and 2003, respectively.

Cost of Materials

Cost of materials decreased by 234 million or 10.1% in 2003 compared to 2002, mainly as a result of the continuing action taken to improve efficiency.

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Other External Charges

The table below sets forth, for the periods indicated, consolidated other external charges broken down by major components.

	Year ended December 31,	
	2002	2003
	(millions of Euro)	
Costs of external services rendered	9,407	9,684
Rents and lease payments	1,166	1,156
Provision for bad debts	546	471
Provision for risks	114	70
Write-downs of tangible and intangible fixed assets	58	6
TLC license fee	431	62
Other provisions and operating charges	466	485
Total other external charges	**12,188**	**11,934**

Other external charges decreased by 254 million or 2.1% in 2003 compared to 2002. These charges include costs of external services rendered, write-downs of tangible and intangible fixed assets, provision for bad debts, rents and lease payments, telecommunications license fees and other provisions and operating charges.

- Costs of external services rendered increased by 277 million or 2.9% in 2003 compared to 2002. The increase was principally due to higher costs to operate and develop mobile telecommunications (including the start-up of GSM services in Brazil).
- Provision for bad debts declined by 75 million in 2003 compared to 2002. The provision for bad debts is made to write-down receivables to their expected present realizable value.
- TLC license fee decreased by 369 million or 85.6% in 2003 compared to 2002; such decrease was principally due to the cancellation of the Italian government TLC license fee (355 million in 2002) after such fee was found not permissible as described above. Such cancellation also positively impacted provision for risks in that a provision of 29 million was recorded in 2002 by Old Telecom Italia relating to the TLC license fee.
- Other provisions and operating charges which included losses on disposals and write-offs of tangible and intangible fixed assets (18 million in 2003 compared to 36 million in 2002) and taxes other than income taxes (128 million in 2003 against 123 million in 2002), increased by 4.1% in 2003 compared to 2002.

Personnel Costs

Personnel costs (salaries and social security contributions) decreased by 434 million or 9.2% to 4,303 million in 2003 from 4,737 million in 2002. The decrease was mainly due to the following:

- a reduction in employee costs following layoffs in 2003 in Old Telecom Italia and in the Olivetti Tecnost Business Unit; and
- changes in the scope of consolidation.

As a percentage of the Telecom Italia Group s operating revenues personnel costs declined to 13.9% in 2003 compared to 15.1% in 2002. Employees at December 31, 2003 numbered 93,187 (106,620 as of December 31, 2002). The breakdown is as follows:

	As of December 31,	
	2002	**2003**
Italy	86,286	78,069
Abroad	20,334	15,118
Total employees	**106,620**	**93,187**

The reduction of 13,433 employees, compared to December 31, 2002, was due to operating turnover representing 4,604 units (of which 4,134 units were in Italy and 470 units outside Italy) and the change in the scope of consolidation relating to 8,829 units.

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The reduction due to the changes in the scope of consolidation is mainly attributable to the following:

- the sales of companies included in the Internet and Media Business Unit (a decrease of 5,642 units, of which 5,402 units related to the disposal of New SEAT) and Tess (a decrease of 404 units), the Olivetti Tecnost de Mexico business segment (a decrease of 1,266 units), the spin-offs of the Logistics business segment by Wireline (a decrease of 337 units), the Facility Management business segment by Olivetti Multiservices (a decrease of 208 units), the Desktop Management (a decrease of 582 units in IT Group and 22 units in IT Market) and Corporate Solutions businesses (a decrease of 380 units in IT Group and 21 units in Olivetti Tecnost), the sale of the Netikos group (a decrease 207 units) as well as of other minor companies and activities (a decrease of 130 units); and

- the inclusion of Hansenet (an increase of 381 units), Tm News (an increase of 55 units) and Top Services (an increase of 21 units).

In 1992, the Italian government enacted a law that required that Old Telecom Italia ensure that all personnel employed as of February 20, 1992 be covered by the Fondo Previdenza Telefonici (FPT), for the entire retirement benefit amount, including sums due by any prior employment in related companies. The contributions to cover these costs were computed by INPS (the Italian Social Security Authority), and are to be paid in 15 equal annual deferred installments. A subsequent law required that, for financial statement reporting purposes, the accounting for this liability was to be on a cash basis, which also matched the allowable tax deductibility of the payments.

Upon the acquisition of the controlling interest of Old Telecom Italia by Olivetti in 1999, the liability was estimated in the development of the acquisition price paid (i.e., the fair value of the assets acquired and liabilities assumed). At the time, the estimated liability by management was that the total amount due was less than that described by INPS, for a variety of reasons. Therefore, in recording the liability, the lower amount of the estimated range of the liability was recorded in the purchase accounting.

We have continued to debate the merits of the INPS valuation, with the issue still being debated in the Italian court system. However, in 2003 additional facts came to light, including the loss of some individual employee court cases (but not all cases), which lead to a revision of the estimated liability in 2003. Based on that review, an additional 315 million charge was taken in 2003 to record the full extent of the liability as computed by INPS. The total liability of 802 million recorded in the consolidated financial statements is net of the payments made to date to INPS to fund the liability, as required by the 1992 law. See also Notes 14 and 18 of Notes to the Consolidated Financial Statements included elsewhere herein.

Capitalized Internal Construction Costs

Capitalized internal construction costs represent sales of equipment, installations and services at market prices by Telecom Italia Group companies, principally to Telecom Italia and TIM. Capitalized internal construction costs increased by 130 million or 19.3% from 675 million in 2002 to 805 million in 2003; such increase was principally due to higher levels of capital expenditures spent on products and services purchased from subsidiaries, mainly software products.

Gross Operating Profit

The table below sets forth, for the periods indicated, our Gross Operating Profit (see Business Unit Financial Data Note 7 for the calculation of Gross Operating Profit) and gross operating margin (gross operating profit as a percentage of operating revenues).

	Year ended December 31,			
	2002		2003	
	(millions of Euro, except percentages)			
Gross Operating Profit	14,015	44.6%	14,280	46.3%

Gross Operating Profit increased by 265 million or 1.9% in 2003 compared to 2002 due to the greater percentage reduction in certain expenses in 2003 compared to the decrease in operating revenues in the same period. Excluding the effect of changes in exchange rates (a decrease of 146 million) and the effect of the change in the scope of consolidation (a decrease of 344 million), Gross Operating Profit grew by 755 million or 5.6% compared with 2002. Gross operating margin increased to 46.3% in 2003 from 44.6% in 2002 for the same reasons.

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The organic growth in Gross Operating Profit was positively impacted by the cancellation of the Italian government TLC license fee (355 million in 2002), partially offset by the negative impact of the start-up of GSM services in Brazil (131 million).

Depreciation and Amortization

Depreciation and amortization which was recorded on a straight line basis over the estimated useful lives of the assets, decreased by 448 million or 6.2% from 7,227 million in 2002 to 6,779 million in 2003.

Depreciation of tangible fixed assets decreased by 138 million or 3.6% from 3,808 million in 2002 to 3,670 million in 2003 mainly as a result of a lower amount of depreciable assets.

Amortization of intangible assets decreased by 310 million or 9.1% (from 3,419 million in 2002 to 3,109 million in 2003) as a result of the following:

- amortization of goodwill decreased by 316 million from 2,151 million in 2002 to 1,835 million in 2003. The decrease in amortization of goodwill was mainly due to:
    - the write-down of goodwill relating to Seat Pagine Gialle made in the 2002 financial statements and the sale of New SEAT (which reduced goodwill amortization by 304 million),
    - the extension, from 16.5 years to 20 years beginning from January 1, 2003, of the residual estimated period of benefit of the unamortized goodwill which resulted from the acquisition in 1999 of the controlling interest in Old Telecom Italia by Olivetti which reduced goodwill amortization by 227 million.

The foregoing was offset by:

- higher amortization of goodwill arising from the tender offers launched by Olivetti for the ordinary and savings shares of Old Telecom Italia (228 million) and the reclassification, from current to long-term, of the shares held by Olivetti in Old Telecom Italia which were subsequently cancelled as a result of the merger (12 million).

At December 31, 2003, goodwill decreased by 749 million (from 27,894 million as of December 31, 2002 to 27,145 million as of December 31, 2003). The change in goodwill was attributable to the following factors:

- goodwill recorded following the tender offers by Olivetti for the shares of Old Telecom Italia of 4,551 million,
-

the reclassification of the shares of Old Telecom Italia from current assets to intangibles made by Olivetti prior to the merger increasing goodwill by an additional 250 million, and

- the exercise of the J.P. Morgan Chase put option increased goodwill by 428 million relating to the acquisition of the additional SEAT shares.

The foregoing was offset by:

- the reduction in goodwill relating to New SEAT and its subsidiaries following their sale (a total of 3,506 million),
- amortization (1,835 million) and write-downs during the period (754 million), and
- amortization of intangible assets (other than goodwill) of 1,274 million in 2003 compared with 1,268 million in 2002.

Operating Income

The table below sets forth, for the periods indicated, our operating income (total revenues less total operating expenses, including depreciation and amortization and other charges).

	Year ended December 31,	
	2002	**2003**
	(millions of Euro)	
Operating income	6,058	6,789

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Our operating income increased by 731 million or 12.1% in 2003 compared to 2002. Excluding the effect of changes in exchange rates and the effect of the change in the scope of consolidation, operating income grew by 15.6%. The growth in operating income takes account of the negative effect of the start-up of GSM services in Brazil (273 million in 2003) as well as the positive impact of the cancellation of the Italian government TLC license fee (395 million in 2002).

The increase in operating income was mainly due to the improvement in Gross Operating Profit described above and the decrease in depreciation and amortization. As a percentage of operating revenues, operating income increased from 19.3% in 2002 to 22.0% in 2003.

Financial Income, Financial Expense, and Other Income and Expense, Net

The table below sets forth, for the periods indicated, the components of financial and other income and expense, net.

	Year ended December 31,	
	2002	**2003**
	(millions of Euro)	
Financial income	1,569	992
Financial expense	(4,647)	(3,256)
of which write-downs and equity in losses in affiliated and other companies, net	*(487)*	*(91)*
Other income and (expense), net	(5,496)	(1,083)
Total financial expense, net and other income and expense, net	**(8,574)**	**(3,347)**

Total *financial expense, net and other income and expense, net* decreased from a net expense of 8,574 million in 2002 to a net expense of 3,347 million in 2003, a 61.0% decrease.

Financial income (which includes interest and other income on securities, interest income from banks, affiliated and other companies, customers and gain on foreign exchange as well as certain other miscellaneous income, including income on hedging contracts) decreased by 577 million or 36.8%. The decrease was principally due to the reduction in gain on foreign exchange which declined 349 million from 508 million in 2002 to 159 million in 2003.

We record monetary assets and liabilities denominated in foreign currencies at the exchange rate in effect at the date of the transaction. We remeasure such assets and liabilities at the prevailing exchange rate on each balance sheet date with unrealized gains included in financial income.

Financial expense (which includes interest expense on financial indebtedness, foreign exchange losses and income or loss from equity investees) decreased by 1,391 million or 29.9%. The decrease was attributable principally to the following:

- a decrease in interest expense, from 2,241 million in 2002 to 2,173 million in 2003, mainly due to the reduction in the level of interest rates as well as to the lower average borrowings outstanding during 2003;

- the reduction of 719 million in losses on foreign exchange (186 million in 2003 compared to 905 million in 2002) which were positively impacted by the exchange rate effect of the companies in South America. As described above under Financial income we remeasure monetary assets and liabilities denominated in foreign currencies on each balance sheet date. If such remeasure results in unrealized losses, such unrealized losses are included in financial expense;

- the expenses of 161 million for the early exercise of the JP Morgan Chase put option on Seat Pagine Gialle shares finalized in August 2003, as well as the expenses connected with the credit lines granted to Olivetti in connection with the Merger to fund the rights of withdrawal and the tender offers (98 million); and

- the reduction in net write-downs and equity in losses in affiliated and other companies of 396 million, mainly as a result of:

  - the reduction of 67 million in amortization of goodwill in companies accounted for using the equity method (13 million in 2003 compared to 80 million in 2002); and

  - the decrease of 329 million in valuation adjustments to the Telecom Italia Group s share of the equity in the earnings and losses of equity investees and other net write-downs (a loss of 78 million compared to a loss of 407 million in 2002). Such decrease was principally due to the reduction in losses of Sky Italia (formerly Stream) of 150 million and Aria Is Tim of 171 million corresponding to the valuation adjustment made in 2002.

Other income and expense, net decreased from a net expense of 5,496 million in 2002 to a net expense of 1,083 million in 2003. This significant decrease (4,413 million) was mainly due to the reduction in provisions and write-downs of goodwill and equity investments of 5,705 million compared to 2002, partly offset by the decrease in gains on the disposal of equity investments, tangible and intangible assets of 2,448 million compared to 2002, as described below.

- In *2003, provisions and write-downs of goodwill and equity investments* amounted to 879 million:

  - 348 million for the write-down of goodwill on Telecom Italia Media made on the basis of an appraisal of independent advisors;

  - 195 million for the write-down of goodwill on Entel Chile following the implementation of restructuring and reorganization plans;

  - 132 million for the write-down of goodwill on Digitel, in view of the persisting difficult macroeconomic environment in which the company operates;

  - 42 million attributable to the write-down of goodwill on EPIClink in respect of the start of the process to strategically reposition the company within the Group;

  - 59 million related to the dispute with minority shareholders of Digitel;

  - 37 million for the write-down of goodwill related to other minor companies;

  - 36 million related to provisions for risks and other charges on investments; and

  - 30 million to be recognized to Mirror in connection with the recognition of a lower sale price of the investment in Inmarsat with respect to the value assumed in 2001 at the time in which such investment was transferred by Telecom Italia to Mirror.

- In *2002, provision and write-downs of goodwill and equity investments* amounted to 6,584 million and included the following:

  - write-down of the equity investment held in Aria Is Tim, the affiliated mobile telecommunications operator in Turkey (1,491 million) and provision to the reserve for risks and charges related to Aria Is Tim (850 million) for the guarantees provided by the Old Telecom Italia Group to the creditors of Aria Is Tim, and for the loans provided directly by the Old Telecom Italia Group to Aria Is Tim. At that time, Old Telecom Italia concluded that the value of its investments was permanently impaired, since, starting from the awarding of the license, some measures which should have fostered effective competition and guaranteed the full operability of the new entrant, did not effectively take place;

- write-down of Seat Pagine Gialle goodwill (1,544 million) and accrual for the forward purchase commitments of Seat Pagine Gialle shares (1,942 million). The write-down and the provision were made on the basis of the average Seat Pagine Gialle ordinary shares based on trading on the Italian Stock Exchange over the second half of 2002;

- provisions made in conjunction with the disposal of the investment in the 9Télécom Group (316 million);

- reserve provision (43 million), made by Seat Pagine Gialle, for estimated losses arising from the exercise of put options by the founding shareholders of Consodata S.A.; and

- other write-downs of investments of 46 million and of goodwill for 321 million (of which: 103 million for Blu, 75 million for Digitel, 96 million for Netco Redes and 47 million for other minor companies).

- In 2003, restructuring costs amounted to 273 million (of which 196 million was attributable to the parent company Telecom Italia) and were related to expenses and provisions for employee cutbacks and layoffs.

- This compared to restructuring costs of 494 million in 2002 (of which 379 million was attributable to Old Telecom Italia) also related to expenses and provisions for employee cutbacks and layoffs.

- In 2003, charges as required under Law No. 58/1992 in order to cover employees under the former Telephone Employees Pension Fund (FPT) amounted to 387 million, of which 315 million resulted from the redetermination of the liability and 72 million for the related accrued interest. In 2002 accrued interests on the liability to INPS related to the former Telephone Employees Pension Fund (FPT) amounted to 79 million.

- In 2003, gains on the disposal of equity investments, tangible and intangible assets amounted to 105 million compared with 2,553 million in 2002. In 2002 Old Telecom Italia was implementing its strategic plan to sell non-core assets to reduce indebtedness. It had largely completed this plan by the end of 2002. The 2002 gains on the disposal of equity investments, tangible and intangible assets arose from:

  - the sale of our 26.89% interest in AUNA (1,245 million);

  - the sale of our 19.61% interest in Bouygues Décaux Télécom (484 million);

  - the acceptance of the tender offer for Lottomatica shares by the Old Telecom Italia Group (133 million) and by Olivetti and Olivetti International (overall 107 million);

  - the sale of our 25% interest in the Mobilkom Austria group (115 million);

  - the sale of the 40% interest held in Telemaco Immobiliare (110 million);

  - the sale of the 100% interest held in Telespazio (70 million);

  - the concentration of the real-estate assets through the companies IM.SER, Emsa and Telimm into Tiglio I (159 million);

  - the transfer of Old Telecom Italia s Asset Management unit to Tiglio II (60 million);

  - the transfer by Old Telecom Italia of its real estate services businesses (excluding facilities management) to the Pirelli & C. Real Estate Group (15 million);

  - the sale of the 100% interest held in OMS2 to Tiglio I (26 million); and

  - the disposal of other equity investments, fixed assets and business segments (29 million).

- In 2003, other, net (351 million net income) included:

- 1,465 million from the reversal of liabilities and reserves for risks and charges relating to the cancellation of the TLC license fee following the verdict handed down by the European Court of Justice (see Notes 12 and 14 of Notes to the Consolidated Financial Statements for further details);

- 237 million of losses on the disposal of equity investments, tangible and intangible assets (of which 195 million was due to the losses on the sale of the entire stake held in New SEAT after the spin-off);

- 74 million of expenses connected with the spin-off and sale of New SEAT;

- a 55 million payment in contractual settlement with Pagine Italia after the agreement to purchase the Pagine Utili business segment was terminated following our sale of New SEAT;

- 56 million for the additional adjustment made by the parent company Telecom Italia to the estimated value of unused prepaid telephone cards following the start of technical data collection procedures;

- 35 million for the recognition of liabilities referring to prior years on interconnection issues, following clarifications on the part of the regulatory agencies and verifications by the operators involved;

- 295 million for the provisions and write-downs of intangibles and fixed assets made by Latin American Nautilus group (235 million), Telecom Italia Learning Service (27 million), EPIClink (15 million) and other minor companies (18 million) as part of the reorganization transactions;

- 118 million of expenses connected with the Merger principally in respect of fees for advisors, legal and tax consultants, technical experts and expenses for banking charges;

- 48 million of indirect taxes and prior period taxes mainly for the portion of the cost of the tax amnesty not covered by the reserve for income taxes;
- 49 million for losses arising from the settlement of adjustments on the contribution of the international wholesale business segment in 2002;
- 33 million for prior year s adjustments to income taxes; and
- 100 million of other expenses net, which included write-offs of receivable balances, net of release of reserves, and other miscellaneous income and expense.

- In 2002, other, net (892 million net charges) included:
  - income arising from the recovery of pre-amortization interest on the expenses for employee benefit obligations under Law 58/1992 that were paid, with reserve, to INPS up to 1999 following the termination of litigation after the courts ruled in Old Telecom Italia s favor (131 million);
  - the release of reserves (98 million), primarily set up in 2001 by Old Telecom Italia to cover the expenses connected with the agreement to sell Stream to News Corporation and Vivendi Universal/Canal+ after the agreement was terminated;
  - losses from the sale of a 15% stake in Telekom Austria (135 million) and the sale of the equity investment in Seat P.G. held by Olivetti (62 million);
  - expenses connected with the disposal of equity investments (239 million);
  - the extraordinary contributions to INPS established by the year 2000 Italian Budget for the three years 2000-2002 to meet the higher financial requirements covered by the rules of the FPT that was abolished and became part of the general Employee Pension Fund (74 million);
  - write-downs of tangible and intangible fixed assets (190 million, of which 142 million related to our Brazilian companies);
  - provisions to the reserves for risks and charges (226 million, of which 135 million for guarantees provided for the disposals of equity investments and business segments);
  - adjustment to Old Telecom Italia s payable to customers relating to telephone prepaid cards (158 million);
  - other losses on disposals of equity investments, tangible and intangible fixed assets (39 million); and
  - other miscellaneous expenses, net (29 million).

Income Taxes

Income taxes decreased from a benefit of 2,210 million in 2002 to an expense of 1,014 million in 2003. Our statutory income tax rate was 34% in 2003 compared to 36% in 2002.

The 2003 increase in income taxes of 3,224 million was due to the improvement of the result for 2003 (income in 2003 compared with a loss in 2002) and consequently higher levels of taxable income. The increase in taxes was offset in part by the recording of 1,266 million of additional deferred tax assets in addition to those already recorded by Telecom Italia (formerly Olivetti) in 2002 following the write-downs, for tax purposes only, of the shares of the merged company (Old Telecom Italia) held by Olivetti prior to the Merger, and which became recoverable on completion of the Merger.

Net Income (loss)

Net income (loss) before minority interests recorded an improvement from a loss of 306 million in 2002 to net income of 2,428 million in 2003. In 2003, the improvement in net income before minority interests was principally due to the increase in operating income, the reduction in financial expense, net and in other expense, net offset in part by the increase in income taxes. In 2003 net income after minority interests was 1,192 million compared to a net loss after minority interests of 773 million in 2002. Minority interest increased by 769 million (from 467 million in 2002 to 1,236 million in 2003) mainly as a result of the higher levels of profit at TIM group (647 million) and the effects of the Merger of Old Telecom Italia with and into Olivetti (152 million).

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Results of Operations of Business Units for the Year Ended December 31, 2003 compared with the Year Ended December 31, 2002.

Wireline

The following table sets forth for the periods indicated certain financial and other data for the Wireline Business Unit.

Wireline	Year ended December 31, 2002(1)	Year ended December 31, 2003
	(millions of Euro, except percentage and employees)	
Gross operating revenues	17,047	17,216
Gross operating profit	7,951	8,255
% of gross operating revenues	46.6	47.9
Operating income	4,677	4,969
% of gross operating revenues	27.4	28.9
Number of employees at year-end	53,935	50,766

(1) The 2002 financial and other data have been reclassified and presented consistent with the 2003 presentation.

The following table sets forth for the periods indicated certain statistical data for Wireline.

	Year ended December 31, 2002	Year ended December 31, 2003
Subscription and Customers:		

Subscriber fixed lines at period-end in Italy (thousands)(1)	27,142	26,596
Subscriber fixed line growth per annum in Italy (%)	(0.8)	(2.0)
ISDN equivalent lines at period-end in Italy (thousands)(2)	5,756	6,027
Broadband Access in Italy and abroad (ADSL + XDSL) (thousands)(3)	850	2,200
Voice Offers in Italy (thousands)(4)	5,224	5,547
Wireline Traffic:		
Wireline total traffic (Retail and Wholesale) (billions of minutes)	214.9	226.6
of which:		
National(5)	*204.7*	*215.2*
International(6)	*10.2*	*11.4*
Retail Traffic(7):		
Average minutes of use per fixed line subscriber in Italy during period(8)	4,292	4,127
of which:		
Local traffic during period (in average minutes)(9)	*3,198*	*2,971*
Long distance traffic during period (domestic and international) (in average minutes)	*1,094*	*1,156*

(1) Data include multiple lines for ISDN and excludes internal lines.
(2) Data exclude internal lines.
(3) Number of contracts.
(4) Number of contracts; includes Teleconomy, Hellò and other Business voice offers.
(5) Data include total retail traffic (international outgoing traffic excluded) and total domestic wholesale traffic.
(6) Data include international retail outgoing traffic and total international wholesale traffic.
(7) Retail traffic consists of traffic from Telecom Italia customers for local calls, long distance national and international calls and calls to mobile phones.
(8) Includes total retail fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks).
(9) Includes district and internet dial-up traffic.

The Wireline Business Unit (which, until June 16, 2003, was called Domestic Wireline) accounted for gross operating revenues of 17,216 million in 2003 and 17,047 million in 2002, an increase of 169 million, or

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1.0%. The increase in revenues in 2003 reversed the trend of the prior year when revenues declined (-0.7% in 2002) and is attributable principally to an increase in Internet (broadband) and VAS (Value Added Services) particularly for business customers. Revenues from Retail Telephone decreased and revenues from Data and Wholesale services were relatively stable.

Wireline tracks gross operating revenues in the following business areas: retail telephone, retail internet, data business, retail value added serves (VAS) and wholesale services.

Retail Telephone. Revenues from Retail Telephone were 10,368 million in 2003, a decrease of 179 million, or 1.7% from 10,547 million in 2002. Retail telephone revenues consist mainly of traffic revenues and fee revenues: traffic revenues are directly related to traffic volumes, tariffs and fees for tariff packages; fees are attributable to access fees, fees for additional services and for equipment rental and assurance.

Wireline Business Unit has implemented various strategies to limit the impact of increasing competition, with such strategies designed to retain customers and minimize the impact of tariff reductions. During 2003 Telecom Italia s traffic packages, retention and win back strategies resulted in limited revenues losses while its market share on traffic volumes remained stable: Telecom Italia s market share in retail traffic volumes voice and on line traffic (on line traffic is included in Retail Internet) at December 31, 2003 was 72.0% compared with 71.4% at December 31, 2002 and 72.1% at December 31, 2001.

This result reflects retention and win back policies supported by Teleconomy and Hellò offers, combined with selective marketing strategies for high value customers. Flat Voice Offers (Teleconomy offers and other business customized offers) had more than 5.5 million users at the end of 2003 compared to 5.2 million users at the end of 2002 and 4.1 million users at the end of 2001.

Retail Internet. Revenues from Retail Internet amounted to 709 million in 2003, an increase of 114 million, or 19.2% (595 million in 2002). Revenues from Retail Internet consist primarily of internet dial-up traffic revenues and revenues from ADSL, (mass market broadband access,) for access fees and traffic. Revenues from ADSL were approximately 257 million, increasing strongly by 190% over 2002 (89 million), mainly due to the larger customer base while revenues from internet dial-up traffic decreased due to migration to internet connections using broadband access.

Data Business. Revenues from Data Business (Data services, Leased Lines for retail customers and Data Equipment) were 1,510 million in 2003, an increase of 4.6% over 2002 (1,443 million in 2002). Data services consist primarily of data transmission and network services for business customers and residential customers. Revenues from data services are included primarily in fixed subscription and connection fees. The growth in services revenues was driven mainly by innovative data services increasing by more than 42% (520 million in 2003 compared to 366 million in 2002); revenues from Data equipment increased to 246 million (approximately 220 million in 2002).

Revenues from traditional Data services decreased due to customer migration to broadband services from approximately 400 million in 2002 to approximately 340 million in 2003. Leased Lines decreased due to similar migration from approximately 461 million in 2002 to approximately 406 million in 2003.

Retail Value Added Services (VAS). Revenues from VAS were 1,122 million in 2003, an increase of 13.3% on 132 million over 2002 (990 million). VAS consist of new services for all Wireline customers such as Web Services, Outsourcing and Security for Business customers and SMS (short messages from fixed telephone), Memotel (centralized mailbox) and Chi è (identification of calling number) for residential customers. The increase is attributable to the introduction of additional services and VAS packages and growth in the customer base.

Wholesale Services. Revenues from Wholesale Services were 3,269 million in 2003 and remained substantially stable compared to 2002. Wholesale consists of national and international services to other domestic and international telecommunications operators. Domestic Wholesale Services decreased by approximately 45 million due to a price reduction in interconnection services and reduced volumes of traffic, not completely absorbed by growth in revenues from Broadband and other services. International Wholesale Services increased by approximately 45 million, due to significant growth in traffic volumes (approximately one billion minutes or 12%), particularly in traffic carried for other operators.

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In 2003 total Wireline traffic revenues decreased from 8,280 billion in 2002 to 7,948 billion in 2003 with 291 million attributable to retail traffic and 41 million attributable to wholesale traffic. The decrease in retail traffic is a result of:

- commercial policies aimed at customer retention with offers (mainly Teleconomy) which provide discounted tariffs with a monthly fee; offset in part by growth in innovative traffic, Value Added Services, data and ADSL traffic, boosted by the success of Alice offers (ADSL access for mass market) that is now replacing traditional internet traffic (internet dial-up traffic);
- fall in traditional traffic (Voice and Internet dial-up traffic) due to continued price reductions, pushed by competition and by retention policies; and
- to volume reductions in Internet dial-up traffic due to the increasing popularity of ADSL.

The increase in wholesale traffic revenues is due to an increase in revenues from international traffic offset by a decline in national wholesale traffic revenues: revenues from international wholesale traffic increased mainly due to an increase in minutes of traffic carried while revenues from domestic wholesale traffic decreased due to price reductions for interconnection despite an increase in volumes.

The number of subscriber fixed lines in Italy decreased by 2.0% to 26,596 thousands as of December 31, 2003 (27,142 thousand as of December 31, 2002) representing a telecommunications density (fixed line subscribers to total population of Italy) of approximately 47% at December 31, 2003. Such decrease takes into account the increase in ISDN lines (6,027,000 lines at the end of 2003 compared to 5,756,000 lines at the end of 2002 and 5,403,000 lines at the end of 2001). Lines include approximately 18.3 million residential lines (including multiple lines for ISDN), approximately 8.1 million business lines (including multiple lines for ISDN), and approximately 235,000 public telephones lines (including ISDN equivalent lines).

As of December 31, 2003, Wireline had contracts in Italy for approximately 2,040,000 broadband points of access (850,000 at the end of 2002) with approximately 536,000 wholesale points of access (220,000 at the end of 2002) and 1,504,000 retail market points of access (630,000 at the end of 2002). The growth is attributable to the success of various tariff structures geared to the Mass Market (Alice) and to business customers. During 2003 Telecom Italia started the European project International Broadband through:

- the start-up of Telecom Italia France, a new licensed French operator; and
- the acquisition of HanseNet, an existing German operator operating in the area of Hamburg.

The Wireline Business Unit intends to offer access to innovative broadband services in the main European cities, leveraging on its know-how and technological assets, beginning with France and Germany. As of December 31, 2003, Wireline had approximately 160,000 contracts for broadband access outside of Italy.

The contribution of Wireline Business Unit to our consolidated operating revenues amounted to 15,112 million in 2002 and 15,364 million in 2003.

Gross operating profit increased by 304 million, or 3.8% from 7,951 million in 2002 to 8,255 million in 2003, due to significant reductions in personnel costs and expenses as the result of an efficiency plan that brought savings in discretionary operating expenses of approximately 320 million in 2003 and the cancellation of the TLC license fee (204 million in 2002).

Gross operating margin improved by 1.3% from 46.6% in 2002 to 47.9% in 2003.

Operating income increased by 292 million, or 6.2%, from 4,677 million in 2002 to 4,969 million in 2003, as a result of the improvement in gross operating profit and a significant reduction in depreciation and amortization.

Operating margin increased to 28.9% in 2003 compared with 27.4% in 2002.

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Mobile

The following table sets forth, for the periods indicated, certain financial and other data for Mobile.

Mobile	Year ended December 31, 2002	2003
	(millions of Euro, except percentages and employees)	
Gross operating revenues	10,867	11,782
Gross operating profit	5,039	5,502
% of gross operating revenues	46.4	46.7
Operating income	3,358	3,786
% of gross operating revenues	30.9	32.1
Number of employees at year-end	18,702	18,888

The following table sets forth for the periods indicated, certain domestic Italian statistical data for TIM.

	Year ended December 31, 2002	2003
TIM lines at period-end (thousands)(1)	25,302	26,076
TIM lines growth per annum (%)	5.7	3.1
Average revenue per mobile line per month ( )(2)	28.8	29.1
Cellular penetration at period-end (TIM customers per 100 inhabitants)(%)	43.9	45.3
Cellular market penetration at period-end (customers for the entire market per 100 inhabitants)(%)	93.7	99.2
Total mobile outgoing traffic per month (millions of minutes)	1,960	2,090

(1) Includes lines of TACS and GSM services, including Prepaid Customers and excludes the silent lines.
(2) Including Prepaid Card revenues and non TIM customer traffic revenues and excluding equipment sales.

Gross operating revenues from mobile services increased by 8.4% in 2003 compared to 2002, despite the impact of adverse exchange rates which affected certain companies operating in the Mobile Business Unit in Latin America, in particular Venezuela and Brazil. Excluding the effect of changes in exchange rates, organic growth in revenues would have been 12.6% compared to 2002.

This increase was primarily due to TIM s performance in the Italian market (an increase of 6.2%), despite increasing competition, and was mainly attributable to an increase in revenues relating to value added services, with some contribution from international companies. In particular, operating revenues of STET Hellas, TIM s Greek mobile operator, were approximately 805 million in 2003, a 16.8% increase compared to 2002 mainly due to growth of outgoing traffic.

The contribution of the Mobile Business Unit to our consolidated operating revenues was 10,595 million in 2002 and 11,562 million in 2003.

Gross operating profit was 5,502 million in 2003, up 463 million, or 9.2% compared to 2002. The gross operating margin, however, improved to 46.7% in 2003 compared to 46.4% in 2002. Excluding the effect of changes in exchange rates, the growth in gross operating profit would have been 10.2%. The improvement in gross operating profit can be attributed to the positive performance of the core Italian operations and Greece, which offset both the higher costs of GSM start-up in Brazil and the foreign exchange effect in the South American region. The increase in gross operating profit was positively impacted by TIM S.p.A. no longer having to accrue the TLC license fee, following the verdict of the European Court of Justice which declared the institutional law establishing the fees as unlawful. In 2002, the TLC license fee amounted to 151 million.

Operating income was 3,786 million in 2003, an increase of 428 million, or 12.7%, compared to 2002. Excluding the effect of changes in exchange rates, the growth in operating income would have been 10.8%. Operating margin improved from 30.9% in 2002 to 32.1% in 2003. Growth in operating income is mainly attributable to the increase in gross operating profit.

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TIM (parent company)

TIM, which during 2002 merged Blu S.p.A., the fourth Italian GSM operator, effective January 1, 2002, had operating revenues in 2003 of 9,469 million, an increase of 5.0% over 2002 revenues of 9,022 million (8,915 million net of the merger impact, representing an increase of 6.2% over 2002). Revenues from services increased by 6.8% (net of the merger impact) with a ratio on total revenues of 94.9% (94.3% in 2002). The impact of lower prices was more than offset by greater traffic in minute terms (an increase of 5.5% in 2003 compared to 2002).

TIM lines increased to 26,076,000 lines at December 31, 2003, a 3.1% increase compared to December 31, 2002. TIM s total GSM lines increased by 4.9% in 2003, to 25,501,000 lines at December 31, 2003, while TIM s total TACS lines decreased by 42.2% in 2003, to 575,000 lines at December 31, 2003, in each case compared to December 31, 2002. Due to the termination of the TACS services over the next few years and implementation of mobile number portability, customer transfer to the GSM service is in progress. Approximately 97.8% of TIM s lines are now GSM lines. The continuing growth in GSM lines was attributable principally to the continuing growth of the GSM TIM Card (a prepaid rechargeable GSM card), which had 22,906 thousand lines by December 31, 2003 compared to 21,622 thousand lines at December 31, 2002. Prepaid lines (GSM and TACS) grew by 4.2% in 2003.

At December 31, 2003, TIM had a market share in Italy of approximately 46% (including TACS and GSM) compared to 46.1% at December 31, 2002, and a market share of approximately 45.3% for GSM only compared to 45.1% in 2002. The overall market grew by 3.6% in 2003 from 54.8 million lines at the end of 2002 to 56.8 million lines at the end of 2003. The aggregate number of customers at December 31, 2003 for TIM s analog and GSM services represented a penetration rate of 45.3% compared to 43.9% at December 31, 2002. In 2003, TIM had a 27.3% market share of net additional GSM lines, corresponding to 0.8 million of net lines, compared to 1.6 million for Vodafone Omnitel, 1.2 million for Wind and the remaining 0.4 million attributable to H3G (3).

TIM s statistical data excludes 700,000 silent lines. The Italian market, which has a high penetration of prepaid cards, is characterized by certain customers acquiring multiple lines in order to take advantage of specific/time-limited commercial offers. Once these offers expire these customers tend not to continue the use of such lines which is facilitated by the prepaid nature of the arrangement. As a result, TIM excludes the silent lines in order to provide greater consistency between the number of lines managed by TIM and the development of the business.

In 2003, TIM traffic volumes increased by 5.5% in terms of minutes and mobile traffic revenues (net of the Blu merger impact) increased by 3.7% in 2003 compared to 2002 (7,099 million against 6,845 million in 2002). The growth in revenues was also due to the net increase in lines (up 3.1% compared to 2002) and mainly to the higher impact of VAS revenues. The average monthly revenue per mobile line (ARPU) (which includes traffic and VAS revenues) increased from approximately 28.80 in 2002 to 29.10 in 2003 (including service revenues from non TIM clients).

TIM revenues from equipment sales decreased by 3.8% in 2003 compared to 2002 (486 million against 505 million in 2002 net of Blu). In particular handset volumes decreased by 9.5% offset in part by a change in the mix of handsets which can take advantage of innovative products (MMS) with a higher price.

Mobile subscription fees decreased by 22.7% in 2003 compared to 2002 (157 million against 203 million in 2002) due to the continuing sharp expansion in the prepaid service customer base, where no subscription fees are paid.

TIM revenues from Value Added Services (VAS) (1,028 million in 2003) increased by 36.7% compared to 2002 excluding Blu. Due to the continuing introduction of new services and the particular success of SMS services, the VAS business grew significantly with revenues from value added services representing 11.4% of services revenues and 10.9% of total revenues in 2003, compared to 8.9% and 8.4%, respectively in 2002. In 2003, TIM actively marketed the increase in use of VAS through promotional campaigns.

Due to effective CRM and innovative offers, TIM s churn rate decreased to 1.1% per month from 1.5% as recorded in 2002.

TIM gross operating profit was 5,035 million in 2003 compared with the gross operating profit, excluding the merger effect (a loss of 125 million), of 4,529 million. 2003 gross operating profit increased by 11.2% compared with the previous year as a result of the increase in operating revenues and actions taken to control operating costs. Gross operating margin was 53.2% (50.8% in 2002, excluding the merger impact). The increase in gross operating profit was positively affected due to TIM S.p.A. no longer having to accrue the TLC license fee, following the verdict of the European Court of Justice which declared the institutional law establishing the fees as unlawful. In 2002, the TLC license fee amounted to 154 million (151 million net of Blu).

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TIM operating income was 3,863 million in 2003 compared with 2002 operating income, excluding the merger effect (a loss of 170 million) of 3,323 million. 2003 operating income increased by 16.3% compared with 2002. Operating margin was 40.8% in 2003 and 37.3% in 2002 (excluding the merger impact).

TIM operating income was positively impacted by the decrease in depreciation and amortization, as a result of the lower depreciation of intangible assets (a decrease of 106 million) due to the change in the method for calculating depreciation of certain intangibles.

Mobile Latin America

The following table sets forth for the periods indicated certain financial and other data for the Mobile business unit in Latin America.

	Year ended December 31,	
Mobile Latin America	**2002**	**2003**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,298	1,547
Gross operating profit	274	196
% of gross operating revenues	21.1	12.7
Operating loss	(98)	(248)
% of gross operating revenues	(7.6)	(16.0)
Number of employees at year-end	7,050	7,502

The gross operating revenues of the Mobile Business Unit in Latin America were 1,547 million in 2003 compared with 1,298 million in 2002, an increase of 19.2%. Excluding the effect of changes in the exchange rates, the growth in gross operating revenues would have been 50.4%.

Gross operating profit amounted to 196 million, a decrease of 78 million, or 28.5%, compared to 2002, mainly due to the start-up costs of certain companies in Brazil.

Operating loss amounted to 248 million compared to an operating loss of 98 million in 2002.

South America

The following table sets forth, for the periods indicated, certain financial and other data for the Entel Chile group, the Entel Bolivia group, the company Telecom Italia America Latina and the South America business segment of Telecom Italia. Certain financial and other data of the Mobile Business Unit in Latin America are described in the section pertaining to the Mobile Business Unit.

	Year ended December 31,	
	2002	**2003**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,409	1,126
Gross operating profit	450	400
% of gross operating revenues	31.9	35.5
Operating income	146	137
% of gross operating revenues	10.4	12.2
Number of employees at year-end	5,461	5,049

Gross operating revenues were 1,126 million in 2003, a decrease of 20.1% compared to 2002. The decrease was mainly due to the adverse effect of the change in exchange rates (a decrease of 236 million, of which 190 million relates to the Chilean peso, 43 million to the Bolivian currency and 3 million to the Brazilian currency). On a constant currency basis, gross operating revenues would have decreased by 3.3%, primarily due to the decrease in the revenues of the Entel Chile group (-5.8% in local currency) and to the suspension as of April 1, 2002 of the management fee under the terms of the contract with Telecom Argentina.

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The contribution of South America Business Unit to our consolidated operating revenues was 1,369 million in 2002 and 1,104 million in 2003.

The fluctuations in exchange rates described above affected profitability. In particular, gross operating profit decreased by 50 million, or 11.1%, compared to 2002, of which approximately 87 million was attributable to the weakening of currencies against the euro. Excluding the exchange rate effects, gross operating profit would have increased by 8.2%. As a percentage of revenues, gross operating profit was 35.5% in 2003 (31.9% in 2002).

Operating income was 137 million, a decrease of 9 million or 6.2% compared to 2002, due to the exchange rate effect (approximately 27 million). On a constant currency basis, operating income would have increased by 12.3% compared to 2002. As a percentage of revenues, operating income was 12.2% in 2003 compared to 10.4% in 2002.

In order to give an overall view of LAO, the following table sets forth, for the periods indicated, certain financial and other data for all the companies operating in South America, providing both wireline and mobile phone services.

	Year ended December 31,	
South America	**2002**	**2003**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	2,706	2,669
Gross operating profit	724	596
% of gross operating revenues	26.8	22.3
Operating income (loss)	48	(111)
% of gross operating revenues	1.8	(4.2)
Number of employees at year-end	12,511	12,551

Internet and Media

The following tables set forth, for the periods indicated, certain financial and other data for the Internet and Media business unit (the Telecom Italia Media Group). In order to allow a better understanding of the results of the business managed by the business unit after the SEAT Spin-off, the figures are presented on an historical and pro forma basis.

The historical data reflects full consolidation of the SEAT Group in 2002 and, in 2003, full consolidation of the SEAT Group for the first seven months of 2003, with the last five months only consolidating Telecom Italia Media following the demerger and sale of our stake in New SEAT.

Historical data

	Year ended December 31,	
	2002	2003
Internet and Media	**Historical**	**Historical**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,991	1,297
Gross operating profit	593	322
% of gross operating revenues	29.8	24.8
Operating income	232	63
% of gross operating revenues	11.7	4.9
Number of employees at year-end	7,715	2,029

The pro forma data has been prepared assuming that the demerger and sale of New SEAT occurred as of January 1, 2002 so that the financial data only includes Telecom Italia Media for the 2002/2003 years.

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Pro forma data

	Year ended December 31,	
Internet and Media	**2002 Pro forma**	**2003 Pro forma**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	577	595
Gross operating profit	(28)	12
% of gross operating revenues	(4.8)	2.0
Operating loss	(153)	(103)
% of gross operating revenues	(26.6)	(17.3)
Number of employees at year-end	2,284	2,029

The historical gross operating revenues decreased by 34.8% from 1,991 million in 2002 to 1,297 million in 2003, while the pro forma gross operating revenues increased by 3.0% from 577 million in 2002 to 595 million in 2003. The decline in historical gross operating revenues is attributable to the sale of New SEAT in August 2003, resulting in its deconsolidation. In detail the pro forma gross operating revenues are analyzed as follows:

- the Internet business area made the largest contribution to growth; the related revenues increased by 80.3% from 139 million in 2002 to 251 million in 2003. Such increase was affected by the new revenue share methods for calculating Internet dial-up traffic (Decade 7) introduced in 2003;
- revenues from the Television business area were 113 million, an increase of 25 million or 27.8% confirming the editorial success of the program schedule of the two stations;
- revenues from the Office Products and Services business area decreased by 94 million from 279 million in 2002 to 185 million in 2003 largely due to the deconsolidation of IS Products S.p.A. and Incas Production S.r.l., which were sold in 2003;
- revenues from Professional Publishing business area were 25 million, a decrease of 8 million (-23.9%). This was largely due to the deconsolidation of TTG Italia (5 million), which was sold at the beginning of 2003.

The contribution of the Internet and Media Business Unit to our consolidated operating revenues amounted to 1,900 million in 2002 and 1,122 million in 2003.

Historical gross operating profit decreased by 45.8% to 322 million due principally to the sale of New SEAT. Pro forma gross operating profit increased from a loss of 28 million in 2002 to a profit of 12 million in 2003.

Historical operating income decreased to 63 million in 2003 compared to 232 million in 2002, while pro forma operating income improved from a loss of 153 million in 2002 to a loss of 103 million in 2003. The improvements in the pro forma operating income were due to the implementation of rationalization measures and the increase in efficiency, especially in the Internet and Television Areas.

Total Internet active users grew from 2.2 million at the end of 2002 to 2.5 million at the end of 2003.

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Information Technology Market

The following table sets forth, for the periods indicated, certain financial and other data for the IT Market Business Unit. In order to allow a better understanding of the results of the business managed by the business unit in 2003, the figures are presented on an historical and pro forma basis in order to provide percentages and comparable comparative information for 2002 and 2003.

Information Technology Market	2002 (1)	2002 Pro forma (2)	2003 (3)
	Year ended December 31, (millions of Euro, except percentages and employees)		
Gross operating revenues	1,039	777	891
Gross operating profit	114	86	84
% of gross operating revenues	11.0	11.1	9.4
Operating income	64	37	58
% of gross operating revenues	6.2	4.8	6.5
Number of employees at year-end	5,506	5,031	4,827

(1) The 2002 historical financial and other data are consistent with the 2003 scope of consolidation. The 2002 historical data included for the full year 2002 the Finsiel group, the Webegg group, the Netikos group, the company Eustema and Finsiel s Enterprise business segment as well as consolidating for the statement of operations purposes Sogei and Consiel for the first six months of 2002 and for the first eight months of 2002, respectively.

(2) The 2002 pro forma financial and other data has been prepared to be consistent with the 2003 scope of consolidation. As a result Sogei S.p.A. and Consiel S.p.A. have been excluded for the full year 2002. In addition, the 2002 pro forma statement of operations data do not include the Netikos group and Domus Academy, included in the second half of 2002 historical results, and Finsiel s Enterprise business segment has been excluded for the last three months of 2002.

(3) The 2003 historical financial and other data includes:

- the statement of operations data of Domus Academy only for the first six months of 2003, as a result of the transfer by Webegg of its 67.33% stake in Domus Academy to Telecom Italia with effect from July 1, 2003;
- the statement of operations data of Netikos group only for the first six months of 2003, as a result its disposal by IT Telecom to third parties (MyQube S.A.) on July 23, 2003, but with effect from July 1, 2003;

- the statement of operations data of the Enterprise business segment only for the first nine months of 2003, as a result of the transfer by Finsiel to IT Telecom of this business segment on October 1, 2003; the Enterprise business segment is responsible for planning, implementing and selling IT solutions on the enterprise market and managing applications and facilities on this same market.

Historical gross operating revenues decreased by 148 million, from 1,039 million in 2002 to 891 million in 2003. The decrease in gross operating revenues was attributable to the changes in the scope of consolidation between 2002 and 2003. On a comparable consolidation basis, gross operating revenues increased by 14.7% from 777 million in 2002 to 891 million in 2003. This increase is principally due to higher revenues of TSF, Eustema and Agrisian. This increase in revenues more than offset the lower revenues recorded by Finsiel and the Webegg Group.

The contribution of the IT Market Business Unit to our historical consolidated operating revenues amounted to 898 million in 2002 and 804 million in 2003.

Historical gross operating profit declined from 114 million in 2002 to 84 million in 2003, primarily due to the change in scope of consolidation between 2002 and 2003. On a comparable consolidation basis, gross operating profit decreased by 2 million, or 2.3%, compared with the preceding financial year (from 86 million in 2002 to 84 million in 2003). The decrease is principally due to Finsiel s performance, which recorded lower profitability owing to lower volumes recorded in the Government and Enterprise areas, only partially offset by the improved profitability margins recorded by Tele Sistemi Ferroviari on the outsourcing contracts with the State Railways Group companies for the development activities.

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Historical operating income decreased by 6 million, from 64 million in 2002 to 58 million in 2003. On a comparable consolidation basis, operating income for 2003 increased by 21 million, or 56.8%, from pro forma 37 million in 2002 to 58 million in 2003. The improvement in operating income was mainly due to the performance of Tele Sistemi Ferroviari, the Webegg Group and Banksiel. Enhanced overall efficiency, cost reductions and a focus on core business implemented principally by Finsiel beginning in 2002 improved profitability margins with regard to operating income (6.5% in 2003 compared with 4.8% in 2002).

Information Technology Group

The following table sets forth, for the periods indicated, certain financial and other data for the IT Group Operating Activity.

Information Technology Group	**Year ended December 31, 2002(1)**	**2003**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	996	1,100
Gross operating profit	98	96
% of gross operating revenues	9.8	8.7
Operating loss	(40)	(36)
% of gross operating revenues	(4.0)	(3.3)
Number of employees at year-end	5,039	4,107

(1) The 2002 financial and other data have been reclassified and presented consistent with the 2003 presentation.

Gross operating revenues increased by 104 million, or 10.4%, from 996 million in 2002 to 1,100 million in 2003 as a result of higher volumes of work on institutional projects for Corporate, such as the SAP Value Program and the development of the Group Portal, projects for the Wireline segment of Telecom Italia on Broadband, CRM and other innovative projects.

The contribution of the IT Group Operating Activity to our consolidated operating revenues was 59 million in 2002 and 41 million in 2003 as substantially all of the business done by this Operating Activity is for Telecom Italia Group companies.

Gross operating profit decreased by 2 million, or 2%, from 98 million in 2002 to 96 million in 2003 as a result of the increase in third party professional services (163 million) associated with higher levels of business activities, partially offset by a decrease in labor cost (4 million).

The operating loss improved by 4 million, or 10%, from 40 million in 2002 to 36 million in 2003 as a result of higher amortization and depreciation (an increase of 4 million) mainly related to capital expenditures made in the second half of 2002.

Olivetti Tecnost group

The following table sets forth, for the periods indicated, certain financial and other data for the Olivetti Tecnost group.

Olivetti Tecnost group	Year ended December 31, 2002	2003
	(millions of Euro, except percentages and employees)	
Gross operating revenues	914	655
Gross operating profit	59	40
% of gross operating revenues	6.5	6.1
Operating income	4	2
% of gross operating income	0.4	0.3
Number of employees at year-end	4,527	2,395

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Gross operating revenues were 655 million in 2003, including 315 million from the Office Products Division, 179 million from the Systems Division and 161 million from other divisions. Such revenues were distributed as follows: 387 million referred to hardware products, 145 million referred to accessories and 123 million to services and others revenues. Gross operating revenues decreased by 259 million, or 28.3%, (down 14.4% net of the exchange rate effect and changes in scope of consolidation). Such decrease was principally attributable to the Office Products Division, following managements decision to reduce the sales of lower margin products and to the significant decrease in sales of Systems Divisions specialized printers in China and to the decrease in Other Divisions, principally the South America region.

The contribution of the Olivetti Tecnost Business Unit to our consolidated operating revenues was 906 million in 2002 and 637 million in 2003.

Gross operating profit and operating income were affected by the sharp reduction in gross operating revenues. Gross operating profit decreased from 59 million in 2002 to 40 million in 2003 and operating income decreased from 4 million in 2002 to 2 million in 2003.

Other Telecom Italia Group Activities

Our Other Activities principally consist of the TILAB Operating Activity, the companies managed by the International Affairs Corporate Function and the companies/Corporate Functions which provide centralized services to the our Business Units/Operating Activities/Companies. These activities are included within other Activities and Eliminations. See Business Unit Financial Data.

Real Estate and General Services

The activities managed by our Real Estate and General Services consisted of the following: to provide asset and property management services and to leverage the value of our real estate properties, to carry out the project design and work on properties and to provide project and facility management services.

As a result of the finalization of the Tiglio Project (See Item 4. Information on the Telecom Italia Group Description of Property), in February 2003, the Real Estate and General Services operating activity was eliminated and the related activities and resources were transferred to the Telecom Italia Purchasing Corporate Function.

The following table sets forth, for the periods indicated, certain financial and other data for the Real Estate and General Services.

	Year ended December 31,	
Real Estate and General Services	**2002**	**2003**

	(millions of Euro, except percentages and employees)	
Gross operating revenues	846	732
Gross operating profit	88	55
% of gross operating revenues	10.4	7.5
Operating loss	(92)	(76)
% of gross operating revenues	(10.9)	(10.4)
Number of employees at year-end	1,393	1,319

Gross operating revenues decreased by 114 million, or 13.5%, from 846 million in 2002 to 732 million in 2003. Such decrease was mainly due to the adjustment of internal charges to other Telecom Italia Group companies to match market rates and the rationalization of premises occupied by clients.

The contribution of Real Estate and General Services to our consolidated operating revenues was 32 million in 2002 and 28 million in 2003.

Gross operating profit decreased by 33 million, or 37.5%, from 88 million in 2002 to 55 million in 2003. Gross operating profit benefited from 81 million of costs savings arising from actions taken to contain operating costs (external charges and personnel costs) which partially offset the reduction in revenues.

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Operating loss improved by 16 million, or 17.4%, from 92 million in 2002 to 76 million in 2003.

Year ended December 31, 2002 compared with Year ended December 31, 2001.

Consolidated Operating Revenues

Our consolidated operating revenues decreased by 1.9% in 2002 compared to 2001. Organic growth was 3.1%, excluding the effect of changes in exchange rates and the effect of the change in the scope of consolidation. In particular, consolidated operating revenues were impacted by the disposition of the 9Télécom group and Sogei (which were consolidated only for the first six months of 2002), as well as by the disposition of the former Satellite Services Business Unit (the Telespazio group) starting from October 1, 2002.

Organic growth in revenues was due principally to:

- the positive contribution made by the Mobile Business Unit, and
- higher revenues from the Internet and Media segment.

These increases were offset in part by a reduction in the amount contributed by the Wireline Business Unit where traffic revenues, despite a 2.4% increase in terms of minutes, decreased by 8.3% as a result of a lower average return on traffic (retail and wholesale). Such decrease was only partially offset by the increase in basic subscription charges.

The table below sets forth, for the periods indicated, gross operating revenues and consolidated operating revenues by Business Unit and the percentage contribution of such Business Unit to our consolidated operating revenues.

	Year ended December 31,					
	2001(1)			2002(1)		
	Gross Operating Revenues(2)	Consolidated Operating Revenues(3)	% of Consolidated Operating Revenues	Gross Operating Revenues(2)	Consolidated Operating Revenues(3)	% of Consolidated Operating Revenues
	(millions of Euro, except percentages)					
Wireline(4)(5)	17,174	15,222	47.5%	17,047	15,112	48.1%
Mobile	10,250	9,963	31.1%	10,867	10,595	33.7%
South America(6)	1,534	1,531	4.8%	1,409	1,369	4.4%
Internet and Media	1,957	1,880	5.9%	1,991	1,900	6.0%
IT Market(5)	1,322	1,197	3.7%	1,039	926	2.9%
IT Group(5)	1,039	120	0.4%	996	59	0.2%
Olivetti Tecnost	1,097	1,076	3.4%	914	906	2.9%

Other activities(5)(7)	1,276	1,027	3.2%	1,574	541	1.8%
Total operating revenues	**35,649**	**32,016**	**100.0%**	**35,837**	**31,408**	**100.0%**

(1) 2001 and 2002 gross operating revenues and consolidated operating revenues for each major business units and our other activities have been reclassified and presented consistent with the 2003 presentation of gross operating revenues and consolidated operating revenues.

(2) Gross operating revenues are total revenues of our various business units of the Telecom Italia Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(3) Consolidated operating revenues are revenues recorded by each business area on a consolidated basis after elimination of intercompany sales.

(4) As of June 16, 2003, Domestic Wireline changed its name to Wireline.

(5) Starting from January 1, 2003, the Netikos group, the Webegg group, TILab, Loquendo and Eustema are no longer consolidated by the IT Group Operating Activity. BBNed is no longer included in Other Activities. TILab moved to Other activities and Loquendo and BBNed became part of Wireline, whereas the other companies moved to the IT Market Business Unit.

(6) The data refer to Entel Chile group, Entel Bolivia group, the company Telecom Italia America Latina and the business segment South America of Telecom Italia.

(7) The data include the operations of the International Affairs Corporate Function, TILab, the former Business Unit Satellite Services (the Telespazio group) - which was disposed of during the fourth quarter of 2002 and consolidated in the statement of operations only for the first nine months of 2002 -, the 9Télécom group - sold in the third quarter of 2002 and for which only the statement of operation data was consolidated for the first six months of 2002, - as well as the finance companies, the centralized group services and the staff functions.

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The table below sets forth, for the periods indicated, consolidated operating revenues by geographic area and the percentage of total consolidated operating revenues:

Geographic Area	Year ended December 31, 2001		2002	
	(millions of Euro, except percentages)			
Italy	24,895	77.8%	25,029	79.7%
Rest of Europe	2,495	7.8%	2,665	8.5%
North America	1,088	3.4%	452	1.4%
Central and South America	2,759	8.6%	2,805	8.9%
Australia, Africa and Asia	779	2.4%	457	1.5%
Total consolidated operating revenues	**32,016**	**100.0%**	**31,408**	**100.0%**

Operating Expenses

The table below sets forth, for the periods indicated, total consolidated operating expenses by major components and expressed as a percentage of total consolidated operating revenues.

	Year ended December 31, 2001		2002	
	(millions of Euro, except percentages)			
Cost of materials	2,640	8.2%	2,315	7.4%
Other external charges	12,687	39.6%	12,188	38.8%
Personnel costs (salaries and social security contributions)	4,919	15.4%	4,737	15.1%
Changes in inventories	92	0.3%	62	0.2%
Capitalized internal construction costs	(583)	(1.8)%	(675)	(2.2%)
Depreciation and amortization	7,612	23.8%	7,227	23.0%
Total operating expenses	**27,367**	**85.5%**	**25,854**	**82.3%**

Our operating expenses decreased by 1,513 million or 5.5% in 2002 compared to 2001. The decrease was attributable to lower costs of materials, costs of external services rendered (included in other external charges), personnel costs and depreciation and amortization.

As a percentage of our operating revenues, operating expenses represented 85.5% and 82.3% in 2001 and 2002, respectively.

Cost of Materials

Cost of materials decreased by 325 million or 12.3% in 2002 compared to 2001, principally as a result of the effect of the changes in the exchange rates which impacted the Latin American companies and the effect of the change in the scope of consolidation (Telespazio and Sogei).

Other External Charges

The table below sets forth, for the periods indicated, consolidated other external charges broken down by major components.

	Year ended December 31,	
	2001	2002
Costs of external services rendered	9,782	9,407
Rents and lease payments	1,096	1,166
Provision for bad debts	448	546
Provision for risk	389	114
Write-downs of tangible and intangible fixed assets	17	58
TLC license fee	524	431
Other provisions and operating charges	431	466
Total other external charges	**12,687**	**12,188**

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Other external charges decreased by 499 million in 2002 compared to 2001 or 3.9%.

- Costs of external services rendered decreased by 375 million or 3.8% in 2002 compared to 2001. The decrease was principally due to continuing action taken to improve efficiency and the exit from the scope of consolidation of the Telespazio and 9Télécom groups and the company Sogei, partly offset by an increase in the costs of operating and developing mobile telecommunications services.

- Rents and lease payments increased by 70 million or 6.4% in 2002 compared to 2001, mainly due to higher costs incurred by TIM due to its continued expansion, partly offset by the effect of the change in scope of consolidation.

- The TLC license fee, which was principally payable to the Italian Government and was proportional to revenues, decreased by 93 million or 17.7% in 2002 compared to 2001 due to a reduction in both the revenue base and the rate (the aggregate rate for Old Telecom Italia and TIM declined from 2.5% in 2001 to 2.0% in 2002).

- Other provisions and operating charges, which included losses on disposals and write-offs of tangible and intangible fixed assets (36 million in 2002 compared to 29 million in 2001) and taxes other than income taxes (123 million in 2002 compared to 125 million in 2001), increased by 8.1% in 2002 compared to 2001.

Personnel Costs

Personnel costs decreased by 182 million or 3.7% to 4,737 million in 2002 from 4,919 million in 2001. The decrease was mainly due to the following:

- a decrease in Old Telecom Italia employee costs following layoffs in 2001 previously agreed with Old Telecom Italia s unions and continuing reductions in employee levels particularly at Old Telecom Italia; and

- the changes in the scope of consolidation described above. As a percentage of our operating revenues personnel costs declined to 15.1% in 2002 compared to 15.4% in 2001. Employees at December 31, 2002 numbered 106,620 (116,020 as of December 31, 2001). The breakdown is as follows:

	As of December 31,	
	2001	**2002**
Italy	94,234	86,286
Abroad	21,786	20,334
Total employees	**116,020**	**106,620**

The decrease of 9,400 employees compared to December 31, 2001 was mainly due to the net effect of changes in the scope of consolidation and the reduction related to lower levels of personnel, particularly at Old Telecom Italia (a decrease of 6,376 units from 61,081 units as of December 31, 2001 to 54,705 units as of December 31, 2002 - of which 1,086 units represented the balance of employees transferred to other Telecom

Italia Group companies).

The reduction due to the changes in the scope of consolidation is attributable to the following:

- exits of the 9Télécom group (a decrease of 1,003 units), the Telespazio group (a decrease of 1,168 units) and the companies Sogei and Consiel (a total decrease of 1,538 units); and
- the inclusion of Blu (an increase of 618 units) and the companies Netesi and EPIClink (a total increase of 168 units).

The dispute with INPS concerning the calculation of social security charges to be paid by the companies operating in Italy s telecommunications services of the Telecom Italia Group has been ongoing for many years.

In accordance with accepted accounting principles, a payable for an amount equivalent to the minimum estimated liability was initially recorded in the Telecom Italia (formerly Olivetti) Group s consolidated financial statements at the time of the allocation of the excess of purchase of the Old Telecom Italia acquisition in June 1999. At December 31, 2002, Old Telecom Italia s potential range of liability for principal contribution was estimated to be between 964 million and 1,289 million, of which 409 million had already been paid (for more details see Item 8. Financial Information Legal Proceedings).

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Capitalized Internal Construction Costs

Capitalized internal construction costs increased from 583 million in 2001 to 675 million in 2002 (or a 15.8% increase) principally due to higher levels of capital expenditures spent on products and services purchased from subsidiaries.

Gross Operating Profit

The table below sets forth, for the periods indicated, our Gross Operating Profit (see Business Unit Financial Data Note 7 for the calculation of Gross Operating Profit) and gross operating margin.

	Year ended December 31,			
	2001		2002	
	(millions of Euro, except percentages)			
Gross Operating Profit	13,655	42.7%	14,015	44.6%

Gross Operating Profit increased by 360 million or 2.6% in 2002 compared to 2001. The overall increase in Gross Operating Profit was positively impacted by the reduction in costs of external services rendered and cost of materials due to continuing action taken to improve efficiency, as well as lower personnel costs taken together with the modest increase in consolidated operating revenues. The increase in Gross Operating Profit was adversely impacted by the negative effect of the changes in exchange rates and changes in the scope of consolidation. Gross operating margin increased to 44.6% in 2002 from 42.7% in 2001.

Depreciation and Amortization

Depreciation and amortization which was recorded on a straight line basis over the estimated useful lives of the assets, decreased by 385 million or 5.1% from 7,612 million in 2001 to 7,227 million in 2002.

Depreciation of tangible fixed assets decreased by 273 million or 6.7% from 4,080 million in 2001 to 3,807 million in 2002. The decrease in depreciation of tangible fixed assets was principally due to a reduction in the depreciation expense of Old Telecom Italia (251 million), owing to a lower amount of depreciable assets and a change in the mix of depreciable assets.

Amortization of intangible assets decreased by 112 million or 3.2% from 3,532 million in 2001 to 3,420 million in 2002 as a result of the following:

- amortization of goodwill decreased by 143 million from 2,294 million in 2001 to 2,151 million in 2002. The decrease in amortization of goodwill was mainly due to the write-downs of goodwill recorded in 2001. At December 31, 2002 goodwill decreased by 3,993 million (from 31,887 million as of December 31, 2001 to 27,894 million as of December 31, 2002), mainly as a result of the amortization described above as well as the extraordinary write-downs of goodwill on consolidated subsidiaries recorded in 2002 (1,769 million, of which 1,544 million related to Seat Pagine Gialle);

- amortization of intangible assets (other than goodwill) amounted to 1,269 million in 2002 (1,238 million in 2001) and was mainly related to software for telecommunications services.

Operating Income

The table below sets forth, for the periods indicated, our operating income (total revenues less total operating expenses, including depreciation and amortization and other charges).

	Year ended December 31,	
	2001	**2002**
	(millions of Euro)	
Operating income	5,125	6,058

Our operating income increased by 933 million or 18.2% in 2002 compared to 2001. The increase in operating income was mainly attributable to the improvement in gross operating profit described above and the decrease in depreciation and amortization. As a percentage of operating revenues, operating income increased from 16.0% in 2001 to 19.3% in 2002.

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Financial Income, Financial Expense, and Other Income and Expense, Net

The table below sets forth, for the periods indicated, the components of financial and other income and expense, net.

	Year ended December 31,	
	2001	**2002**
	(millions of Euro)	
Financial income	1,446	1,569
Financial expense	(6,559)	(4,647)
of which writedowns and equity in losses in affiliated and other companies, net	*(1,771)*	*(487)*
Other income and (expense), net	(3,109)	(5,496)
Total financial expense, net and other income and expense, net	**(8,222)**	**(8,574)**

Total financial expense, net and other income and expense, net increased from a net expense of 8,222 million in 2001 to a net expense of 8,574 million in 2002, a 4.3% increase.

Financial income increased by 123 million or 8.5%. The growth was principally due to the increase in gain on foreign exchange (251 million) and income on hedging contracts, partly offset by the decrease in capital gain on sale and other income from equity investments.

Financial expense decreased by 1,912 million or 29.2%. The decrease was attributable principally to the following:

- a decrease in interest expense, from 2,430 million in 2001 to 2,241 million in 2002, due to lower average borrowings outstanding during 2002 as well as lower interest rates and fees;
- the reduction in net write-downs and equity in losses in affiliated and other companies (1,284 million), mainly as a result of:
  - the reduction of 236 million in amortization of goodwill in companies accounted for using the equity method (80 million in 2002 compared to 316 million in 2001) principally due to write-downs of goodwill recorded in 2001;
  - the decrease of 1,048 million in valuation adjustments to the Telecom Italia Group s share of equity in the earnings and losses of equity investees and other net write-downs (a loss of 407 million in 2002 compared to a loss of 1,455 million in 2001). The 2002 valuation adjustments were related to the losses of Sky Italia (formerly Stream) of 246 million (241 million in 2001), of Aria Is Tim of 171 million (334 million in 2001) and the earnings balance of 10 million relating to the earnings (losses) of the other companies.

These decreases were offset in part by:

- the increase in losses on foreign exchange (905 million in 2002 compared to 392 million in 2001) due to the negative performance of the rates of exchange which impacted certain Latin American companies, in particular the companies in Venezuela and Brazil.

In 2001, financial expense was also affected by the negative results of the investments in the Nortel Inversora group (238 million) and in the Auna group (203 million) and the write-down of Astrolink (259 million) by Telespazio as the related project was interrupted. The investment in the Nortel Inversora group, the carrying value of which was written-off in the consolidated financial statements at December 31, 2001, remained unchanged in 2002. In 2003 the investment was transferred to Sofora.

Other income and expense, net increased from a net expense of 3,109 million in 2001 to a net expense of 5,496 million in 2002. This significant increase (2,387 million) was mainly due to the increase in provisions and write-downs of goodwill and equity investments (3,600 million), partly offset by the increase in gains on the disposal of equity investments, tangible and intangible assets (2,088 million), as described below.

- In 2002, provision and write-downs of goodwill and equity investments amounted to 6,584 million and included the following:

  - write-down of the equity investment held in Aria Is Tim (1,491 million) and provision to the reserve for risks and charges related to Aria Is Tim (850 million) for the guarantees provided by the Old Telecom Italia Group to the creditors of Aria Is Tim and the loans provided directly

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by the Old Telecom Italia Group to Aria Is Tim. At that time, Old Telecom Italia concluded that the value of its investments was permanently impaired, since, starting from the awarding of the license, some measures which should have fostered effective competition and guaranteed the full operability of the new entrant, had not effectively taken place;

- write-down of Seat Pagine Gialle goodwill (1,544 million) and accrual for the forward purchase commitments of Seat Pagine Gialle shares (1,942 million). The write-down and the provision were made on the basis of the average Seat Pagine Gialle ordinary shares based on trading on the Italian Stock Exchange over the second half of 2002;
- provisions made in conjunction with the disposal of the investment in the 9Télécom Group (316 million);
- reserve provision (43 million), made by Seat Pagine Gialle, for estimated losses arising from the exercise of put options by the founding shareholders of Consodata S.A.; and
- other write-downs of investments for 46 million and of goodwill for 321 million (of which: 103 million for Blu, 75 million for Digitel, 96 million for Netco Redes and 47 million for other minor companies).

- In 2001, provision and write-downs of goodwill and equity investments amounted to 2,984 million and consisted of the following:
  - 1,303 million for the write-down of goodwill relating to consolidated companies (9Télécom group, Entel Bolivia, Entel Chile group, Maxitel group, Tele Celular Sul group, Tele Nordeste Celular group, Tim Brazil, Med-1 group and certain companies in the Seat Pagine Gialle group);
  - 1,078 million for the write-down of goodwill relating to companies accounted for by the equity method (GLB Serviços Interativos, Solpart Participaçoes, Telekom Austria and the Nortel Inversora group); and
  - 603 million for other provisions relating to equity investees.
- In 2002, restructuring costs amounted to 494 million (of which 379 million was attributable to Old Telecom Italia) and were related to expenses and provisions for employee cutbacks and layoffs. This compared to restructuring costs of 400 million in 2001 (of which 203 million attributable to Old Telecom Italia) also related to expenses and provisions for employee cutbacks and layoffs.
- In 2002, accrued interests on the liability to INPS related to the former Telephone Employees Pension Fund (FPT) amounted to 79 million. In 2001, accrued interests on the liability to INPS related to the former Telephone Employees Pension Fund (FPT) amounted to 84 million.
- In 2002, gains on the disposal of equity investments, tangible and intangible assets (2,553 million) arose from:
  - the sale of the 26.89% interest in Auna, the Spanish telecommunication companies in which Old Telecom Italia was a joint venture partner and equity holder (1,245 million);
  - the sale of the 19.61% interest in Bouygues Décaux Télécom (484 million), a French telecommunications company;
  - the acceptance of the tender offer for Lottomatica shares by the Old Telecom Italia Group (133 million) and by Olivetti and Olivetti International (overall 107 million);

- the sale of our 25% interest in the Mobilkom Austria group, one of the Austrian mobile operators (115 million);
- the sale of our 40% interest held in Telemaco Immobiliare (110 million);
- the sale of our 100% interest held in Telespazio, the Group s former satellite operator (70 million);
- the concentration of the real-estate assets through the companies IM.SER, Emsa and Telimm into Tiglio I (159 million);
- the transfer of Old Telecom Italia s Asset Management unit to Tiglio II (60 million);
- the transfer by Old Telecom Italia of its real estate services businesses (excluding facilities management) to the Pirelli & C. Real Estate Group (15 million);
- the sale of the 100% interest held in OMS2 to Tiglio I (26 million); and
- the disposal of other equity investments, fixed assets and business segments (29 million).

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- In 2001, gains on the disposal of equity investments, tangible and intangible assets (465 million) arose from the sale of the 70% holding in Mirror International Holding, the company through which the satellite companies were contributed to the Lehman Brothers group (170 million) and the 30% holding in Mediterranean Nautilus S.A. to the Israeli company F.T.T. Investment (94 million), the dilution of the investment in Auna (16 million) and the increase in the net equity of Lottomatica as a result of the capital increase set aside for third parties when it was listed (64 million), the sale of the residual equity investment in Globespan Virata Corp. (43 million), and other minor disposals (78 million).

- In 2002, other, net (892 million net charges) included:

  - income arising from the recovery of pre-amortization interest on the expenses for employee benefit obligations under Law 58/1992 that were paid, with reserve, to INPS up to 1999 following the termination of litigation after the courts ruled in Old Telecom Italia s favor (131 million);

  - the release of reserves (98 million), primarily set up in 2001 by Old Telecom Italia to cover the expenses connected with the agreement to sell Stream to News Corporation and Vivendi Universal/Canal+ after the agreement was terminated;

  - losses from the sale of a 15% stake in Telekom Austria (135 million) and the sale of the equity investment in Seat P.G. held by Olivetti (62 million);

  - expenses connected with the disposal of equity investees (239 million);

  - the extraordinary contributions to INPS established by the year 2000 Italian Budget for the three years 2000-2002 to meet the higher financial requirements covered by the rules of the Fondo Previdenza Telefonici (FPT) that was abolished and became part of the general Employee Pension Fund (74 million);

  - write-downs of tangible and intangible fixed assets (190 million, of which 142 million related to the Brazilian companies);

  - provisions to the reserves for risks and charges (226 million, of which 135 million for guarantees provided for the disposals of equity investments and business segments);

  - adjustment to Old Telecom Italia s payable to customers relating to telephone prepaid cards (158 million);

  - other losses on disposals of equity investments, tangible and intangible fixed assets (39 million); and

  - other miscellaneous expenses, net (29 million).

- In 2001, other, net (106 million net charges) included:

  - income from the release of reserves by Old Telecom Italia recorded in prior years for risks which did not materialize (120 million mainly relating to the reserve for a contract with Iraq of 62 million and the reserve for corporate restructuring of 50 million);

  -

income (32 million) deriving from the partial cancellation, by the Council of State, of resolution No. 7533/1999 of the Antitrust Authority under which TIM and Vodafone Omnitel were levied administrative fines for the alleged violation of antitrust laws relating to the price fixing of fixed-mobile rates;

- the provision for expenses connected with the Vivendi/Canal Plus agreement for the transfer of the investment in Sky Italia (formerly Stream) (248 million);

- the extraordinary contributions to INPS established by the 2000 Finance Bill for the three years 2000-2002 to meet the higher financial requirements covered by the rules of the Fondo Previdenza Telefonici (FPT) that was abolished and became part of the general Employee Pension Fund (77 million); and

- the costs resulting from the decision to reposition the broadcasting station La7 as a consequence of the closing of a series of contracts (85 million).

Income Taxes

Income taxes represented a benefit of 2,210 million in 2002 compared to a tax expense of 579 million in 2001. The Group s statutory income tax rate for 2002 and 2001 was 36%.

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The 2002 decrease in income taxes 2,789 million was due to a reduction in the taxable base caused mainly by the write-downs of equity investments which involved an increase in prepaid income taxes, as well as to certain tax benefits arising from the merger of Blu into TIM.

Net Income (loss)

Net loss before minority interests decreased from a net loss of 3,676 million in 2001 to a net loss of 306 million in 2002. The decrease in net loss before minority interests in 2002 was principally attributable to the income tax benefit in 2002, together with the increase in operating income and the reduction in total financial expense, net, offset in part by the increase in other expense, net. Net loss after minority interests was 773 million in 2002 compared to a net loss of 3,090 million in 2001. Minority interests decreased from a benefit of 586 million in 2001 to a loss of 467 million in 2002 mainly due to higher levels of profit at Old Telecom Italia Group (which reported net income in 2002 compared to a net loss in 2001).

Results of Operations of Business Units for the Year Ended December 31, 2002 compared to the Year Ended December 31, 2001.

Wireline

The following table sets forth, for the periods indicated, certain financial and other data for the Wireline Business Unit.

	Year ended December 31,	
	2001(1)	**2002(1)**
Wireline	**(millions of Euro, except percentages and employees)**	
Gross operating revenues	17,174	17,047
Gross operating profit	7,730	7,951
% of gross operating revenues	45.0	46.6
Operating income	4,338	4,677
% of gross operating revenues	25.3	27.4
Number of employees at year-end	58,112	53,935

(1) The 2001 and 2002 financial and other data have been reclassified and presented consistent with the 2003 presentation.

The following table sets forth for the periods indicated certain statistical data for Wireline.

	Year ended December 31, 2001	2002
Subscription and Customers:		
Subscriber fixed lines at period-end in Italy (thousands)(1)	27,353	27,142
Subscriber fixed line growth per annum in Italy (%)	0.7	(0.8)
ISDN equivalent lines at period-end in Italy (thousands)(2)	5,403	5,756
Broadband Access in Italy and abroad (ADSL + XDSL) (thousands)(3)	390	850
Voice Offers in Italy (thousands)(4)	4,094	5,224
Wireline Traffic:		
Wireline total traffic (Retail and Wholesale) (billion of minutes)	209.8	214.9
of which:		
National(5)	201.1	204.7
International(6)	8.7	10.2
Retail Traffic(7):		
Average minutes of use per fixed line subscriber in Italy during period(8)	4,739	4,292
of which:		
Local traffic during period (in average minutes)(9)	3,575	3,198
Long distance traffic during period (domestic and international) (in average minutes)	1,164	1,094

(1) Data include multiple lines for ISDN and excludes internal lines.

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(2) Data exclude internal lines.
(3) Number of contracts.
(4) Number of contracts; includes Teleconomy, Hellò and other Business voice offers.
(5) Data include total retail traffic (international outgoing traffic excluded) and total domestic wholesale traffic.
(6) Data include international retail outgoing traffic and total international wholesale traffic.
(7) Retail traffic consists of traffic from Telecom Italia customers for local calls, long distance national and international calls and calls to mobile phones.
(8) Includes total retail fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks).
(9) Includes district and internet dial-up traffic.

The Wireline Business Unit accounted for gross operating revenues of 17,047 million in 2002 and 17,174 million in 2001, a decrease of 127 million, or 0.7%. The small decrease in revenues in 2002 is attributable to a decrease in Retail Telephone revenues only partially offset by an increase in VAS (Value Added Services) revenues. Internet and Data revenues were largely unchanged despite significant growth in ADSL revenues in 2002 compared to 2001.

Retail Telephone. Revenues from Retail Telephone were 10,547 million in 2002, a decrease of 446 million, or 4.1% compare to 10,993 million in 2001.

Traffic revenues decreased significantly by more than 12% compared to 2001 due to the continuing decline in prices and lower volumes of 11% compared to 2001. Prices decreased as a result of commercial policies aimed at customer retention with offers such as Teleconomy which provide discounted tariffs with a monthly fee and competition. In addition, further reductions in traffic tariffs were only partially offset by an increase in subscription fees due to the price cap system (adjustments in subscription fees were made on July 1, 2001 and February 1, 2002). Traffic volumes in Retail Telephone decreased as a result of the substitution effect of fixed to mobile traffic (long distance traffic) and competition (local and international outgoing traffic).

The Wireline Business Unit during 2002 began implementing strategies to limit the impact of competition and revenue losses. These strategies slowed further market share losses. Market share on retail traffic volumes voice and on line internet traffic -, at December 31, 2002 was 71.4% in line with December 31, 2001 (72.1%) although market share on voice traffic at December 31, 2002 was 72.8% compared with 75.8% at December 31, 2001.

This result reflected retention and win back policies supported by new Teleconomy offers, combined with selective marketing strategies for high value customers. Flat Voice Offers (Teleconomy offers and other business customized offers) had 5.2 million users at the end of 2002 compared to 4.1 million users at the end of 2001.

Retail Internet. Revenues from Retail Internet were 595 million in 2002 and 599 million in 2001. Growth in ADSL revenues (89 million in 2002 and 9 million in 2001), mainly due to growth in the customer base offset the decrease in on line dial-up traffic revenues which decreased due to reduction in volumes and prices (competition and ADSL substitution).

Data Business. Revenues from Data Business were 1,443 million in 2002, an increase of 1.0% over 2001 (1,429 million in 2001). Growth in services revenues was driven mainly by innovative data services while revenues in traditional data services, leased lines and equipment decreased mainly due to substitution for innovative services and price reductions in leased lines.

Retail Value Added Services (VAS). Revenues from VAS were 990 million in 2002 and increased by 24.4% over 2001 (796 million in 2001). Retail Value Added Services (VAS) increased due to the introduction of new services for all Wireline customers such as Web Services, Outsourcing and Security for Business customers and SMS (short messages from fixed telephone), Memotel (centralized mail box) and Chi é (identification of calling number) for residential customers.

Wholesale Services. Revenues from Wholesale Services were 3,269 million in 2002 and 3,175 million in 2001, a 3.0% increase. Such growth was mainly due to International Wholesale Services, which recorded a significant increase in revenues mainly due to higher volumes. Domestic Wholesale revenues increased mainly in XDSL services and in Traffic revenues, principally due to volume growth in all categories of traffic.

The number of fixed line subscribers in Italy decreased by 0.8% to approximately 27,142 million at December 31, 2002 representing a telecommunications density (fixed line subscribers to total population of Italy) of approximately 48% at December 31, 2002, which remained unchanged compared to December 31, 2001. Such decrease takes into account the increase in ISDN lines (5,403,000 lines at the end of 2001 and 5,756,000 lines at the end of 2002).

The contribution of the Wireline Business Unit to our consolidated operating revenues amounted to 15,222 million in 2001 and 15,112 million in 2002.

Despite the revenue decline, Gross operating profit increased from 7,730 million in 2001 to 7,951 million in 2002, a 2.9% increase compared to 2001, due to significant reductions in personnel costs as well as expenses reduction resulting from an efficiency plan that brought savings in discretionary operating expenses of approximately 500 million.

Gross operating margin improved by 1.6%, from 45.0% in 2001 to 46.6% in 2002 as cost savings made up for the small decline in revenues.

Operating income increased from 4,338 million in 2001 to 4,677 million in 2002, as a result of efforts to contain costs and improve the level of efficiency of invested capital.

Operating margin increased to 27.4% in 2002 compared with 25.3% in 2001, also due to a significant reduction in depreciation and amortization.

Mobile

The following table sets forth, for the periods indicated, certain financial and other data for Mobile.

Mobile	Year ended December 31, 2001	Year ended December 31, 2002
	(millions of Euro, except percentages and employees)	
Gross operating revenues	10,250	10,867
Gross operating profit	4,760	5,039
% of gross operating revenues	46.4	46.4

Operating income	3,136	3,358
% of gross operating revenues	30.6	30.9
Number of employees at year-end	16,721	18,702

The following table sets forth for the periods indicated, certain statistical data for TIM.

	Year ended December 31,	
	2001	2002
TIM lines at period-end (thousands)	23,946	25,302
TIM lines growth per annum (%)	10.9	5.7
Average revenue per mobile line per month ( )(1)	29.1	28.8
Cellular penetration at period-end (TIM customers per 100 inhabitants)(%)	41.6	43.9
Cellular market penetration at period-end (customers for the entire market per 100 inhabitants)(%)	89.0	93.7
Total mobile outgoing traffic per month (millions of minutes)	1,795	1,960

(1) Including Prepaid Customers revenues and non TIM customer traffic and excluding equipment sales.

Gross operating revenues from mobile services increased by 6% in 2002 compared to 2001, despite the impact of adverse exchange rates which affected certain companies included in the Mobile Business Unit in Latin America, in particular Venezuela and Brazil. Excluding the effect of changes in exchange rates, organic growth of revenues would have been 11.9% compared to 2001.

This increase was primarily due to TIM s performance in the Italian market (an increase of 6.7%), despite increasing competition, and was mainly attributable to the increase in revenues relating to value added services,

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with some contribution from international companies. In particular, operating revenues of STET Hellas were approximately 689 million in 2002, a 31.7% increase compared to 2001 mainly due to growth of outgoing traffic and value added services. The number of mobile lines at STET Hellas increased 17.8%.

The contribution of the Mobile Business Unit to our consolidated operating revenues was 9,963 million in 2001 and 10,595 million in 2002.

Gross operating profit was 5,039 million in 2002, up 279 million, or 5.9% as compared to 2001. The gross operating margin however remained flat at 46.4%. Excluding the effect of changes in exchange rates, the growth in Gross Operating Profit would have been 8.6% and is mainly attributable to the good performance of TIM and STET Hellas as well as improved results of TIM Perù, partially offset by the start-up costs of certain Latin American companies.

Operating income was 3,358 million in 2002, an increase of 222 million, or 7.1%, compared to 2001.

Operating margin improved from 30.6% in 2001 to 30.9% in 2002. Growth in operating income is mainly attributable to the increase in gross operating profit.

TIM (parent company)

TIM, which during 2002 merged Blu S.p.A., the fourth Italian GSM operator effective as of January 1, 2002, had operating revenues in 2002 of 9,022 million, an increase of 8.0% over 2001 (8,915 million net of the merger impact, representing an increase of 6.7% over 2001). Revenues from services increased by 6.5% (net of the merger impact) with the same percentage of 2001 on total revenues (94.3%). The impact of lower prices was more than offset by greater traffic in minute terms (an increase of 7.8%).

TIM lines increased to 25,302,000 lines at December 31, 2002, a 5.7% increase compared to December 31, 2001. TIM s total GSM lines increased by 9.4% in 2002, to 24,307,000 lines at December 31, 2002, while TIM s total TACS lines decreased by 42.6% in 2002, to 995,000 lines at December 31, 2002, in each case compared to December 31, 2001. Due to termination of the TACS services, customer transfer was taking place to TIM s GSM service. Approximately 96% of TIM s lines in 2002 were GSM lines. The continuing significant growth in GSM lines was attributable principally to the continuing growth of the GSM TIM Card (a prepaid rechargeable GSM card), which had 21,622 thousand lines by December 31, 2002 compared to 19,674 thousand lines at December 31, 2001. Prepaid lines grew by 6.3% in 2002.

At December 31, 2002, TIM had a market share in Italy of approximately 46.1% (including TACS and GSM) compared to 46.7% at December 31, 2001, and a market share of approximately 45.1% for GSM only compared to 44.8% in 2001. The overall market grew by 6.8% in 2002 from 51.3 million lines at the end of 2001 to 54.8 million lines at the end of 2002. The aggregate number of customers at December 31, 2002 for TIM s analog and GSM services represented a penetration rate of 43.9% compared to 41.6% at December 31, 2001.

In 2002, TIM traffic volumes increased by 7.8% in terms of minutes and mobile traffic revenues (net of the Blu merger impact) increased by 3.5% in 2002 compared to 2001 (6,845 million in 2002 against 6,613 million in 2001). The net increase in lines (up 5.7% compared to 2001) was partially offset by the continuing decline in ARPU due to increasing competitive pressures and the effect on prices. ARPU per mobile line (which includes traffic revenues and subscription fees) decreased from approximately 29.10 in 2001 to 28.80 in 2002 (including visitors).

TIM revenues from equipment sales increased by 9.3% in 2002 compared to 2001 (505 million net of Blu against 462 million in 2001) as a result of the launch of Multimedia Messaging Services (MMS services) and TIM customers upgrading their phones to be able to utilize such services. Mobile subscription fees decreased by 5.6% in 2002 compared to 2001 (203 million against 215 million in 2001) due to the continuing sharp expansion in the prepaid service customer base, where no subscription fees are paid.

TIM revenues from VAS (752 million in 2002 net of Blu) increased by 41.4% compared to 2001. Due to the continuing introduction of new services and the particular success of SMS services, the VAS business grew significantly with revenues from value added services representing 8.9% of services revenues and 8.4% of total revenues in 2002, compared to 6.7% and 6.4%, respectively in 2001. In 2002, TIM actively marketed the increase in use of VAS through promotional campaigns.

The TIM churn rate, as a result of increased competition, rose to 1.5% per month, up from the 1.3% rate recorded in 2001.

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In 2002, TIM gross operating profit was 4,404 million. Excluding a loss of 125 million due to the merger effect, gross operating profit was 4,529 million, an increase of 7.2% compared with the previous year (4,225 million) as a result of the increase in operating revenues and the actions taken for the containment of operating costs. Excluding the merger impact, gross operating margin was 50.8% (50.6% in 2001).

In 2002, TIM operating income was 3,153 million. Excluding a loss of 170 million due to the merger impact, operating income was 3,323 million, a 2.8% increase compared with 2001. Excluding the merger impact, operating margin was 37.3% in 2002 and 38.7% in 2001.

TIM operating income was impacted by the increase in depreciation and amortization, as a result of the following:

- the amortization only for fiscal purposes of the UMTS license (121 million gross of tax effects of 49 million);
- the higher depreciation of fixed assets (an increase of 53 million) due to the revision of the estimate of the useful life of the depreciable assets.

Mobile Latin America

The following table sets forth for the periods indicated certain financial and other data for Mobile Business Unit in Latin America, coordinated at that time by Latin American Operations.

	Year ended December 31,	
Mobile Latin America	**2001(1)**	**2002**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,403	1,298
Gross operating profit	355	274
% of gross operating revenues	25.3	21.1
Operating loss	(72)	(98)
% of gross operating revenues	(5.1)	(7.6)

Number of employees at year-end	5,678	7,050

(1) The 2001 financial and other data have been reclassified and presented consistent with the 2002 presentation.

The gross operating revenues of the Mobile Business Unit in Latin America were 1,298 million in 2002 compared with 1,403 million in 2001, a decrease of 7.5%. The decrease was mainly due to the weakening of the Brazilian and Venezuelan currencies against the Euro.

Gross operating profit was 274 million, a decrease of 81 million, or 22.8%, compared to 2001, mainly due to the start-up costs of certain companies.

Operating loss was 98 million in 2002 compared to an operating loss of 72 million in 2001.

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South America

The following table sets forth, for the periods indicated, certain financial and other data for the Entel Chile group, the Entel Bolivia group, the company Telecom Italia America Latina and the South America business segment of Telecom Italia. Certain financial and other data of the Mobile Business Unit in Latin America are described in the section pertaining to the Mobile Business Unit.

	Year ended December 31,	
	2001(1)	2002
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,534	1,409
Gross operating profit	527	450
% of gross operating revenues	34.4	31.9
Operating income	187	146
% of gross operating revenues	12.2	10.4
Number of employees at year-end	5,746	5,461

(1) The 2001 financial and other data have been reclassified and presented consistent with the 2002 presentation.

Gross operating revenues were 1,409 million in 2002, a decrease of 8.1% compared to 2001. The decrease was mainly due to the adverse effect of the change in exchange rates (a decrease of 212 million, of which 182 million related to the Chilean peso and 29 million to the Bolivian currency). On a constant currency basis, gross operating revenues would have increased by 5.7%, primarily due to an increase in the revenues of the Entel Chile group (+12.3% in local currency). This was partially offset by the effects of deregulation in the Bolivian market (Entel Bolivia reported a reduction in revenues of approximately 4.5% in local currency). In addition, revenues also declined due to the suspension as of April 1, 2002 of the management fee under the terms of the contract with Telecom Argentina. Due to general economic conditions in Argentina, Telecom Argentina experienced significant financial difficulties, suspending payment of its outstanding debt and began restructuring its outstanding debt during 2002.

The contribution of South America Business Unit to our consolidated operating revenues was 1,531 million in 2001 and 1,369 million in 2002, respectively.

The fluctuations in exchange rates adversely affected profitability. In particular, gross operating profit decreased by 77 million, or 14.6%, compared to 2001, of which approximately 65 million was attributable to the weakening of local currencies against the Euro. Excluding the exchange effects, the reduction in gross operating profit would have been 2.3%, due primarily to the suspension of the management fee from Telecom Argentina and the lower profit margins in Bolivia partially offset by a recovery in profit margins in the Chilean mobile sector. As a percentage of revenues, gross operating profit was 31.9% in 2002 and 34.4% in 2001.

Operating income is consistent with the trends described with regard to gross operating profit. As a percentage of revenues, in 2002 operating income was 10.4% in 2002 compared to 12.2% in 2001.

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In order to give an overall view of Latin America Operations (LAO), the following table sets forth, for the periods indicated, certain financial and other data for all the companies operating in South America, providing both wireline and mobile phone services.

South America	Year ended December 31, 2001(1)	Year ended December 31, 2002
	(millions of Euro, except percentages and employees)	
Gross operating revenues	2,937	2,706
Gross operating profit	882	724
% of gross operating revenues	30.0	26.8
Operating income	115	48
% of gross operating revenues	3.9	1.8
Number of employees at year-end	11,424	12,511

(1) The 2001 financial and other data have been reclassified and presented consistent with the 2002 presentation.

Internet and Media

The following table sets forth, for the periods indicated, certain financial and other data for the Internet and Media business unit (the SEAT group). As described above, due to the disposition of New SEAT following the demerger transaction completed in August 2003 this business unit has changed significantly and the discussion of 2002/2001 results will not be comparable to 2003. See Results of Operations for the Three Years Ended December 31, 2003 Results of Operations of Business Units for the Year Ended December 31, 2003 compared with the Year Ended December 31, 2002 Internet and Media .

Internet and Media	Year ended December 31, 2001(1)	Year ended December 31, 2002
	(millions of	

	Euro, except percentages and employees)	
Gross operating revenues	1,957	1,991
Gross operating profit	444	593
% of gross operating revenues	22.7	29.8
Operating income	31	232
% of gross operating revenues	1.6	11.7
Number of employees at year-end	9,264	7,715

(1) The 2001 financial and other data have been reclassified and presented consistent with the 2002 presentation.

Gross operating revenues increased by 1.7% from 1,957 million in 2001 to 1,991 million in 2002. The Directories business area made the largest contribution to growth with the related revenues increasing by 3.4%.

The contribution of the Internet and Media Business Unit to our consolidated operating revenues amounted to 1,880 million in 2001 and 1,900 million in 2002.

Gross operating profit increased by 33.6% to 593 million (with a gross margin of 29.8%), while operating income increased to 232 million in 2002 compared to 31 million in 2001. These improvements were achieved, despite the poor advertising market, due to implementation of rationalization measures and the improvements achieved in efficiency, especially in the Internet, Directories and Directory Assistance areas (which together represented 73% of combined revenues). In 2002, for the first time, all the business areas made a positive contribution to the consolidated Gross Operating Profit (with the sole exception of television, where reduced losses were recorded compared to 2001).

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Total Internet users grew from 5 million at the end of 2001 to 6.6 million at the end of 2002, of which 2.2 million remained active after 45 days. Average connection time increased by 5.6% in 2002 compared to 2001.

Information Technology Market

The following table sets forth, for the periods indicated, certain financial and other data for the IT Market Business Unit. In order to allow a better understanding of the results of the business managed by the business unit, the figures are presented on an historical and pro forma basis.

	Year ended December 31,			
Information Technology Market	**2001(1)**	**2001 Pro forma(2)**	**2002(1)**	**2002 Pro forma**
	(millions of Euro, except percentages and employees)			
Gross operating revenues	1,322	818	1,039	777
Gross operating profit	181	121	114	86
% of gross operating revenues	13.7	14.8	11.0	11.1
Operating income	133	85	64	37
% of gross operating revenues	10.1	10.4	6.2	4.8
Number of employees at year-end	7,454	5,374	5,506	5,031

(1) The 2002 and 2001 historical financial and other data are consistent with the 2003 scope of consolidation.
(2) The 2001 and 2002 pro forma financial and other data are consistent with the 2003 scope of consolidation.

Gross operating revenues decreased due to a contraction in the revenues of Finsiel, Banksiel and the Webegg Group, resulting from lower volumes, reduction in prices on some contracts which renewed during the year 2002 and lower contract prices on new bids won in 2002.

The contribution of the IT Market Business Unit to our consolidated operating revenues was 1,197 million in 2001 and 898 million in 2002 (historical).

Gross operating profit decreased due to the reduction in prices mentioned above, that were only partly offset by cost cuts and improved level of efficiency.

Information Technology Group

The following table sets forth, for the periods indicated, certain financial and other data for the IT Group Operating Activity.

Information Technology Group	Year ended December 31, 2001(1)	2002
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,039	996
Gross operating profit	198	98
% of gross operating revenues	19.1	9.8
Operating income (loss)	51	(40)
% of gross operating revenues	4.9	(4.0)
Number of employees at year-end	5,127	5,039

(1) The 2001 financial and other data have been reclassified and presented consistent with the 2002 presentation.

Gross operating revenues declined 4.1% from 2001 to 2002 and were mainly affected by a reduction in prices on the services rendered principally to the Wireline Business Unit, continuing with the price reduction policy of the previous year.

The contribution of the IT Group Operating Activity to our consolidated operating revenues was 120 million in 2001 and 59 million in 2002.

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Gross operating profit decreased by 50.5% from 198 million in 2001 to 98 million in 2002. Operating income decreased by 91 million from operating income of 51 million in 2001 to an operating loss of 40 million in 2002.

The decrease in profitability reflects the aforementioned reduction in prices as well as an increase in use of outside services and labor costs.

In 2002, operating loss was also impacted by higher levels of amortization of software licenses as a result of acquisitions made during the year.

Olivetti Tecnost Group

The following table sets forth, for the periods indicated, certain financial and other data for the Olivetti Tecnost group Business Unit.

	Year ended December 31,	
Olivetti Tecnost Group	**2001**	**2002**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	1,097	914
Gross operating profit	57	59
% of gross operating revenues	5.2	6.5
Operating income	4	4
% of gross operating revenues	0.4	0.4
Number of employees at year-end	4,896	4,527

Gross operating revenues were 914 million in 2002, including 340 million from the Office Products Division, 256 million from the Systems Division and 318 million from other divisions. Such revenues were distributed as follows: 588 million referred to hardware products, 154 million referred to accessories, 73 million referred to services and 99 million referred to other revenues. Gross operating revenues decreased by 16.7% (down 12.7% net of exchange rate effect) from 1,097 million in 2001 to 914 million in 2002. Such decrease was primarily attributable to the office products division where third-party revenues fell sharply (down 19%) and to a lesser extent to the vertical applications division where third-party revenues also fell (down 11.6%).

The contribution of the Olivetti Tecnost Business Unit to our consolidated operating revenues was 1,076 million in 2001 and 906 million in 2002.

Gross operating profit increased from 57 million in 2001 to 59 million in 2002 due to a reduction in operating costs (labor cost, materials and services).

In 2002 and in 2001 operating income remained stable at 4 million.

Other Telecom Italia Group Activities

Our Other Activities of 2002 and 2001 principally included the TILAB Operating Activity, the companies which previously reported to the former International Operations Business Unit and which, following the 2002 reorganization of international activities, were transferred to the Foreign Holdings Corporate Function, and by the companies/Corporate Functions that provide centralized services to the Telecom Italia Group (Business Units/Operating Activities/Companies). Our Other Activities also included the Satellite Business Unit which was disposed of during the 4th quarter of 2002.

Real Estate and General Services

Until December 31, 2002, the range of services offered by the Real Estate and General Services operating activity was directed mainly towards our other Corporate Functions/Business Units. The activities managed by Real Estate and General Services consisted of the following: to provide asset and property management services and to leverage the value of our real estate properties, to carry out the project design and work on properties and to provide project and facility management services.

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As a result of the finalization of the Tiglio Project (See Item 4. Information on the Telecom Italia Group Description of Property), in February 2003, the Real Estate and General Services operating activity was eliminated and the related activities and resources were transferred to the Telecom Italia Purchasing Corporate Function.

The following table sets forth, for the periods indicated, certain financial and other data for Real Estate and General Services.

Real Estate and General Services	Year ended December 31, 2001	2002
	(millions of Euro, except percentages and employees)	
Gross operating revenues	953	846
Gross operating profit	145	88
% of gross operating revenues	15.2	10.4
Operating loss	(65)	(92)
% of gross operating revenues	(6.8)	(10.9)
Number of employees at year-end	1,889	1,393

Gross operating revenues decreased by 107 million, or 11.2%, from 953 million in 2001 to 846 million in 2002. Such decrease was mainly due to the adjustment of internal charges to other Telecom Italia Group companies to match market rates and the rationalization of premises occupied by clients.

The contribution of the Real Estate and General Services to our consolidated operating revenues amounted to 50 million in 2001 and 32 million in 2002.

Gross operating profit decreased by 57 million, or 39.3%, from 145 million in 2001 to 88 million in 2002. Gross Operating Profit benefited from 51 million of costs savings arising from actions taken to contain operating costs (external charges and personnel costs) which partially offset the reduction in revenues.

Operating loss increased by 27 million, or 41.5%, from 65 million in 2001 to 92 million in 2002.

Satellite Services

The former Business Unit, Satellite Services (the Telespazio group), was disposed of during the 4th quarter of 2002 and consolidated in the statement of operations only for the first nine months of 2002. The Satellite Services (the Telespazio group and the Satellite Telecommunications business segment of Telecom Italia) was responsible for developing satellite communication systems for phone and data, radio and television broadcasting and earth-observation.

The following table sets forth, for the periods indicated, certain financial data for Satellite Services.

	Year ended December 31,	
Satellite Services	**2001(1)**	**2002(1)**
	(millions of Euro)	
Gross operating revenues	648	237
Gross operating profit	159	12
Operating income (loss)	60	(6)

(1) The 2002 financial data are related only to the first nine months, while the 2001 financial data refer to the entire year.

Liquidity and Capital Resources

Liquidity

The Telecom Italia Group s primary source of liquidity is cash generated from operations and its principal uses of funds are the payment of operating expenses, capital expenditures and investments, the servicing of debt, the payment of dividends to shareholders and strategic investments, such as international acquisitions.

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The table below summarizes, for the periods indicated, the Telecom Italia Group s cash flows.

	2001	2002	2003
	(millions of euro)		
Net cash provided by operating activities	8,719	9,815	9,921
Net cash provided by (used in) investing activities	(10,384)	840	(9,193)
Net cash provided by (used in) financing activities	2,606	(9,762)	(182)
Effect of exchange rate changes on cash and cash equivalents	(7)	(173)	(35)
Net increase in cash and cash equivalents	**934**	**720**	**511**
Cash and cash equivalents:			
Beginning of the year	**2,772**	**3,706**	**4,426**
End of the year	**3,706**	**4,426**	**4,937**

Net Cash Provided by Operating Activities. Net cash provided by operating activities was 9,921 million in 2003, 9,815 million in 2002 and 8,719 million in 2001.

2003 compared to 2002

The increase in 2003 compared to 2002 of 106 million was primarily due to:

- higher levels of net income before minority interest (2,428 million of income in 2003 compared to a loss of 306 million in 2002), an increase of 2,734 million;
- a decrease in change in deferred tax assets, net equal to 2,225 million (with a negative contribution of 611 million in 2003 compared to a negative contribution of 2,836 million in 2002); and
- 2,382 million attributable to the decrease in gains on disposal of fixed assets and other investments (from a gain of 2,243 million in 2002 to a loss of 139 million in 2003).

Such effects were largely offset by:

- the decrease in the levels of depreciation and amortization of 448 million (from 7,227 million in 2002 to 6,779 million in 2003);

- the lower levels of write-downs of fixed assets and other investments (from 4,387 million in 2002 to 1,188 million in 2003), a decrease of 3,199 million;
- a 16 million decrease in provision for employee termination indemnities (from 216 million in 2002 to 200 million in 2003) and 64 million for the increase in the payment of employee termination indemnities (from 187 million in 2002 to 251 million in 2003); and
- a 3,508 million decrease in the contribution of the change in operating assets and liabilities, which increased cash from operating activities by 3,557 million in 2002 and by only 294 million in 2003, mainly as a result of the provisions recorded in 2002 to the reserve for the put option on SEAT shares (1,942 million) and the reserve for risks and charges related to Aria Is Tim (850 million).

2002 compared to 2001

The increase in 2002 compared to 2001 of 1,096 million was primarily due to:

- significantly lower levels of net loss before minority interest (306 million loss in 2002 compared to a loss of 3,676 million in 2001) an improvement of 3,370 million;
- higher levels of write-downs of fixed assets and other investments of 634 million (from 3,753 million in 2001 to 4,387 million in 2002); and
- 1,695 million increase in the contribution of the change in operating assets and liabilities, which increased cash from operating activities by 1,862 million in 2001 and by 3,557 million in 2002, mainly as a result of the provisions recorded in 2001 and in 2002 to the reserve for the put option on SEAT shares of 569 million and 1,942 million, respectively.

Such effects were only partially offset by:

- the decrease in the levels of depreciation and amortization of 385 million (from 7,612 million in 2001 to 7,227 million in 2002);

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- an increase in change in deferred tax assets, net of 2,305 million (with a negative contribution of 2,836 million in 2002 compared to a negative contribution of 531 million in 2001); and
- a 1,870 million increase in gains on disposal of fixed assets and other investments (from a gain of 373 million in 2001 to a gain of 2,243 million in 2002); and
- a 8 million decrease in provision for employee termination indemnities (from 224 million in 2001 to 216 million in 2002) and 35 million for the increase in the payment of employee termination indemnities (from 152 million in 2001 to 187 million in 2002).

Net Cash Provided by (used in) Investing Activities. Net cash provided by (used in) investing activities was a net cash use of 9,193 million in 2003 compared to net cash provided of 840 million in 2002 and a net cash use of 10,384 million in 2001.

2003 compared to 2002

The net cash use of 9,193 million in 2003 compared to net cash provided of 840 million in 2002 was principally due to:

- capital expenditures that amounted to 4,894 million in 2003 (4,901 million in 2002); in 2003 they included 3,111 million of investments in fixed assets (3,291 million in 2002) and 1,783 million of additions to intangible assets (1,610 million in 2002);
- additions to other investments that decreased by 869 million from 1,563 million in 2002 to 694 million in 2003;
- a cash use of 5,274 million for the voluntary cash tender offers by Olivetti for a portion of the outstanding Old Telecom Italia ordinary shares and savings shares made in connection with the Merger;
- net change in marketable securities with a negative contribution of 1,497 million in 2003 compared to a positive contribution of 1,909 million in 2002;
- the increase in the proceeds from disposal of investments in consolidated subsidiaries, net of cash disposed of, by 2,964 million (from 33 million in 2002 compared to 2,997 million in 2003) mainly as a result of the disposal of New SEAT; and
- the decrease by 4,968 million in the proceeds from sale or redemption value of tangible and intangible assets, and other investments (from 5,736 million in 2002 to 768 million in 2003).

2002 compared to 2001

The net cash provided of 840 million in 2002 compared to net cash use of 10,384 million in 2001 was principally due to:

- capital expenditures that decreased by 2,330 million in 2002 (from 7,231 million in 2001 to 4,901 million in 2002); in 2002 they included 3,291 million of investments in fixed assets (4,317 million in 2001) and 1,610 million of additions to intangible assets (2,914 million in 2001);

- additions to other investments that decreased by 1,800 million from 3,363 million in 2001 to 1,563 million in 2002;

- net change in marketable securities with a positive contribution of 1,909 million in 2002 compared to a negative contribution of 361 million in 2001; and

- the increase in 2002 by 4,252 million in the proceeds from sale or redemption value of tangible and intangible assets, and other investments (from 1,484 million in 2001 to 5,736 million in 2002).

Net Cash Provided by (Used in) Financing Activities. Net cash provided by (used in) financing activities was a net cash use of 182 million in 2003 compared to net cash use of 9,762 million in 2002 and net cash provided of 2,606 million in 2001.

Net cash used in financing activities in 2003 reflected mainly the following:

- an increase in short-term debt of 3,786 million, from 6,827 million at December 31, 2002 (including current portion of long-term debt of 3,450 million) to 10,613 million (including current portion of long-term debt of 9,289 million) at December 31, 2003;

- a decrease of 2,952 million in long-term debt, from 33,804 million at December 31, 2002 to 30,852 million at December 31, 2003, since the issue of new notes for the total principal amount of 6,568 million was more than offset by the increase of 5,839 million in the current portion of long-term debt and the repayments of medium-long term debt; and

- the 2003 payment of dividends on income and reserves of 1,049 million.

Linked to the gross debt change there was an increase in cash and cash equivalents, marketable securities and financial receivables under current assets mainly due to the proceeds arising from the issue of new bonds, the repayments of medium-long term debt maturing by the end of 2003 and the cash of 1,485 million used to partially finance the cash tender offers by Olivetti for a portion of the outstanding Old Telecom Italia shares.

As of December 31, 2003, cash and cash equivalents, marketable securities and financial receivables under current assets were 8,482 million (7,348 million as of December 31, 2002).

Net cash used in financing activities in 2002 reflected mainly the following:

- a decrease in short-term debt of 2,245 million, from 9,072 million at December 31, 2001 (including current portion of long-term debt of 1,939 million) to 6,827 million (including current portion of long-term debt of 3,450 million) at December 31, 2002;

- a decrease of 3,943 million in long-term debt, from 37,747 million at December 31, 2001 to 33,804 million at December 31, 2002; and

- the 2002 payment of dividends of 3,668 million.

Net cash provided by financing activities in 2001 consisted of the followings:

- a decrease in short-term debt of 7,855 million, from 16,927 million at December 31, 2000 (including current portion of long-term debt of 2,750 million) to 9,072 million (including current portion of long-term debt of 1,939 million) at December 31, 2001;

- an increase of 10,262 million in long-term debt, from 27,485 million at December 31, 2000 to 37,747 million at December 31, 2001;

- paid in capital in consolidated subsidiaries of 2,660 million; and

- the 2001 payment of dividends of 2,461 million.

Capital Resources

Gross Financial Debt

On a consolidated basis, at December 31, 2003, our outstanding long-term debt was 30,852 million (33,804 million at December 31, 2002) and our short-term debt was 10,613 million (including current portion of long-term debt of 9,289 million) compared to 6,827 million at December 31, 2002 (including current portion of long-term debt of 3,450 million). At December 31, 2003, short-term debt included 1,500 million of Telecom Italia s floating rate notes maturing June 21, 2005 which were repaid early on March 22, 2004. Interest on our gross financial debt totaled 2,173 million in 2003 compared with 2,241 million in 2002.

In 2003, the increase of 834 million in gross financial debt (from 40,631 million at December 31, 2002 to 41,465 million at December 31, 2003) was more than offset by the increase of 1,134 million in cash and cash equivalents, marketable securities and financial receivables under current assets (from 7,348 million at December 31, 2002 to 8,482 million at December 31, 2003) that principally arose from the difference between the proceeds on new notes issued in 2003 and the repayments of medium and long-term debt falling due during 2003, in addition to cash resources used to partially pay the tender offers (1,485 million).

As of December 31, 2003, approximately 86% of our long-term debt was denominated in Euro, while the remainder was primarily denominated in U.S. Dollars, Pound Sterling, Brazilian Reais, Japanese Yen and Chilean Peso.

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The following table sets out the currency of our gross financial debt:

	As of December 31,							
	2003						2002	
(millions of euro)	**Euro**	**%**	**Foreign currency**	**%**	**Total**	**%**	**Total**	**%**
Medium/long-term debt	26,393	72	4,459	90	30,852	74	33,804	83
Short-term debt	10,137	28	476	10	10,613	26	6,827	17
Total gross financial debt	**36,530**	**100**	**4,935**	**100**	**41,465**	**100**	**40,631**	**100**

In 2003, the share of our long-term debt (excluding current portion) as a percentage of total gross financial debt decreased from 83% to 74%. At December 31, 2003, approximately 35% of the long-term debt carried a floating rate.

Long term debt includes notes we have issued in order to reduce our dependence on short-term debt, extend the average life of our financial debt and expand our investor base. To this effect, we issued long-term debt in the capital markets under, among others, the Telecom Italia Euro Medium Term Note Program, the Olivetti EMTN Program and the Old Telecom Italia Global Note Program, the net proceeds of which have been used to repay short-term debt.

As of December 31, 2003, notes and bonds outstanding amounted to 37,365 million (31,805 million at December 31, 2002) and increased by 5,560 million (net of reimbursements and other causes), mainly as a result of the following:

- issue, in January 2003, of fixed-rate notes by Olivetti Finance N.V., under the Euro Medium Term Note (EMTN), in the principal amount of 3,400 million divided into three tranches:
  - notes 2003-2008 issued by Olivetti Finance N.V. in the principal amount of 1,750 million with an annual fixed-rate coupon of 5.875%, maturing in January 2008;
  - notes 2003-2013 issued by Olivetti Finance N.V. in the principal amount of 850 million with an annual fixed-rate coupon of 6.875%, maturing in January 2013;
  - notes 2003-2033 issued by Olivetti Finance N.V. in the principal amount of 800 million with an annual fixed-rate coupon of 7.75%, maturing in January 2033;
- issue, in October 2003, of fixed-rate notes by Telecom Italia Capital S.A., fully and unconditionally guaranteed by Telecom Italia, in the principal amount of U.S.$4,000 million (3,168 million). The issue was divided into three tranches:

- Series A notes in the principal amount of U.S.$1,000 million (792 million) with an annual fixed-rate coupon of 4%, maturing in November 2008;
- Series B notes in the principal amount of U.S.$2,000 million (1,584 million) with an annual fixed-rate coupon of 5.25%, maturing November 2013;
- Series C notes in the principal amount of U.S.$1,000 million (792 million) with an annual fixed-rate coupon of 6.375%, maturing in November 2033.

The issuance of these notes allowed us to complete the repayment of the loan in November 2003 used to fund the tender offers (see below Bank Facilities Term Loan Facility).

Furthermore, on January 29, 2004, Telecom Italia issued 1,000 million principal amount of floating rate notes due October 29, 2007 (Euribor 3 months + 0.33%; issue price 99.927), 750 million principal amount of 4.5% notes due January 28, 2011 (issue price 99.56) and 1,250 million principal amount of 5.375% notes due January 29, 2019 (issue price 99.07). This issue was part of Telecom Italia s 10 billion Euro MTN Program authorized by the Board of Directors of Telecom Italia S.p.A. on October 10, 2003. The notes under this program can be issued by Telecom Italia and/or its subsidiary Telecom Italia Finance, with a guarantee by Telecom Italia.

On April 8, 2004, Telecom Italia issued, at par, 110 million principal amount of Floating Rate Notes due 2009 under the Euro MTN Program. Such notes were subscribed in full, by way of a private placement, by one investor.

Our debt due to banks was 2,460 million at December 31, 2003 (5,776 million at December 31, 2002), of which 1,278 million (3,926 million at December 31, 2002) of short-term debt, including the current portion of long-term debt.

As of December 31, 2003, the amount of unutilized bank lines of credit of Telecom Italia Group was 9,110 million (9,081 million as of December 31, 2002), of which 6,500 million related to the Revolving Credit

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Facility (see below Bank Facilities Revolving Facility). Approximately 98% of our lines of credit were denominated in Euro and had varying interest rates. Of the total amount, 6,153 million were Telecom Italia S.p.A. unutilized bank lines of credit (5,813 million as of December 31, 2002).

Off-Balance Sheet Arrangements

Off-balance sheet arrangements refer to any transaction, agreement, or other contractual arrangement involving an unconsolidated entity (other than contingent liabilities arising from litigation, arbitration or regulatory actions), under which Telecom Italia has:

- Guarantee contracts required to be initially recorded at fair value under FASB Interpretation No. 45, *Guarantor s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* (FIN 45);
- retained or contingent interests in transferred assets;
- any obligation under derivative instruments classified as equity; or
- any obligation arising out of a material variable interest in an unconsolidated entity that provides financing, liquidity, market risk or credit risk support to the company, or that engages in leasing, hedging, or research and development arrangements with the company.

As of December 31, 2003, Telecom Italia has the following items that are considered to be off-balance sheet.

As of December 31, 2003, the Telecom Italia Group had a purchase commitment of 72 million for the purchase of buildings leased from Fintecna (which was exercised on April 1, 2004), and Telecom Italia International s commitment of 32 million in order to cover, on a proportional basis through capital increases, the residual amount due by Etec S.A. to the Cuban government in connection with the new license acquired.

As of December 31, 2003, the Telecom Italia Group has given guarantees of 1,631 million, mainly consisting of sureties provided by Telecom Italia and TIM on behalf of affiliated companies. The most significant of these relate to the indebtedness of Aria-Is Tim that is guaranteed by TIM for 672 million. Remaining guarantees consist of medium/long-term loan transactions and guarantees for bids to acquire TLC licenses abroad.

Telecom Italia has also issued support letters totaling 197 million on behalf of affiliated companies to guarantee insurance policies, lines of credit arrangements and overdraft agreements with financial institutions.

Telecom Italia also has a purchase commitment, at fair value, to acquire the outstanding minority interest of the consolidated subsidiaries Mediterranean Nautilus Ltd and Med-1 Submarine Cables Ltd.

See also Note 18 of Notes to the Consolidated Financial Statements included elsewhere herein for a further discussion of commitments and contingencies.

Contractual Obligations and Commitments

In accordance with the requirements of Form 20-F we present our contractual obligations and other commitments in the table that follows. However, our future cash flow prospects cannot solely be assessed on the basis of such obligations.

The following table aggregates our contractual obligations and commitments with definitive payment terms which will require significant cash outlays in the future. As of December 31, 2003, the amounts payable are as follows:

	Year Ended December 31,						
	2004	**2005**	**2006**	**2007**	**2008**	**After 2008**	**Total**
	(millions of Euro)						
Notes and bonds	8,445	1,510	6,073	3,105	2,550	15,682	37,365
Loans and other debt	817	476	406	421	77	424	2,621
Finance lease	27	22	18	19	14	55	155
Total long-term debt	9,289	2,008	6,497	3,545	2,641	16,161	40,141
Operating lease	8	6	4	2			20
Rental obligations to IM.SER60, TIGLIO I, TIGLIO II, FMP Italy 1 (formerly Ireos)(1)	229	229	229	229	229	2,844	3,989
Total contractual obligations and commitments	**9,526**	**2,243**	**6,730**	**3,776**	**2,870**	**19,005**	**44,150**

(1) Aggregate contractual rental payments due between 9 and 21 years.

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The table above does not include short-term financial debt of 1,324 million (excluding current portion of long-term debt) outstanding at December 31, 2003.

Total long-term debt of 9,289 million, 14,691 million and 16,161 million is scheduled to become due for repayment during 2004, in the years 2005-2008 and beyond, respectively.

See also Note 18 of Notes to Consolidated Financial Statements for a description of derivatives.

For a discussion of our capital expenditures in 2001, 2002 and 2003 and the Telecom Italia Group s proposed capital expenditure commitments over the next three years, see Capital Expenditures .

Net Financial Debt

On a consolidated basis, at December 31, 2003, net financial debt was 33,346 million compared to 33,399 million at the end of 2002 (a decrease of 53 million). Net financial debt is a non-GAAP financial measure as defined in Item 10 of Regulation S-K under the 1934 Act. Although net financial debt is a non-GAAP measure, it is widely used in Italy by financial institutions to assess liquidity and adequacy of a company s financial structure. Therefore, we believe it is useful information for investors to receive and is consistent with how we present ourselves to the analyst community. Net financial debt at December 31, 2003 includes borrowings to finance the effects of the withdrawals and the tender offers (5,285 million) relating to the Merger, the distribution of profits and reserves (1,049 million) in payment of the dividend on Old Telecom Italia shares and the payment for the early exercise of the JP Morgan Chase put option on Seat Pagine Gialle shares (2,272 million). Such requirements were mostly financed by cash generated by operations, the sale of the investment in New SEAT (3,681 million) and the disposal of other investments (768 million).

The following chart summarizes the major components which had an impact on the change in net financial debt during 2003 (in millions of euro):

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(1) For a more detailed description, see Item 4. Information on the Telecom Italia Group Business Significant Developments during 2003 Sale of Telecom Italia s stake in New SEAT .

Furthermore, securitization and factoring arrangements led to an improvement in consolidated net financial debt as of December 31, 2003 of 1,201 million (1,046 million as of December 31, 2002), of which 851 million (826 million as of December 31, 2002) was due to the securitization program.

In particular:

- during 2003 and 2002, Telecom Italia continued a program (the Program) that began in 2001 for the securitization of receivables generated by the services rendered to the customers of the Wireline

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business unit and the customers of Path.Net (a wholly-owned subsidiary of Telecom Italia, which provides telephone services to the Public Administration). A first tranche of 700 million of notes was issued by a non-consolidated special purpose vehicle for the Program incorporated pursuant to the Italian securitization law (Law No. 130/1999). The Program allows for the possibility of successive issues of notes, all with the same rights and risk profile, up to a total maximum amount of 2 billion.

The total amount of the trade accounts receivable sold under the securitization transactions in 2003 was 8.9 billion (9 billion in 2002), solely referred to receivables from residential customers generated by Telecom Italia;

- in 2003, Telecom Italia, TIM and Olivetti Tecnost sold trade accounts receivable under non-recourse factoring arrangements in the amount of 3,873 million. In 2002, the Telecom Italia Group sold trade accounts receivable under non-recourse factoring arrangements in the amount of 3,969 million.

Compared to September 2001, the date on which new management took over responsibility for the running of the Telecom Italia Group, net financial debt has decreased by approximately 10 billion as showed in the following table:

The overall reduction is attributable to the following: cash flows generated by operations, proceeds from disposal of tangible assets, investments in consolidated subsidiaries and associated companies and other investing activities for 10 billion and distributions to shareholders (dividends, withdrawals and the tender offers on Old Telecom Italia shares) of 10 billion.

The reduction had no impact on investments and in particular capital expenditures. In fact, the commitment to investments continued in 2003 with total investments of approximately 12 billion that were financed by cash flows provided by operations and which contributed to strengthening our competitiveness.

Our strategic objectives for the three-year period 2004 2006 confirmed that the target is to reduce net financial debt below 30 billion by the end of 2004.

In order to better understand the change in net financial debt, the following table presents details of the changes in our net financial debt between December 31, 2002 and December 31, 2003, taking into account the JP Morgan Chase put option:

	As of December 31,		
(millions of euro)	**2003**	**2002**	**Change**
Old Telecom Italia Group	30,238	18,118	(3,161)
Olivetti Group		15,281	
Effects of withdrawals and tender offers	5,285		5,285
Sale of New SEAT and other disposals	(4,449)		(4,449)

JP Morgan Chase put option	2,272		2,272
Net financial debt as reported in the financial statements	**33,346**	**33,399**	**(53)**
JP Morgan Chase put option		2,417	(2,417)
TOTAL	**33,346**	**35,816**	**(2,470)**

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A reconciliation of net financial debt with the financial statement line items is presented in the table below.

(millions of euro)	As of December 31, 2003 Maturing within 12 months	2003 Maturing Beyond 12 months	2003 Total	2002 Total
Notes and bonds	6,730	23,323	30,053	24,404
Convertible notes	1,715	5,597	7,312	7,401
Total notes and bonds	**8,445**	**28,920**	**37,365**	**31,805**
Debt to banks	1,278	1,182	2,460	5,776
Debt to other financial institutions	342	670	1,012	1,970
Payables to associated companies	19	23	42	406
Note payables				241
Suppliers	5	4	9	21
Other	524	53	577	412
Total other financial payables	**2,168**	**1,932**	**4,100**	**8,826**
Total gross financial debt	**10,613**	**30,852**	**41,465**	**40,631**
Cash and cash equivalents:				
Bank and postal accounts	(4,870)		(4,870)	(4,363)
Cash and valuables on hand	(7)		(7)	(7)
Receivables for securities held under reverse repurchase agreements	(60)		(60)	(56)
Marketable securities (*)	(2,719)		(2,719)	(1,927)
Financial accounts receivable (included under Receivables and Other current assets)	(826)		(826)	(995)
Total cash and cash equivalents, marketable securities and financial receivables under current assets	**(8,482)**		**(8,482)**	**(7,348)**
Financial prepaid expense/deferred income, net and accrued financial income/expense, net	**670**	**(307)**	**363**	**116**
Net financial debt	**2,801**	**30,545**	**33,346**	**33,399**

(*) As of December 31, 2003, marketable securities include: Euro commercial paper (735 million), own notes (1,341 million), notes and bonds (583 million) and other securities (60 million). As of December 31, 2002 marketable securities include Old Telecom Italia shares held by Olivetti (299 million).

At December 31, 2003, we had cash and cash equivalents, marketable debt securities and financial accounts receivable in excess of 8,482 million (7,348 million at December 31, 2002). We believe that these financial assets together with our bank facilities, as well as the proceeds that arose from the issuance of notes in January 2004, mentioned above, and the disposal of Telekom Austria (770 million) in January 2004 will make it possible to meet our debt obligations maturing in 2004 and 2005, detailed below.

	Financial debt maturing in 2004 and 2005		
(millions of euro)	**Notes and Bonds**	**Loans, other debt and finance lease**	**Total**
Year 2004	8,445	844	9,289
Year 2005	1,510	498	2,008
Total	**9,955**	**1,342**	**11,297**

Notes and bonds

In July 1999, the Telecom Italia Group (formerly the Olivetti Group) established the Olivetti EMTN Program, as updated and amended on June 8, 2001 and May 14, 2002, which allowed for the issuance of a total amount of 15 billion in debt (or the equivalent in other currencies), at various terms, rates and maturities.

At the end of 2000, the Old Telecom Italia Group established a Global Medium Term Note Program, which allowed for the issuance of a total amount of U.S.$10 billion in debt (or the equivalent in other currencies), at various terms, rates and maturities. On December 18, 2001, the Old Telecom Italia s Board of Directors authorized the increase of the Global Medium Term Note Program to up to U.S.$12 billion (or the equivalent in other currencies).

On October 10, 2003, as part of the plan to refinance short and long-term borrowings falling due, the board of directors of Telecom Italia authorized the creation of the Euro MTN Program up to a maximum amount of 10 billion. These notes can be issued by Telecom Italia and/or its subsidiary Telecom Italia Finance, with a guarantee by Telecom Italia.

As of December 31, 2003, total notes and bonds amounted to 37,365 million (31,805 million at December 31, 2002) and consisted of the followings:

- convertible notes of 7,312 million (7,401 million at December 31, 2002), detailed as follows:

Original Currency	Amount (million)	Coupon	Convertible into shares of	Issue date	Maturity date	Issue price (%)
Convertible notes issued by Telecom Italia S.p.A.						
Euro	1,331(1)	1.50%	TI S.p.A.	03/09/01	01/01/04	100
Euro	2,829	1.50%	TI S.p.A.	11/23/01	01/01/10	100
Convertible notes issued by Telecom Italia Finance S.A. guaranteed by Telecom Italia S.p.A.						
Euro	1,964	1.00%	TIM/Telecom Italia Media	03/15/01	03/15/06	100
Convertible notes issued by Olivetti Finance N.V. guaranteed by Telecom Italia S.p.A.						
Euro	385(2)	0.00%	TI S.p.A.	09/20/02	03/19/04	100
Euro	803	1.00%	TI S.p.A.	11/03/00	11/03/05	100
Total	**7,312**					

(1) These notes were repaid on January 1, 2004, their maturity date.
(2) On March 19, 2004, Olivetti Finance N.V., S.A. redeemed 385 million in principal amount of notes on their maturity date.

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For a more detailed description of these convertible notes see Note 11 of Notes to the Consolidated Financial Statements included elsewhere herein;

- notes and bonds of 30,053 million (24,404 million at December 31, 2002), detailed as follows:

Original Currency	Amount in original currency (million)	Amount in Euro (million)	Coupon	Issue date	Maturity date	Issue price (%)
Notes and bonds issued by Telecom Italia S.p.A.						
Euro	1,500(1)	1,500	Euribor 3 months + 0.95%	12/21/01	06/21/05	99.837
Euro	1,250	1,250	5.625%	02/01/02	02/01/07	99.841
Euro	1,250	1,250	6.250%	02/01/02	02/01/12	98.952
Euro	215	215	Euribor 6 months	01/01/02	01/01/22	100
Sub Total		**4,215**				
Notes and bonds issued by Telecom Italia Finance S.A. and guaranteed by Telecom Italia S.p.A.						
Euro	1,000(2)	1,000	Euribor 3 months + 1.125%(a)	04/20/01	04/20/04	99.514
Euro	3,000(2)	3,000	6.125%(a)	04/20/01	04/20/06	99.937
Euro	1,500	1,500	5.15%(b)	02/09/99	02/09/09	99.633
Euro	2,000(2)	2,000	7.00%(a)	04/20/01	04/20/11	99.214
CHF	100	64	5.625%	06/12/86	06/12/46	99.000
Sub Total		**7,564**				
Notes and bonds issued by Olivetti Finance N.V. and guaranteed by Telecom Italia S.p.A.						
Euro	4,200	4,200	5.825%	07/30/99	07/30/04	99.786
Euro	200	200	EONIA + 1.45%	08/07/02	02/07/05	99.900
Euro	500	500	Euribor 3 months + 1.3%	03/14/02	03/14/05	100
Euro	1,100	1,100	Euribor 3 months + 1.25%	05/29/02	01/03/06	99.6673
Euro	1,750	1,750	6.500%	04/24/02	04/24/07	99.637
Euro	1,750	1,750	5.875%	01/24/03	01/24/08	99.937
Euro	2,350	2,350	6.575%(c)	07/30/99	07/30/09	99.272
Euro	1,000	1,000	7.25%	04/24/02	04/24/12	99.602
Euro	850	850	6.875%	01/24/03	01/24/13	99.332
JPY	20,000	148	3.550%	04/22/02	05/14/32	99.25
Euro	250	250	7.770%	08/09/02	08/09/32	100.2
Euro	800	800	7.750%	01/24/03	01/24/33	99.239
Sub-Total		**14,898**				
Notes and bonds issued by Telecom Italia Capital S.A. and guaranteed by Telecom Italia S.p.A.						
USD	1,000	792	4.000%	10/29/03	11/15/08	99.953
USD	2,000	1,584	5.250%	10/29/03	11/15/13	99.742
USD	1,000	792	6.375%	10/29/03	11/15/33	99.558
Sub-Total		**3,168**				
Notes and bonds issued by Entel Chile						
CLP	156,820	208	From 5.93 % to 8.06 %			

		From 2000 to 2002	From 2004 to 2023
Sub-Total	**208**		
Total	**30,053**		

Note (a), (b) and (c): see the next paragraph Ratings Triggers

(1) These notes were repaid in advance, at par, on March 22, 2004, in accordance with a resolution approved by the Telecom Italia Board of Directors on February 17, 2004.

(2) On April 20, 2004, the first tranche of 1,000 million was paid. On the same date, the 0.25% step-up took effect on the annual coupon for the remaining two tranches: 3,000 million (6.125% + 0.25%), maturing April 2006; 2,000 million (7% + 0.25%), maturing April 2011.

For a more detailed description of the notes and bonds summarized in the table above see Note 11 of Notes to the Consolidated Financial Statements included elsewhere herein.

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Ratings Triggers

Certain of the notes and bonds we have issued provide certain protections to investors in the event that our debt ratings are downgraded.

The ratings assigned to Telecom Italia by the various agencies are the following:

Standard & Poor s:	BBB+	positive outlook
Moody s:	Baa2	stable outlook
Fitch IBCA:	A-	stable outlook

A securities rating is not a recommendation to buy, sell or hold securities. Ratings may be subject to revision or withdrawal at any time by the assigning rating organization. Each rating should be evaluated independently of any other rating.

(a) Telecom Italia Finance S.A. Notes:

- 1,000 million, Euribor 3M + 1.125% interest, maturing April 2004
- 3,000 million, 6.125% interest, maturing April 2006
- 2,000 million, 7% interest, maturing April 2011

These notes carry protection for investors which would be triggered by a change in the rating assigned to Telecom Italia to below the Baa1/BBB+ ratings (by Moody s and S&P s, respectively): each reduction in the rating by one notch by either of the two agencies to below the stated thresholds would cause an increase in the interest coupon (or in the spread above the Euribor in the case of floating-rate securities) of 0.25%, starting from the interest payment date subsequent to the downgrade in the rating.

Any change in the rating is evaluated at the end of each interest period and, on the basis of the then applicable rating, the interest for the next coupon is fixed; therefore, changes in the ratings during the interest period would have no impact on the determination of the coupon except for the applicable ratings immediately prior to the beginning of the new interest period.

Therefore, the step-up/down will only be applied when the rating at the end of a coupon period is different from the rating at the end of the preceding coupon period.

As a result, these securities are currently subject to an 0.25% increase in interest due to the assignment of a Baa2 rating by Moody s in August 2003. In the case of the floating-rate security, this increase was applied to the coupon for the period beginning October 2003; in the case of the two fixed-rate securities, the increase has been applied beginning with the interest period which started in April 2004.

(b) Telecom Italia Finance S.A. Notes: 1,500 million, 5.15% interest, maturing February 2009.

These notes carry protection for investors which would be triggered by a downgrade in the minimum rating (among those assigned by the various agencies, specifically in reference to the Baa2 rating by Moody s).

At the beginning of every coupon period, this minimum rating is checked, and depending upon the rating, the interest coupon will be fixed; once fixed, changes in the minimum rating during the interest period will have no effect on the coupon to be paid, and will only have an impact when the next coupon interest rate is fixed (if the changes are still in effect).

Starting from the initial level of the interest coupon at issue (5%), a 0.15% increase in interest was granted to investors to the maturity date, bringing the current coupon interest rate to 5.15%.

This current coupon can be further increased in relation to the level of the minimum rating:

- if, at the time the interest coupon is fixed, the minimum rating is Ba1/BB+ or less, 1.50% will be added to the original coupon;
- if, at the time the interest coupon is fixed, the minimum rating is Baa3/BBB-, 0.5% will be added to the original coupon;
- higher levels of minimum ratings do not involve increases in the current coupon.

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Therefore, only future downgrades in the minimum rating could cause an increase in the current coupon; this coupon cannot be reduced because of upgrades in the ratings.

(c) Olivetti Finance N.V. Notes: 2,350 million, 6.575% interest, maturing July 2009.

These notes carry protection for investors which would be triggered by a change in the minimum rating (among those assigned by the various agencies, specifically the Baa2 rating by Moody s).

At the beginning of each interest period, this minimum rating is checked, and depending upon the rating, the interest coupon will be fixed; once fixed, changes in the minimum rating during the interest period will have no effect on the coupon to be paid, and will only have an impact when the next coupon interest rate is fixed (if the changes are still in effect).

Starting from the initial level of interest at issue (6.125%), the coupon that will effectively be paid will be increased in relation to the level of the minimum rating:

- if, at the time the interest coupon is fixed, the minimum rating is Ba1/BB+ or less, 1.95% will be added to the original coupon;
- if, at the time the interest coupon is fixed, the minimum rating is Baa3/BBB-, 0.95% will be added to the original coupon;
- if, at the time the interest coupon is fixed, the minimum rating is Baa2/BBB, 0.45% will be added to the original coupon;
- higher levels of minimum ratings do not involve increases in the original coupon.

In line with this mechanism, starting October 2000 (date of the introduction of this mechanism), the original coupon was increased by 0.45% (reaching the current 6.575%).

Future upgrades/downgrades in the minimum rating might cause decreases/increases in the coupons according to the mechanism described above.

Financial covenants / other covenants / other features

The notes and bonds summarized above contain customary covenants and events of default but do not contain financial covenants or covenants which would force the notes to be repaid at an earlier date as a result of events other than the insolvency of the Telecom Italia Group. However, certain of the Olivetti Group notes and bonds contain cross defaults to subsidiary indebtedness.

For example, there are no clauses which would cause the notes to be repaid due to a downgrade in the ratings to below the established thresholds.

The guarantees provided by Telecom Italia S.p.A. on notes issued by foreign subsidiaries are all full and unconditional.

None of the notes summarized above carry any other interest rate structures or structural complexities.

Since these transactions have principally been placed with institutional investors on major world capital markets (the Euro market and the U.S.A.), the terms which regulate the notes are in line with the market practice for similar transactions effected on the same markets.

For the U.S.$4,000 million principal amount of Notes issued by Telecom Italia Capital S.A. in October 2003, guaranteed by Telecom Italia, there is a covenant requiring that Telecom Italia Capital and Telecom Italia complete an exchange offer registered with the SEC in order to allow investors to exchange their notes originally purchased for registered notes which will be freely saleable without restrictions. Should Telecom Italia Capital not complete the registered exchange offer by October 31, 2004, this would result in an increase in the coupon by 0.50% until the exchange offer was completed.

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Bank Facilities

In connection with the Merger, Telecom Italia (formerly Olivetti) mandated a group of Mandated Lead Arrangers to arrange and underwrite 15.5 billion of senior credit facilities (the Facilities). The Facilities, which were subsequently fully syndicated, consisted of:

- a 9.0 billion senior term loan (the Term Loan Facility) to fund both the cash out payment to dissenting Olivetti shareholders and the cash consideration payable upon completion of Olivetti s voluntary partial cash tender offers for Old Telecom Italia Shares and Savings Shares, and

- a 6.5 billion senior revolving credit facility (the Revolving Credit Facility) to fund the needs for working capital and general corporate purposes of Old Telecom Italia and, following the Merger, of the new merged entity, and the refinancing of Old Telecom Italia s existing 7.5 billion facility.

Details of the facilities were as follows:

Term Loan Facility

On April 24, 2003, Telecom Italia (formerly Olivetti) entered into the 9 billion Term Loan Facility with Banca Intesa S.p.A., Barclays Capital, BNP Paribas, HSBC Bank plc, J.P.Morgan plc, The Royal Bank of Scotland plc, Unicredit Banca Mobiliare S.p.A. (as mandated lead arrangers), and J.P.Morgan Europe Limited (as agent).

Pursuant to the Term Loan Facility, up to 9 billion was available to finance:

(i) the cash-out payment to Olivetti shareholders who exercised their withdrawal right; and, for the amounts not used to finance the cash-out payment, and

(ii) the partial voluntary cash tender offers made by Olivetti for a portion of the Old Telecom Italia shares and savings shares.

The Term Loan Facility was divided into the following three tranches aggregating 9 billion.

	Amount (millions of euro)	Tenor	Term out
Tranche A	3,600	364 days	6 months
Tranche B	3,600	18 months(1)	6 months

Tranche C	1,800	2 years	12 months

(1) Less one day.

5,274 million of the Term Loan Facility was utilized in connection with the Merger. 1,474 million of this amount was repaid in August with the liquidity available, while the residual amount (3,800 million) was repaid in advance, as follows:

- 2,000 million in October 2003 (the due date was October 2004); and
- 1,800 million in November 2003 (the due date was April 2005), following the issuance of notes by Telecom Italia Capital in the principal amount of U.S.$4 billion on October 29, 2003.

Revolving Facility

On April 24, 2003, Telecom Italia (formerly Olivetti) received a binding offer from Banca Intesa S.p.A., Barclays Capital, BNP Paribas, HSBC Bank plc, J.P.Morgan plc, The Royal Bank of Scotland plc, Unicredit Banca Mobiliare S.p.A. (as mandated lead arrangers), and J.P.Morgan Europe Limited (as agent) to enter into the 6.5 billion multicurrency Revolving Credit Facility with:

- Telecom Italia and Telecom Italia Finance Société Anonyme (with the guarantee of Telecom Italia) if the Merger would have been effective prior to August 8, 2003; or
- Old Telecom Italia and Telecom Italia Finance Société Anonyme (with the guarantee of Old Telecom Italia) if the Merger would have not been effective prior to August 8, 2003.

The Revolving Credit Facility was divided into the following two tranches aggregating 6.5 billion.

	Amount (millions of euro)	Tenor	Term out
Tranche D	4,500	364 days	12 months
Tranche E	2,000	3 years	None

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Under the terms and conditions of the Revolving Credit Facility the borrower or borrowers (as defined therein) were entitled to use funds available for the short-term financial requirements of the Telecom Italia Group, including repayments of commercial paper issued by any member of the Telecom Italia Group, to refinance existing debt and for the general corporate purposes of the Telecom Italia Group.

On March 30, 2004, the Tranche D (4,500 million), maturing on April 2004, and the Tranche E (2,000 million), maturing on April 2006, were replaced by a new facility (the New Facility) of 6.5 billion with a three year maturity. The New Facility does not contain any financial covenants and does not place any constraints on how we operate our business.

The agreement includes customary representations and warranties and events of default for a revolving credit agreement of this type. However, according to the terms of the agreement, the Telecom Italia Group is not required to represent that there has been no material adverse change in the business or financial condition of the Telecom Italia Group at the time of any drawdown.

Debt to Equity Ratio

The Telecom Italia Group s debt to equity ratio, calculated as the ratio of consolidated net financial debt to total stockholders equity (including minority interest), was 162.0% and 161.9% as of December 31, 2003 and December 31, 2002 , respectively.

Centralized Treasury. Telecom Italia has a centralized treasury that provides financial assistance to the Telecom Italia Group including TIM, and generally operates as the Telecom Italia Group s principal banker, allocating cash where needed and collecting the liquid resources of the members of the Telecom Italia Group. As a result, Telecom Italia is able to ensure that its subsidiaries have adequate liquidity to satisfy their requirements. Telecom Italia also acts on behalf of its subsidiaries in negotiating bank lines of credit and provides financial consultancy services to its subsidiaries.

The central treasury function reduces the need of the members of the Telecom Italia Group to utilize banks, enables members of the Telecom Italia Group to obtain more favorable terms from banks when needed and enables Telecom Italia to maintain control over cash flows and to assure better utilization of surplus liquidity.

Cash Management. Telecom Italia utilizes short-term credit lines to support expenses and disbursements that occur in the ordinary course of business, using free cash flow generated by its business to fund capital expenditures and acquisitions and to repay long-term debt.

Lines of Credit. Short-term lines of credit granted to the Telecom Italia Group by banks, according to standard money market terms and conditions, consist partly of lines of credit with specified maturities and partly of lines of credit callable upon notice. All of the Company s medium and long-term lines of credit relate to specific loans drawn down to fund the Company s activities.

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Capital Expenditures

The table below sets forth, for the periods indicated, our total capital expenditures based on the organization by Business Unit at December 31, 2003.

	Year ended December 31,		
	2001	2002	2003
	(millions of Euro)		
Fixed assets:			
Wireline(1)	1,979	1,837	1,497
Mobile	1,530	1,075	1,244
South America(2)	351	201	116
Internet and Media	82	28	32
IT Market(1)	20	13	13
IT Group(1)	84	83	106
Olivetti Tecnost	42	26	14
Other activities(1)(3)	229	28	89
Total fixed assets(4)	4,317	3,291	3,111
Intangible assets (other than goodwill)(5)	2,914	1,610	1,783
Total capital expenditures(6)	**7,231**	**4,901**	**4,894**

(1) Since January 1, 2003, the Netikos group, the Webegg group, the TILab, Loquendo and Eustema are no longer consolidated by the IT Group Operating Activity. BBNed is no longer included in Other Activities. The TILab moved to Other activities and Loquendo and BB Ned became part of Wireline, whereas the other companies moved to the IT Market Business Unit.
(2) The data refer to Entel Chile group, Entel Bolivia group, the company Telecom Italia America Latina and the business segment South America of Telecom Italia.
(3) The data presented include the additions to fixed assets of the International Affairs Corporate Function, the TILab, the Business Unit Satellite Services (the Telespazio group) which was disposed of during the fourth quarter of 2002 and consolidated in the statement of operations only for the first nine months of 2002 the 9Télécom group sold in the third quarter of 2002 and for which only the statement of income data was consolidated for the first six months of 2002 as well as the financial companies, the centralized group services and the staff functions.
(4) Capital expenditures in fixed assets are mainly related to local and long distance networks, exchange equipment, investment in subscribers equipment, radio and transmission equipment.
(5) Intangible assets, other than goodwill, include investments such as software for telecommunications systems and licenses.
(6) Intercompany capital expenditures are adjusted to eliminate intercompany profit.

In the three years ended December 31, 2003, cash flows from operating activities (9,921 million in 2003, 9,815 million in 2002 and 8,719 million in 2001) exceeded capital expenditures in fixed and intangible assets (4,894 million in 2003, 4,901 million in 2002 and 7,231 million in 2001).

Capital expenditures under the Business Plan

The capital expenditures planned for the three years 2004-2006 will be approximately 15 billion, in line with the forecast for the three years 2003-2005. The breakdown by sector of activity is shown in the table below.

	Approximate % of Capital Expenditures
Wireline	42%
Mobile	47%
Telecom Italia Media	1%
Other	10%

Approximately two thirds of the total of our capital expenditures planned for the period 2004-2006 (15 billion) will be invested in new products and market innovation and development.

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Wireline

The Wireline Business Unit plans to invest approximately 6.3 billion of capital expenditures for the 2004-2006 period in order to continue the development of broadband services both in the domestic market and in other selected European countries (France and Germany, where operations are already on going) and to invest in infractructures and systems of innovation.

Mobile

The Mobile Business Unit, will invest approximately 40% of the 7 billion planned for the 2004-2006 period for international development, mainly in Brazil. It will continue the start-up of the PCS operations and the GSM overlay in areas previously covered with TDMA.

In Italy, TIM has planned the commercial launch of innovative services based on EDGE technology and, afterwards, of UMTS.

Telecom Italia Media

Telecom Italia Media will focus its investments on Internet services and the Television business. In this sector, it is planned also the launch of the Digital Terrestrial Television .

Research and Development Activities

The Group spent 204 million, 151 million and 148 million on research and development in 2001, 2002 and 2003 respectively. The Group also receives grants from research and development national and international programs.

TILAB performs both strategic research and research specifically requested by Group Companies that focuses on projects that are of strategic interest for the individual Business Units and advances the Group s technological leadership. Research is also carried out in specific area in partnership with Pirelli Labs.

The activities are organized into the main innovative areas of interest of the Group such as:

- Terminal and user interfaces,

- Applications and Services,
- Service control,
- Access, metro and core network,
- Network operations and management.

Increasing attention to the opportunity of generating competitive advantages and creating value for the Telecom Italia Group was also pursued through the strategic management of the relations between research, Intellectual Property Rights (IPR) and business with the aim of increasing the number of registered patents. In this context, during the year, 68 new patents were filed of which 14 are jointly owned with Pirelli.

In 2003 TILAB s research was based on three macro areas: Broadband Services, Mobile Services, Network Innovation.

Consolidated Financial Statements as of and for the three Year period Ended December 31, 2003 Reconciliation of Italian GAAP to U.S. GAAP.

During the three year period between 2001 to 2003 the Telecom Italia Group engaged in certain significant transactions which, under U.S. GAAP give rise to material differences in net income, shareholders equity and indebtedness when compared to Italian GAAP. In addition, adoption and application of certain U.S. GAAP accounting principles has resulted in material adjustments to U.S. GAAP net income and shareholders equity when compared to Italian GAAP. In the course of 2001, 2002 and 2003, the following transactions and application of U.S. GAAP accounting principles have given rise to the most significant differences:

- the Merger;
- the differences in the accounting for the 2000 acquisition of SEAT required significant impairment charges when compared to Italian GAAP;
- the significant number of acquisitions made by SEAT using its ordinary shares as consideration for such acquisitions;
- adoption of SFAS 142 under U.S. GAAP, which requires that amortization of goodwill and indefinite lived intangibles be eliminated, and instead reviewed annually for impairment based on fair value;
- the sale of certain real estate properties to IM.SER, at that time a wholly owned subsidiary of the Telecom Italia Group, the subsequent sale of 60% of IM.SER to third parties and the transfer of these interests and other real estate assets as part of the Tiglio transactions;
- restructuring of certain real estate properties within the Tiglio I and the Tiglio II framework;
- fair value accounting for the various derivative positions of the Telecom Italia Group, including the original and significant derivative positions of Olivetti that came about from the 1999 controlling interest acquisition by Olivetti of Old Telecom Italia;
- the substantial decrease in asset valuations in the Telecom and Internet sectors in general;
- the capitalization of interest expense based on the average value of the assets under construction, as opposed to the specific borrowings related to an asset;
- the accounting for deferred income tax asset and liability recognition; and
- the sale of certain equity investments in the satellite sector, with the Telecom Italia Group recognizing gains on the sale of an entity for which it still has a continuing ownership interest.

As a result of the foregoing transactions there are material differences for the three year period ended December 31, 2003 in reconciling Italian GAAP net income and stockholders equity to U.S. GAAP. The following is a discussion of the U.S. GAAP treatment of such transactions and the application of the described U.S. GAAP accounting principles and the impact on net income or loss and stockholders equity under Italian GAAP for the three year period ended December 31, 2003. For a complete description of the Telecom Italia Group s reconciliation and other required U.S. GAAP disclosures see Notes 27, 28 and 29 of the Notes to the Consolidated Financial Statements included elsewhere herein.

Year ended December 31, 2003

Net Income, net of minority interests

Under Italian GAAP, net income was 1,192 million, compared to 1,841 million under U.S. GAAP. The increase in net income of 649 million is largely attributable to certain of the transactions as well as the application of certain of the U.S. GAAP accounting principles described above which resulted in material adjustments to the Italian GAAP operating results. A description of such transactions and accounting differences and their impact on 2003 are described below:

- As discussed in Note 29 (i) of the Notes to the Consolidated Financial Statements, the Telecom Italia Group adopted the accounting and presentation requirements of SFAS 142 as of January 1, 2002 for accounting applicable to goodwill and indefinite-lived intangible assets. The requirements of SFAS 142 are such that goodwill and certain non-amortizing intangibles are no longer considered to be wasting assets. Instead, it is necessary to apply a fair value approach to goodwill on an annual basis. The total adjustment deriving from the application of SFAS 142 in 2003 was 268 million (which includes the amortization of goodwill under Italian GAAP and is net of the reversal of accumulated amortization of goodwill pertaining to New SEAT, reclassified to discontinued operations). For U.S. GAAP purposes, applying SFAS 142, this amount has been reversed, increasing operating income under U.S. GAAP by the same amount.

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- As discussed in Note 27 of the Notes to the Consolidated Financial Statements, the Merger has been accounted for as the acquisition of a minority interests under U.S. GAAP. Therefore the basis of accounting, including the exchange of Olivetti (now Telecom Italia) shares for Old Telecom Italia shares, has been determined on the basis of fair value, generating substantially higher amounts of intangibles, goodwill, other assets and shareholders equity compared to Italian GAAP. Similar U.S. GAAP accounting treatment was also applied to Olivetti s 1999 acquisition of control of Old Telecom Italia. As a result, these transactions gave rise to classes of assets, in particular other tangible and intangible assets besides goodwill, that are being amortized. These accounting principle differences accounted for approximately 946 million in additional income gross of taxes in 2003.

- Telecom Italia, due to its high levels of gross debt, has entered into significant interest rate and currency swaps in order to hedge the economic risk associated with those positions. From the perspective of U.S. GAAP, these transactions have not met the accounting requirements to allow the Telecom Italia Group to utilize hedge accounting. Therefore, the fair values of the Telecom Italia Group s derivatives have been marked to market with the change in the fair values being charged to income. In 2003, pre-tax expense for the Telecom Italia Group was 171 million.

- In 2003, for Italian GAAP purposes, Olivetti (now Telecom Italia) recognized an additional tax benefit of 1,266 million related to the write-down taken in the tax basis of the investment in Old Telecom Italia in 2002. The tax benefit arising from this write-down (totaling 2,397 million), was not fully recognized in the Italian GAAP financial statements of Olivetti at December 31, 2002, as the use of the tax benefit was subject to, among other things, the completion of the Merger. However, for U.S. GAAP purposes, the Merger was considered to be a tax planning strategy that would, more likely than not, allow the recognition of the tax asset. Therefore, for U.S. GAAP accounting purposes the entire deferred tax asset was recognized in the 2002 U.S. GAAP net income.

- As a result of the sale of New SEAT in August 2003, the activities of New SEAT are treated as a discontinued operation for U.S. GAAP. During 2003 there were significant U.S. GAAP adjustments relating to New SEAT which are the results of transactions which are described in more detail in the discussion for the year ended December 31, 2002 and the year ended December 31, 2001. The adjustments, which are included in the discontinued operation line of the U.S. GAAP reconciliation, resulted in an increase in U.S. GAAP net income of 473 million.

Stockholders Equity, net of minority interests

Stockholder s equity under U.S. GAAP at December 31, 2003 was 35,067 million, compared to 16,092 million under Italian GAAP. The overall impact of the U.S. GAAP adjustments was to increase stockholders equity net of minority interests by 18,975 million.

Total assets as of December 31, 2003 under Italian GAAP were 80,501 million, compared to 108,093 million included in the U.S. GAAP balance sheet, an increase under U.S. GAAP in total assets of 27,592 million. The difference can be attributed to the following:

- As described above and in Note 27 of the Notes to the Consolidated Financial Statements, the differences in accounting principles for the acquisition of the minority interests in Old Telecom Italia, in particular the valuation of Olivetti (now Telecom Italia) shares exchanged for the Old Telecom Italia minority interests shares, increased the book value of the U.S. GAAP equity by 24,161 million. Approximately 17,927 million of this increase came from the value of the shares exchanged, which for Italian GAAP purposes have not been accounted for at fair value.

- Approximately 364 million related to the capitalization of interest expense on construction in progress. For U.S. GAAP purposes, the Telecom Italia Group capitalizes interest on the average amount of construction in progress throughout the year; however for Italian GAAP purposes only interest expense on specific borrowings related to fixed assets are capitalized.

- For purposes of U.S. GAAP, the Telecom Italia Group has not amortized goodwill since January 1, 2002. The effect on shareholders equity has been an increase of 364 million compared to Italian GAAP shareholders equity.

- For purposes of U.S. GAAP, the Telecom Italia Group accounted for 4,982 million of additional deferred tax liabilities principally in connection with the purchase accounting mentioned above and other business combinations.

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Total liabilities as of December 31, 2003 under Italian GAAP were 59,912 million, compared to 67,946 million under U.S. GAAP. In particular, total long-term debt increases from 30,852 million under Italian GAAP to 32,586 million under U.S. GAAP, due to the following items:

- Telecom Italia has entered into a series of leasing arrangements whereby selected properties have been transferred to certain equity method investees. Prior to these arrangements Telecom Italia had owned these properties. Under Italian GAAP, the transfers of the assets and the subsequent lease agreements have been accounted for as a sale and operating lease. Under U.S. GAAP, the fixed assets remain on the balance sheet, with the lease agreements included in long-term debt. The long-term debt at the end of 2003 includes an additional 2,071 million related to the effects of the leasing agreements.

- In 2001 Telecom Italia entered into an arrangement whereby certain securities were transferred to an existing wholly owned entity, this entity was then partially sold after incurring non-recourse indebtedness. Under U.S. GAAP the transaction did not qualify for sale accounting, therefore at the end of 2003 an additional 191 million is still included in long-term debt.

Year ended December 31, 2002

Net Income, net of minority interests

Under Italian GAAP, the net loss for the year ended December 31, 2002 was 773 million, whereas under U.S. GAAP the result was net income of 1,956 million. In 2002, the 2,729 million improvement in net result from Italian to U.S. GAAP is largely attributable to certain of the transactions as well as the application of certain of the U.S. GAAP accounting principles described above that have resulted in material adjustments to the Italian GAAP operating results. A description of such transactions and accounting differences and their impact on 2002 are described below:

- The adoption of SFAS 142 decreased pre-tax loss by 524 million.

- In 2000 Telecom Italia entered into a series of transactions whereby certain real estate assets were transferred to a related party and subsequently partially sold. Telecom Italia retained an interest in the vehicle that held the real estate assets and, concurrent with the transaction, entered into long-term leases for the assets. In 2002, those same assets, in conjunction with other real estate assets of the Telecom Italia Group, were again transferred through a complex series of contributions, acquisitions and disposals (collectively referred to as the Tiglio transactions). The result of the Tiglio transactions was that, under U.S. GAAP, the Telecom Italia Group was still considered to retain an interest in the underlying real estate assets. Therefore they failed the requirements under U.S. GAAP to recognize any gains on the sales and the Telecom Italia Group was not allowed, under U.S. GAAP, to deconsolidate the assets and liabilities associated with the Tiglio structuring. Under U.S. GAAP in 2002, the increase in pre-tax loss of 153 million is due to the reversal of the gain recognized in the underlying Italian GAAP financial statements for the Tiglio transactions, net of the continuing impact of the original real estate transaction in 2000.

- Telecom Italia considers a certain amount of shares in its controlled subsidiaries to be available for sale , meaning that those shares are available to be sold on the open market when the proper conditions exist. These shares are accounted for in marketable securities at the lower of cost or market for Italian GAAP purposes. For purposes of U.S. GAAP, it is not possible to allocate a portion of the shares held in the consolidated subsidiary as marketable securities in the balance sheet, instead, all of the shares must be consolidated. The effect on the consolidation of the Telecom Italia Group is to decrease the net income attributable to minority interests and to decrease the associated minority interest liability on the U.S. GAAP balance sheet. In 2002, the minority interests allocation performed under Italian GAAP was decreased by 83 million pre-tax, representing the fact that the Telecom Italia Group actually holds a higher percentage of shares in the controlled subsidiary than is accounted for in the Italian GAAP consolidation, therefore the earnings allocated to the minority interest is less in the U.S. GAAP results.

- U.S. GAAP requires that interest expense be capitalized on all qualified borrowings for assets under construction. Italian GAAP requires that interest expense only be capitalized on assets that have a specific borrowing. During 2002, the Group continued to maintain the UMTS licenses acquired between 2000 to 2002 in construction in progress while the supporting networks are implemented. Under U.S. GAAP, an additional 127 million in interest expense was capitalized as the financing costs associated with constructing these assets. Interest capitalization will cease on these assets when they are ready for use. The higher level of capitalized interest results in higher levels of depreciation charges in the future.

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- As described above, certain derivative instruments intended to hedge the economic risks of Telecom Italia s high levels of debt do not satisfy the hedge accounting treatment required under U.S. GAAP. In 2002 the fair value of these derivative instruments increased net income by 319 million.

- In 2002, for U.S. GAAP purposes, Olivetti (now Telecom Italia) took a tax only write-down of its existing investment in Old Telecom Italia, with a total tax benefit of 2,397 million being created. For Italian financial reporting purposes, this tax asset was reserved for 1,266 million as the recognition of the tax benefit was dependent upon, among other things, the Merger being consummated. For U.S. GAAP purposes, the tax asset was considered more likely than not to be recovered due to the use of the Merger as a tax planning strategy that could reasonably be considered to be consummated. Therefore, for U.S. GAAP purposes, the 2,397 million asset was fully recognized in 2002 net income, whereas for Italian GAAP it was recognized in part in 2002 and in part in 2003.

As a result of the sale of New SEAT in August 2003, the activities of New SEAT are treated as a discontinued operation for U.S. GAAP. During 2002 there were significant U.S. GAAP adjustments relating to New SEAT which are consolidated into the gross adjustment in the discontinued operation line of the U.S. GAAP reconciliation. The most significant of these adjustments included:

- Telecom Italia entered into a simultaneous put and call arrangement with a minority interest shareholder in its 2000 acquisition of SEAT. Under U.S. GAAP, that transaction was considered the acquisition of a minority interest, and the entire agreement was accounted for in the 2000 U.S. GAAP financial statements. A significant portion of that acquisition was also written-off in the 2000 U.S. GAAP financial statements. In 2000 there was no accounting recognition for this agreement in the Italian GAAP financial statements. In the 2002 Italian GAAP financial statements, Telecom Italia accrued for an additional 1,942 million of the estimated amount of the put/call transaction, representing the estimated amount of the required future payment that will not be recoverable from the operations of SEAT. As the entire put/call financing, including the associated goodwill and impairment, had already been accounted for in the U.S. GAAP financial statements, the 2002 recognition of the same event in the underlying Italian GAAP financial statements requires that the 2002 recognition of the impairment be reversed, increasing U.S. GAAP net income.

- In 2002, Telecom Italia recorded additional impairments to its SEAT investment. As discussed in the accompanying financial statements as of December 31, 2002, Telecom Italia reviewed the carrying value of its investment in the Internet and Media operating segment as of December 31, 2002. That analysis resulted in an additional impairment charge for U.S. GAAP of 1,808 million. This difference is due to the fact that, because a different basis of accounting under Italian and U.S. GAAP was used for the original acquisition of SEAT, the carrying values of the reporting units impaired in 2002 were different, therefore leading to different impairment amounts.

Stockholders Equity, net of minority interests

Stockholder s equity under U.S. GAAP at December 31, 2002 was 15,224 million, compared to 11,640 million under Italian GAAP. The overall impact of the U.S. GAAP adjustments was a material increase in stockholders equity net of minority interests of 3,584 million, with the net increase due to certain material adjustments in certain line items of the U.S. GAAP condensed consolidated balance sheet.

Total assets as of December 31, 2002 under Italian GAAP were 83,384 million, compared to 92,911 million included in the U.S. GAAP balance sheet, an increase in total assets of 9,527 million. The difference can be attributed to the following:

- at the end of 2002, there was a total of 31,065 million of goodwill recorded under U.S. GAAP, compared to 27,894 million for Italian GAAP, an increase of 3,171 million. The higher level of goodwill is primarily attributable to the differences in accounting principles related to accounting for acquisition transactions that involve share exchanges and the discontinuance of goodwill amortization for U.S. GAAP purposes. The most significant difference is attributable to the 1999 acquisition by Olivetti (now Telecom Italia) of its controlling stake in Old Telecom Italia;

- net fixed assets on the U.S. GAAP balance sheet are higher due to the inclusion of the real estate transferred to IM.SER in 2000 and Tiglio I and Tiglio II in 2002, which under U.S. GAAP have a book value of 1,907 million as of December 31, 2002, whereas under Italian GAAP these fixed assets are not recorded. Instead, the vehicles that own the assets and for which the Telecom Italia Group holds a minority interest stake are recognized on the equity basis of accounting; and

- other various items including intangibles arising from purchase accounting under U.S. GAAP, capitalization of interest on tangible and intangible assets under construction and deferred tax assets.

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Total liabilities as of December 31, 2002 under Italian GAAP were 62,760 million, compared to 68,314 million under U.S. GAAP. With respect to liabilities, the material impact from the U.S. GAAP adjustments relates to long-term debt. Total long-term debt increases from 33,804 million under Italian GAAP to 38,375 million under U.S. GAAP, due to the following items:

- SEAT Put/Call Option Financing pursuant to the various transactions relating to the arrangements between Huit II and the J.P. Morgan Chase Group, in which J.P. Morgan Chase had a put option to Telecom Italia for approximately 710 million SEAT shares at a price of 4.20 per share and Telecom Italia had a call option on approximately 660 million SEAT shares for the same price. The strike price was subsequently renegotiated to 3.40 per share. U.S. GAAP considers this transaction as the acquisition financing of a minority equity interest. As a result, U.S. GAAP required Telecom Italia to record additional long-term debt of 2,417 million. Telecom Italia accrued 569 million of the obligation in 2001 which was paid in 2002 at its present value (500 million), and 1,942 million in 2002. The amount accrued under Italian GAAP in 2002 is included under Other Liabilities in the accompanying financial statements, leaving an unrecognized liability of 475 million of the put/call transaction.

- Sale of Real Estate to IM.SER and Tiglio Projects In 2000 Telecom Italia transferred certain properties to a wholly owned subsidiary, IM.SER, after which Telecom Italia sold 60% of the shares to third party investors. After the sale of the majority stake in IM.SER, it subsequently borrowed 2,427 million and distributed the cash to the shareholders as an extraordinary dividend. Telecom Italia received, from both the divested equity ownership stake and the special dividend from IM.SER, approximately 2,700 million in cash receipts. Under Italian GAAP the Group recognized a gain on the partial sale of the ownership interest, removed the historical cost of the real estate from the balance sheet and IM.SER s debt was not recognized. Telecom Italia subsequently leased the assets back from IM.SER. For purposes of U.S. GAAP, the continuing economic interest of the Group in IM.SER requires that the real estate remain on the consolidated balance sheet, along with the associated debt. In 2002, as discussed above, the Telecom Italia Group also entered into a series of transactions with related parties and affiliates whereby certain real estate assets were transferred in exchange for ownership interests in two new companies (Tiglio I and Tiglio II) and the right to share in future sales of real estate property (also referred to as the Tiglio transactions). Therefore, under U.S. GAAP, similar to IM.SER, the assets and debt associated with the Tiglio transactions must remain on the consolidated balance sheet of the Telecom Italia Group. The debt on the consolidated U.S. GAAP balance sheet at the end of 2002 for these transactions (IM.SER and Tiglio) was 2,366 million.

Year Ended December 31, 2001

Net Loss, net of minority interests

Under Italian GAAP, the net loss for the year ended December 31, 2001 was 3,090 million and under U.S. GAAP the net loss was 4,006 million. In 2001, the 916 million increase in net loss from Italian to U.S. GAAP is largely attributable to certain of the transactions as well as the application of certain of the U.S. GAAP accounting principles described above that resulted in certain material adjustments. A description of such transactions and accounting differences and their impact on 2001 are described below:

- In 2001 the net effect of applying the purchase method of accounting relating to the acquisition of Old Telecom Italia resulted in an increase of the loss for U.S. GAAP reporting purposes of 483 million, principally as a result of higher amortization expense for U.S. GAAP purposes (where the purchase price allocation included also the identification of intangible assets in addition to goodwill). Under Italian GAAP all the excess of the purchase price was allocated to goodwill resulting in lower amortization expense.

- In 2001 Telecom Italia sold certain non-core investments in satellite sector companies, transferring its equity interests to Mirror, a wholly owned company, at fair value. Mirror borrowed 217 million in non-recourse debt to acquire these assets. Subsequent to the transfer, Telecom Italia sold 70% of Mirror to a merchant bank for 233 million. For purposes of Italian GAAP the Company recognized a gain of 170 million, with no additional debt recorded on the balance sheet. For Italian GAAP purposes the remaining equity investment was impaired for 40 million at December 31, 2001. For purposes of U.S. GAAP, Mirror was deemed to be a non-qualified special purpose entity, therefore the accounts of Mirror were required to be consolidated within the Telecom Italia Group. The effects of consolidating Mirror into the Telecom Italia Group s U.S. GAAP financial statements was to reverse the gain and the impairment recognized and increase the U.S. GAAP net loss by 130 million, and to place an

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additional 450 million in debt on the balance sheet, 217 million as bank debt and 233 million as additional minority interest.

- Certain subsidiaries of the Telecom Italia Group have their own publicly traded shares, which they use from time to time to effect acquisitions. Under Italian GAAP the reduction of the Telecom Italia Group s ownership interest in a subsidiary is accounted for as an adjustment to stockholders equity. Under U.S. GAAP, the Telecom Italia Group consistently accounts for these types of dilutions as a non-operating gain or loss through the statement of operations. In 2001, 325 million in gains were recorded in the U.S. GAAP results due to these types of transactions.

Partially offsetting the effects of the foregoing was the capitalization of interest expense on construction in progress (including the UMTS licenses and their supporting networks) which reduced the U.S. GAAP loss by 124 million pre-tax.

As a result of the sale of New SEAT in August 2003, as noted above, the activities of New SEAT are treated as a discontinued operation and adjustments related to New SEAT are included in the gross adjustment under the discontinued operation line. The most significant of these adjustments included:

- *SEAT acquisition* In late 2000 and into 2001, SEAT acquired a significant number of companies using SEAT s own shares as consideration. Under Italian GAAP there is no economic value assigned to the use of stock in a transaction, therefore the purchase price of these transactions on an Italian GAAP basis is considerably lower. For purposes of U.S. GAAP, these transactions have also been treated as acquisitions; however, the fair value of the consideration given is used as the basis to assign the purchase price to the fair value of the assets acquired and liabilities assumed. In general, higher levels of intangible assets, including goodwill, exist in these transactions. For U.S. GAAP purposes, SEAT added additional goodwill of 810 million in 2001 due to the use of its stock as the acquisition currency. In 2001, 184 million of this goodwill was amortized in the statement of operations.

- In 2001, the Telecom Italia Group recorded 2,381 million in impairment charges under Italian GAAP. For purposes of U.S. GAAP, an additional 2,641 million in impairment charges were recorded, for a total charge of 5,022 million. For purposes of Italian GAAP the Telecom Italia Group used the fair value of the individual entities reviewed, with fair value generally being based on a discounted cash flow model. For purposes of U.S. GAAP, the process of reviewing assets for possible impairments requires the review of assets assuming the lowest level of cash flows . Therefore, for purposes of U.S. GAAP, the Telecom Italia Group was required to review certain assets for impairment at a lower level of analysis than that performed in the Italian GAAP review. Of the total charges under U.S. GAAP for impairment in 2001, 2,338 million was related to SEAT and SEAT subsidiaries. The remaining amount of the impairment charge is related to investments in Austria and Latin America.

- Telecom Italia entered into a simultaneous put and call arrangement with a minority interest shareholder in its 2000 acquisition of SEAT. The U.S. GAAP treatment of the transaction is described above. In 2001, the Telecom Italia Group re-negotiated certain terms with the option holder, with an agreement to reduce the option put price. However, the Telecom Italia Group was still required to pay the difference in the strike price reduction to the holder. For purposes of Italian GAAP, an accrual of 569 million was made to record this portion of the obligation in 2001, with a comparable charge to the statement of operations. For purposes of U.S. GAAP, since the transaction is recorded as debt on the U.S. GAAP balance sheet and accounted for in the SEAT purchase accounting the charge is reversed under U.S. GAAP and reduces the U.S. GAAP loss by 569 million before tax.

Stockholders Equity, net of minority interests

Stockholders equity under U.S. GAAP at December 31, 2001 was 13,612 million, compared to 12,729 million under Italian GAAP. Although the overall impact on stockholders equity of the U.S. GAAP adjustments was to increase stockholders equity net of minority interests by only 883 million, certain adjustments were material and certain line items of the U.S. GAAP condensed consolidated balance sheet were materially impacted.

Total assets as of December 31, 2001 under Italian GAAP were 94,227 million, compared to 103,588 million on the U.S. GAAP balance sheet, an increase in total assets of 9,361 million. The difference can be attributed to three asset classes:

- at the end of 2001, there was a total of 34,323 million in goodwill recorded under U.S. GAAP, compared to 31,887 million for Italian GAAP, an increase of 2,436 million. The higher level of

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goodwill is attributable to the continuing effects of both the SEAT acquisition and the subsequent acquisitions done by SEAT, generally using their stock as the acquisition consideration, as well as the residual amount of goodwill from the STET-Telecom Italia Merger;

- net fixed assets on the U.S. GAAP balance sheet are higher due to the inclusion of the real estate transferred to IM.SER in 2000 which under U.S. GAAP have a book value of 2,202 million as of December 31, 2001; and

- other intangibles arising from the purchase accounting under U.S. GAAP for 2,698 million.

With respect to liabilities, the material impact from the U.S. GAAP adjustments relates to long-term debt. Long-term debt increased from 37,747 million to 43,117 million, due to the following items:

- SEAT Put/Call Option Financing pursuant to the various transactions relating to the arrangements between Huit II and the J.P. Morgan Chase group, in which J.P. Morgan Chase had a put option to Telecom Italia for approximately 710 million SEAT shares at a price of 4.20 per share and Telecom Italia has a call option on approximately 660 million SEAT shares for the same price. U.S. GAAP considers this transaction as the acquisition financing of a minority equity interest. As a result, U.S. GAAP required Telecom Italia to record additional long-term debt of 2,985 million.

- Sale of Real Estate to IM.SER See a description of these transactions above under Sale of Real Estate to IM.SER and Tiglio Projects . As described above, for purposes of U.S. GAAP, the continuing economic interest of the Telecom Italia Group in IM.SER requires that the real estate remain in the consolidated balance sheet, along with the associated debt. The debt on the consolidated U.S. GAAP balance sheet at the end of 2001 for this transaction was 2,520 million.

As a result of the demerger and sale of New SEAT, the J.P. Morgan put and call arrangements were settled during 2003, so that the adjustments made during 2001 and 2002 were no longer required in 2003.

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Recent Developments Telecom Italia Group Results for the First Quarter Ended March 31, 2004 compared to March 31, 2003

The information in this section should be read in conjunction with the Telecom Italia Group s consolidated financial statements, and the notes thereto, included elsewhere in this Annual Report.

The summary historical consolidated financial data for the Telecom Italia Group as of March 31, 2004, and for the three months ended March 31, 2004 and 2003, have been derived from unaudited interim consolidated financial statements which, in our opinion, reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of our results of operations for the unaudited interim periods. Results for the three months ended March 31, 2004 are not necessarily indicative of results that may be expected for the entire year.

	Three Months ended March 31,	
	2003	2004
	(Unaudited) (millions of Euro)	
Statement of Operations Data:		
Operating revenues	7,291	7,418
Other income	69	58
Total revenues	7,360	7,476
Cost of materials	415	452
Salaries and social security contributions	1,115	1,033
Depreciation and amortization	1,653	1,590
Other external charges	2,813	2,813
Changes in inventories	(18)	(44)
Capitalized internal construction costs	(145)	(156)
Total operating expenses	5,833	5,688
Operating income	1,527	1,788
Financial income	288	292
Financial expense	(940)	(722)
of which writedowns and equity in losses in affiliated and other companies, net	*(82)*	*(14)*
Other income and expense, net	(7)	(14)
Income before income taxes and minority interests	868	1,344
Income taxes	(713)	(809)
Net income before minority interests	155	535
Minority interest	(552)	(258)
Net income (loss)	(397)	277

	As of December 31, 2003	As of March 31, 2004
		(Unaudited)
	(millions of Euro)	
Balance Sheet Data:		
Total current assets	22,498	22,082
Fixed assets, net	18,324	17,977
Intangible assets, net	33,853	33,474
Total assets	80,501	79,537
Short-term debt	10,613	6,863
Total current liabilities	23,373	19,222
Long-term debt	30,852	33,071
Total liabilities	59,912	58,358
Total stockholders equity before minority interest	16,092	16,390
Total stockholders equity	20,589	21,179

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Business Unit Financial Data

The following table sets forth operating revenues, gross operating profit and operating income by Business Unit.

	Operating Revenues		Gross Operating Profit		Operating Income	
	Three months ended March 31,		Three months ended March 31,		Three months ended March 31,	
	2003	2004	2003	2004	2003	2004
			(Unaudited) (millions of Euro)			
Wireline(1)(2)	4,242	4,303	1,970	2,037	1,228	1,315
Mobile	2,616	2,937	1,262	1,425	897	955
South America(2)	291	264	106	101	41	37
Internet and Media(3)	345	149	47	3	(35)	(24)
IT Market	156	169	10	11	0	3
IT Group	229	225	11	15	(22)	(15)
Olivetti Tecnost	158	144	2	7	(5)	2
Other activities and elimination(2)(4)	(746)	(773)	(100)	(105)	(577)	(485)
Total	**7,291**	**7,418**	**3,308**	**3,494**	**1,527**	**1,788**

(1) Starting from January 1, 2004, the company Telefonia Mobile Sanmarinese S.p.A., 51% owned by Intelcom San Marino, is consolidated on a line by line basis in the Wireline Business Unit.

(2) The data refer to Entel Chile Group and Entel Bolivia Group. On March 1, 2004, the Latin America Operations function was disbanded. This function was set up in 2002 and reported to the head of the Mobile Business Unit for mobile telecommunications and to the CEO Carlo Buora for wireline telecommunications and was responsible for the global coordination of all the activities of the Group in Latin America. Telecom Italia Latam S.A. has now taken over the new role of the delocalized Corporate function in Latin America, consistent with our chosen strategy to consolidate and develop our international presence in the Latin America geographical area. The Wireline and Mobile business units with their present corporate organizational structure are nevertheless responsible for the results of the subsidiaries in Latin America under their control. As a result of this reorganization and with effect on January 1, 2004, the company Telecom Italia Latam S.A. and the business segment South America of Telecom Italia are included in other activities. The data relating to the first quarter ended March 31, 2003 has been reclassified and presented consistent with the first quarter ended March 31, 2004 presentation. This represents a change in this reported segment compared to the South America segment as reported for the three years in the period ended December 31, 2003.

(3) New SEAT, the beneficiary company of the spin-off from Seat Pagine Gialle which took place on August 1, 2003, was sold on August 8, 2003. As a result of this, the figures related to the three months ended March 31, 2003 include the results of operations of New SEAT Group that was subsequently disposed of, as well as the results of operations of the remaining part of Seat Pagine Gialle that after the spin-off was renamed Telecom Italia Media.

(4) The data refer to the activities managed by International Affairs Corporate Function, TILab, the centralized Group services and the staff functions, the financial companies, the company Telecom Italia Latam S.A. and the business segment South America of Telecom Italia.

Telecom Italia Group Consolidated Results

For the three months ended March 31, 2004, our consolidated net income after minority interests was 277 million (535 million before minority interests) compared to a loss of 397 million (income of 155 million before minority interests) for the first three months of 2003. Our consolidated net income (loss) for the three months ended March 31, 2003 would have been a loss of 88 million, attributing to Olivetti the minority interest in the result of the Old Telecom Italia, acquired following the merger of Old Telecom Italia into Olivetti.

The improvement in our consolidated net income (loss) (+ 674 million) was due to the following factors:

- the increase in operating income (+ 261 million, of which 75 million is attributable to the cancellation of the TLC license fee following the verdict handed down by the European Court of Justice in September 2003);
- the reduction in financial expense, net of 222 million; and
- the lower minority interests in earnings of 294 million due to the Merger.

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These factors were offset in part by higher income taxes of 96 million.

Our consolidated operating revenues for the three months ended March 31, 2004 were 7,418 million, an increase of 127 million or 1.7% compared to the same period in 2003. Excluding the negative effects of exchange rate fluctuations (10 million) and changes to the consolidation area (231 million, of which 185 million related to the sale of New SEAT from the Internet and Media Business Unit which occurred in August 2003), organic growth reached 5.2% (an increase of 368 million). Organic growth of consolidated operating revenues reflected:

- a significant increase in the revenues of the Mobile Business Unit (+ 326 million), which were driven by the domestic market (voice traffic and value-added services) and by the South-American market;
- an increase in the revenues of the Wireline Business Unit (+ 42 million), which was achieved due to the effective management of the core telephone services market and the growth in innovative business segments such as Broadband, innovative data transmission and data and Web VAS for the business clientele;
- an increase in the revenues of the IT Market Business Unit (+ 23 million) and Internet and Media (+ 23 million); and
- a decrease in the revenues of wireline/integrated companies in South America (- 35 million), mainly due to the Entel Chile Group).

As of March 31, 2004, Telecom Italia had 26.4 million domestic subscriber fixed lines, including ISDN equivalent lines (compared to 26.6 million as of December 31, 2003 and 27.1 million as of March 31, 2003). As of March 31, 2004, TIM had 26.0 million domestic mobile lines in Italy (substantially in line with those as of December 31, 2003; as of March 31, 2003, TIM had 25.7 million domestic mobile lines).

Our consolidated Gross Operating Profit, as calculated below, was 3,494 million for the three months ended March 31, 2004 compared to 3,308 million for the three months ended March 31, 2003 (please see table below), an increase of 186 million or 5.6%. In the three months ended March 31, 2004, gross operating profit was positively impacted, other than by the increase in consolidated operating revenues, by the lower costs of personnel (a decrease of 82 million, from 1,115 million in the three months ended March 31, 2003 to 1,033 million in the three months ended March 31, 2004) and the cancellation of the TLC license fee (66 million in the three months ended March 31, 2003).

As Gross Operating Profit includes certain financial statement items and excludes others, it is considered a non-GAAP financial measure as defined in Item 10 of Regulation S-K under the 1934 Act. The following table reconciles operating income to the calculation of Gross Operating Profit by showing the statement of operation items included in calculating Gross Operating Profit:

	Three Months ended March 31,	
	2003	2004
	(Unaudited) (millions of Euro)	
Operating income	1,527	1,788
Depreciation and Amortization	1,653	1,590

Other external charges:		
• Provision for bad debts	75	51
• Write-downs of fixed assets and intangibles		1
• Provision for risks	32	12
• Other provisions and operating charges	83	106
Other income (excluding operating grants, reimbursements for personnel costs and costs of external services rendered)	(62)	(54)
Gross Operating Profit	**3,308**	**3,494**

We believe that Gross Operating Profit (as calculated above) provides the best indication of our operating performance and is meaningful information for investors. In addition, we also believe (although other telecommunication operators will calculate such information differently) that Gross Operating Profit permits an adequate comparison of the Telecom Italia Group s performance against its peer group.

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Excluding the charges for the TLC license fee (66 million) recorded in the three months ended March 31, 2003, Gross Operating Profit increased by 120 million or 3.6%. Moreover, excluding the negative effects of exchange rate fluctuations (4 million) and changes to the consolidation area (46 million, mainly due to the disposal of the New SEAT) organic growth of Gross Operating Profit was 5.1% (an increase of 170 million) and arose principally from the Mobile Business Unit (+ 138 million) and the Wireline Business Unit (+ 28 million).

Gross operating margin was 47.1% in the three months ended March 31, 2004 compared to 45.4% in the three months ended March 31, 2003 (46.3% excluding from the first quarter of 2003 the charges for the TLC license fee).

Our consolidated operating income amounted to 1,788 million for the three months ended March 31, 2004 compared to 1,527 million for the three months ended March 31, 2003 (an increase of 261 million or 17.1%).

Excluding the charges for the TLC license fee (75 million, which includes a provision for the reserves for risks and charges of 9 million) recorded in the three months ended March 31, 2003, operating income increased by 186 million or 11.6%. Organic growth was 184 million or 11.5%.

The increase in operating income was largely due to the decrease of 63 million in depreciation and amortization (from 1,653 million in the three months ended March 31, 2003 to 1,590 million in the three months ended March 31, 2004) principally as a result of the following factors:

- the decrease of 106 million in amortization of goodwill (from 492 million in the three months ended March 31, 2003 to 386 million in the three months ended March 31, 2004), mainly due to the disposal of New SEAT and the write-downs of goodwill made in 2003;

- the increase in amortization and depreciation of fixed intangible (other than goodwill) and tangible assets of 43 million (from 1,161 million in the three months ended March 31, 2003 to 1,204 million in the three months ended March 31, 2004), of which 34 million relates to the amortization of the UMTS license by TIM S.p.A..

As a percentage of operating revenues, operating income was 24.1% in the three months ended March 31, 2004 compared to 20.9% in the three months ended March 31, 2003 (22.0% excluding from the first quarter of 2003 the charges for the TLC license fee).

Total financial income and expense, net decreased by 222 million or 34.0%, from a net expense of 652 million in the three months ended March 31, 2003 to a net expense of 430 million in the three months ended March 31, 2004, mainly as a result of the following:

- a decrease in interest expense mainly due to the reduction in the level of interest rates as well as to the lower average borrowings outstanding during the three months ended March 31, 2004, partially offset by the excess of losses on foreign exchange over the positive effect of the monetary correction incurred by Digitel;

- the reduction in net write-downs and equity in losses in affiliated and other companies of 68 million (from 82 million in the three months ended March 31, 2003 to 14 million in the three months ended March 31, 2004);

- the gain of 62 million arising from the sale in January 2004 of the residual stake (14.78%) held by the Group in Telekom Austria.

Our gross debt decreased by 1,531 million, from 41,465 million at December 31, 2003 to 39,934 million at March 31, 2004 and our net financial debt decreased by 2,560 million, from 33,346 million as of December 31, 2003 to 30,786 million as of March 31, 2004. See the reconciliation of gross debt and net financial debt below. Net financial debt decreased mainly as a result of the followings:

- cash flow from operating activities was higher than capital expenditures (826 million) and other investing activities (36 million) totaling 862 million (860 million in the three months ended March 31, 2003);

- proceeds from the sale of tangible and intangible assets and other investing activities of 100 million.

- net proceeds from the sale of Telekom Austria of 768 million.

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Net financial debt is determined as follows:

	As of December 31, 2003	As of March 31, 2004
		(Unaudited)
	(millions of Euro)	
Short-term debt, including current portion of long-term debt	10,613	6,863
Long-term debt	30,852	33,071
Gross Debt	41,465	39,934
Cash and cash equivalents:		
• Bank and postal accounts	(4,870)	(7,514)
• Cash and valuables on hand	(7)	(6)
• Receivables for securities held under reverse repurchase agreements	(60)	(12)
• Marketable debt securities	(2,719)	(1,456)
Financial accounts receivable (included under Receivables and Other Current Assets)	(826)	(446)
Financial prepaid expense/deferred income, net and accrued financial income/expense, net (long-term)	(307)	(265)
Financial prepaid expense/deferred income, net and accrued financial income/expense, net (short-term)	670	551
Net Financial Debt(1)	**33,346**	**30,786**

(1) Net financial debt is a non-GAAP financial measure as defined in Item 10 of Regulation S-K under the 1934 Act. Although net financial debt is a non-GAAP measure, it is widely used in Italy by financial institutions to assess liquidity and the adequacy of a company s financial structure. Therefore, we believe it is useful information for investors to receive and is consistent with how we present ourselves to the analyst community.

The portion of gross financial debt due beyond twelve months rose from 74% at December 31, 2003 to 83% at March 31, 2004. On March 31, 2004, short-term debt included 5,878 million as current portion of long-term debt (9,289 million at December 31, 2003). See, however, Liquidity and Capital Resources Capital Resources.

In the first quarter of 2004, we repaid notes with a total principal amount of 3,225 millions, as follows:

- on January 1, 2004, 1,331 million principal amount of convertible notes 2001-2004 issued by Telecom Italia S.p.A.;
- on March 19, 2004, 385 million principal amount of convertible notes 2002-2004 issued by Olivetti Finance N.V. with the guarantee by Telecom Italia S.p.A.;
- on March 22, 2004, 1,500 million principal amount of notes issued by Telecom Italia S.p.A., originally maturing on June 21, 2005, repaid in advance, at par, in accordance with the terms of the notes;

- 9 million principal amount of notes 2002-2022 issued by Telecom Italia S.p.A. and reserved for subscription by employees (at March 31, 2004, the residual amount was 206 million).

On March 26, 2004, 850 million principal amount of notes were cancelled by Olivetti Finance N.V. after their buy-back:

- 650 million principal amount of notes that are part of the Olivetti Finance N.V. S.A. (originally Olivetti International Finance N.V.) 4,200 million Notes (1999-2004) with a fixed annual 5 3/8% coupon +0.45% step-up maturing in July 2004. As a result of this cancellation, notes in the principal amount of 3,550 million remain outstanding;

- Olivetti Finance N.V. S.A. 200 million principal amount of notes (2002-2005) with a floating rate coupon of 1.45% over the EONIA maturing in February 2005. As a result of this transaction none of these notes remain outstanding.

The Program, also continued for trade accounts receivable generated by the services rendered to residential customers of Telecom Italia S.p.A.. The securitization and the factoring arrangements led to an improvement in consolidated net financial debt as of March 31, 2004 of 833 million (1,201 million as of December 31, 2003).

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As of March 31, 2004, the Telecom Italia Group had 93,036 employees, a decrease of 151 units compared to December 31, 2003. The fall is due to the changes to the area of consolidation (a decrease of 455 units, of which 188 units relating to the sale of CIPI by Internet and Media and 257 units as a result of the outsourcing of the Document management activities by Telecom Italia and Emsa Servizi) partially offset by increased hiring in the operating businesses (an increase of 304 units).

Business Units

The following discussion relates to our principal Business Units as they were organized in the first quarter of 2004.

In particular, on March 1, 2004, the Latin America Operations function was disbanded. This function was set up in 2002 and reported to the head of the Mobile Business Unit for mobile telecommunications and to the CEO Carlo Buora for wireline telecommunications and was responsible for the global coordination of all the activities of the Group in Latin America. Telecom Italia Latam S.A. has now taken over the new role of the delocalized Corporate function in Latin America, consistent with our chosen strategy to consolidate and develop our international presence in the Latin America geographical area. The Wireline and Mobile Business Units with their present corporate organizational structure are nevertheless responsible for the results of the subsidiaries in Latin America under their control.

As a result of this reorganization and with effect on January 1, 2004, the company Telecom Italia Latam S.A. and the business segment South America of Telecom Italia are included in other activities.

Wireline

The following table sets forth, for the periods indicated, certain financial and other data for the Wireline Business Unit.

	Three Months ended March 31,	
Wireline	**2003(1)**	**2004(1)**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	4,242	4,303
Gross operating profit	1,970	2,037
% of gross operating revenues	46.4	47.3
Operating income	1,228	1,315
% of gross operating revenues	28.9	30.6

Number of employees at period-end	(2) 50,766	51,025

(1) The three months ended March 31, 2003 financial and other data have been reclassified and presented consistent with the three months ended March 31, 2004 presentation.
(2) Number of employees at December 31, 2003.

Wireline gross operating revenues for the three months ended March 31, 2004 were 4,303 million, an increase of 61 million or 1.4% compared to 4,242 million for the three months ended March 31, 2003; organic growth was 1% (+ 42 million). This increase was achieved mainly due to effective support of the core telephony market and to significant continuing growth of the broadband markets, innovative data services and value-added services.

In particular, Retail Internet revenues increased by 69 million or 39.9% (from 173 million in the three months ended March 31, 2003 to 242 million in the three months ended March 31, 2004), mainly achieved through the ADSL Alice and Smart offers (an increase of 76 million or 155%). Data Business revenues increased by 5 million or 1.4% (from 370 million in the three months ended March 31, 2003 to 375 million in the three months ended March 31, 2004). The growth in these revenues has been driven by innovative data services (+ 25 million or 21.0% compared to the three months ended March 31, 2003) which offset the decrease in the revenues from traditional Data services and Leased Lines, that are subject to regulated prices and to the effect of migration to innovative services.

In addition, the success and growth of new value-added service packages (Tutto 4* and Chat SMS), which rose to 589,000 units at March 31, 2004, contributed together with a stable market share on traffic to stabilizing revenues in the Retail Telephone segment. With regard to the Internet segment, broadband accesses at March 31, 2004 rose to 2,800,000, of which 2,575,000 are attributable to the domestic market, with an increase of 535,000 accesses in the three months ended March 31, 2004 (+114% compared to March 31, 2003). Accesses in the European markets of Germany, France and The Netherlands totaled 225,000 and increased by 65,000 accesses compared to December 31, 2003.

Gross operating profit increased by 67 million or 3.4% from 1,970 million in the three months ended March 31, 2003 to 2,037 million in the three months ended March 31, 2004 (excluding the charges for the TLC license fee recorded in the three months ended March 31, 2003 of 37 million, gross operating profit increased by 1.5%).

Gross operating margin was 47.3% in the three months ended March 31, 2004 and remained substantially stable with respect to the corresponding period of the previous year (excluding the charges for the TLC license fee). Gross operating margin benefitted also from the reductions in personnel costs.

Operating income improved by 87 million or 7.1% from 1,228 million in the three months ended March 31, 2003 to 1,315 million in the three months ended March 31, 2004 (excluding the charges for the TLC license fee recorded in the three months ended March 31, 2003, operating income increased by 3.2%). Operating income was also positively impacted by lower levels of depreciation and amortization and provision for bad debts.

As of March 31, 2004, the Wireline Business Unit had 51,025 employees, an increase of 259 units compared to December 31, 2003.

Mobile (TIM group)

The following table sets forth, for the periods indicated, certain financial and other data for the Mobile Business Unit.

	Three Months ended March 31,	
Mobile	**2003**	**2004**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	2,616	2,937
Gross operating profit	1,262	1,425
% of gross operating revenues	48.2	48.5

Operating income	897	955
% of gross operating revenues	34.3	32.5
Number of employees at period-end	(1)18,888	18,936

(1) Number of employees at December 31, 2003.

TIM group gross operating revenues for the three months ended March 31, 2004 were 2,937 million, an increase of 321 million or 12.3% compared to 2,616 million for the three months ended March 31, 2003. Excluding the negative effects of exchange rate fluctuations, growth was 326 million or 12.5%. Part of this increase was attributable to the international operations and in particular to the development of mobile activities in Brazil.

Consolidated Gross Operating Profit increased by 163 million or 12.9% from 1,262 million for the three months ended March 31, 2003 to 1,425 million for the three months ended March 31, 2004. Excluding the effects of exchange rate fluctuations and the charges related to the TLC license fee of 29 million recorded in the three months ended March 31, 2003, organic growth reached 10.7%. The improvement in gross operating profit was attributable principally to positive performance in Italy, offset in part by the negative impact of the Brazilian companies in the start-up phase.

Gross operating margin was 48.5% in the three months ended March 31, 2004 (49.4% in the three months ended March 31, 2003, determined by excluding the charges related to the TLC license fee).

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TIM group operating income for the three months ended March 31, 2004 increased by 58 million or 6.5% from 897 million in the three months ended March 31, 2003 to 955 million in the three months ended March 31, 2004; organic growth was 3.0%. Consolidated operating margin was 32.5% in the three months ended March 31, 2004 (35.4% in three months ended March 31, 2003, determined by excluding the charges related to the TLC license fee). The lower operating margin is mainly due to the start in January 2004 of amortization of the UMTS license of TIM S.p.A.. Consolidated operating income for the first quarter of 2004 was adversely affected by this larger amortization amount of 34 million.

As of March 31, 2004, the TIM Group had a total of 47.6 million mobile lines, not including Telecom Italia Group mobile lines, an increase of 7.0% compared to December 31, 2003 (a total of 44.5 million mobile lines). The Brazilian mobile lines as of March 31, 2004, totaled 9.1 million (of which 3.5 million were GSM lines), an increase of approximately 800,000 mobile lines compared to the end of 2003.

As of March 31, 2004, the Mobile Business Unit had 18,936 employees, an increase of 48 units compared to December 31, 2003.

For TIM, operating revenues for the three months ended March 31, 2004 were 2,303 million, an increase of 154 million or 7.2% over the three months ended March 31, 2003. The growth in operating revenues is due not only to the positive trend in traffic revenues, totaling 1,718 million and up 3.3% compared to the first quarter of 2003 (1,663 million) but also to the significant contribution made by the growth in revenues from value-added services. The operating revenues from VAS amounted to 299 million, a 28.3% increase compared to the first quarter of 2003; in the first quarter of 2004 the ratio of operating revenues from VAS to total service revenues was 13.4% compared to 11.1% in the first quarter of 2003.

TIM Gross Operating Profit for the three months ended March 31, 2004 was 1,289 million, a 13.5% increase compared to the first three months of 2003 (1,136 million). Excluding the charges related to the TLC license fee recorded in the three months ended March 31, 2003 (29 million), the growth in Gross Operating Profit reached 10.6%.

TIM operating income amounted to 1,004 million and increased by 124 million or 14.1% compared to the first quarter of 2003 (880 million). Excluding the charges related to the TLC license fee recorded in the three months ended March 31, 2003, growth in operating income was 10.5%.

South America (Chile and Bolivia)

The following table sets forth, for the periods indicated, certain financial and other data for the Entel Chile group and Entel Bolivia group.

	Three Months ended March 31,	
South America (Chile and Bolivia)	**2003(1)**	**2004(1)**
	(millions of	

	Euro, except percentages and employees)	
Gross operating revenues	291	264
Gross operating profit	106	101
% of gross operating revenues	36.4	38.3
Operating income	41	37
% of gross operating revenues	14.1	14.0
Number of employees at period-end	(2) 4,953	4,981

(1) The data relating to the first quarter ended March 31, 2003 has been reclassified and presented consistent with the first quarter ended March 31, 2004 presentation.

(2) Number of employees at December 31, 2003.

South America gross operating revenues for the three months ended March 31, 2004 were 264 million, a decrease of 27 million or 9.3% compared to 291 million for the three months ended March 31, 2003. The decrease in gross operating revenues was mainly attributable to the reduction in the revenues of the wireline

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telecommunications services of the Entel Chile Group. The exchange rate fluctuations had a positive impact of approximately 8 million (a positive effect of 16 million for Chilean Peso partly offset by a negative effect of 8 million for the Boliviano). Excluding this effect, 35 million or a 12% of decrease would have been recorded.

Gross operating profit decreased by 5 million or 4.7% from 106 million in the three months ended March 31, 2003 to 101 million in the three months ended March 31, 2004. Excluding the positive effects of exchange rate fluctuations (2 million), organic decrease was 7 million, or 6.6%.

Gross operating margin increased from 36.4% in the three months ended March 31, 2003 to 38.3% in the three months ended March 31, 2004.

Operating income decreased by 4 million or 9.8% from 41 million in the three months ended March 31, 2003 to 37 million in three months ended March 31, 2004. The positive impact due to exchange rate fluctuations was 2 million.

The following table sets forth, for the periods indicated, certain financial data on a stand alone basis for Entel Chile group and Entel Bolivia group for wireline and mobile phone services.

	Three Months ended March 31,							
South America	**2003**				**2004**			
	(millions of Euro, except percentages)							
	Wireline	**Mobile**	**Elimination**	**Total**	**Wireline**	**Mobile**	**Elimination**	**Total**
Gross operating revenues	199	123	(31)	291	169	129	(34)	264
Gross operating profit	51	55		106	47	54		101
% of gross operating revenues	25.6	44.7		36.4	27.8	41.9		38.3
Operating income	9	32		41	6	31		37
% of gross operating revenues	4.5	26.0		14.1	3.6	24.0		14.0

Internet and Media (Telecom Italia Media Group)

The following table sets forth, for the periods indicated, certain financial and other data for the Internet and Media Business Unit. In order to allow a better understanding of the results of the businesses managed by the business unit, the figures for the first quarter of 2003 are presented on an historical and pro forma basis, taking into account both the Seat spin-off and the changes in the scope of consolidation.

Internet and Media (Telecom Italia Media Group)	Three Months ended March 31, 2003(1)	2003 Pro Forma (2)	2004
	(millions of Euro, except percentages and employees)		
Gross operating revenues	345	126	149
Gross operating profit	47	(2)	3
% of gross operating revenues	13.6	(1.6)	2.2
Operating loss	(35)	(29)	(24)
% of gross operating revenues	(10.1)	(23.4)	(15.9)
Number of employees at year-end	2,029(3)	2,029(3)	1,882

(1) First quarter 2003 historical financial and other data.
(2) The pro forma first quarter 2003 financial and other data have been prepared to be consistent with the 2004 scope of consolidation and taking into account the Seat Spin-off.
(3) Number of employees at December 31, 2003.

The gross operating revenues for the three months ended March 31, 2004 were 148.5 million, an increase of 22.8 million or 18.1% compared to 125.7 million for the pro forma three months ended March 31, 2003.

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The organic growth was mainly influenced by the performance of the Internet business area, which recorded a 32.1% increase in operating revenues and the Television business area, which recorded a 23.7% increase in operating revenues.

In particular gross operating revenues are analyzed as follows:

- the Internet business area made the largest contribution to growth with the related revenues increasing by 32.2% from 56.8 million for the pro forma three months ended March 31, 2003 to 75.1 million for the three months ended March 31, 2004. Such increase was due to the positive trend in use of the portal Virgilio and the Internet activities, and to the improvement of operating revenues related to ADSL products;

- revenues from the Television business area were 26.4 million for the three months ended March 31, 2004 compared to 21.3 million for the pro forma three months ended March 31, 2003, an increase of 5.1 million or 23.9% evidencing the success of the program schedule of the two stations which is attracting larger numbers of viewers;

- revenues from the Office Products and Services business area were 38.2 million for the three months ended March 31, 2004 and remained substantially stable with respect to the pro forma amounts of the corresponding period of the previous year.

Gross operating profit was 3.2 million in the three months ended March 31, 2004 compared to a gross operating loss of 2.0 million in the pro forma three months ended March 31, 2003, an increase of 5.2 million. The improvement was mainly due to the above mentioned increase in operating revenues.

Operating loss decreased by 5.8 million or 19.7% from 29.4 million in the pro forma three months ended March 31, 2003 to 23.6 million in three months ended March 31, 2004.

As of March 31, 2004, Internet and Media had 1,882 employees, with a reduction of 147 units compared to December 31, 2003.

Information Technology Market

The following table sets forth, for the periods indicated, certain financial and other data for the Information Technology Market Business Unit.

	Three Months ended March 31,		
	2003(1)	2003 Pro Forma (2)	2004

	(millions of Euro, except percentages and employees)		
Gross operating revenues	156	146	169
Gross operating profit	10	11	11
% of gross operating revenues	6.4	7.5	6.5
Operating income		1	3
% of gross operating revenues		0.7	1.8
Number of employees at year-end	(3) 4,827	(3) 4,827	4,806

(1) Historical financial and other data.

(2) The pro forma first quarter 2003 financial and other data has been prepared to be consistent with the 2004 scope of consolidation. As a result of this, NETikos Group, Domus Academy and Finsiel s Enterprise business segment, which were sold during 2003, have been excluded.

(3) Number of employees at December 31, 2003.

Gross operating revenues for the three months ended March 31, 2004 were 169 million, an increase of 23 million or 15.8% compared to 146 million for the pro forma three months ended March 31, 2003. The growth was mainly attributable to the increase in the revenues of TSF (Tele Sistemi Ferroviari), Agrisian and of Finsiel.

Gross operating profit amounted to 11 million in the three months ended March 31, 2004 and remained unchanged with respect to the pro forma amounts of the corresponding period of the previous year. However, gross operating margin decreased from 7.5% in the pro forma three months ended March 31, 2003 to 6.5% in the three months ended March 31, 2004.

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Operating income increased by 2 million from 1 million in the pro forma three months ended March 31, 2003 to 3 million in three months ended March 31, 2004. This increase was principally attributable to Finsiel and TSF.

As of March 31, 2004, the Information Technology Market Business Unit had 4,806 employees, with a reduction of 21 units compared to December 31, 2003.

Information Technology Group

The following table sets forth, for the periods indicated, certain financial and other data for the Information Technology Group.

Information Technology Group	Three Months ended March 31, 2003	Three Months ended March 31, 2004
	(millions of Euro, except percentages and employees)	
Gross operating revenues	229	225
Gross operating profit	11	15
% of gross operating revenues	4.8	6.7
Operating loss	(22)	(15)
% of gross operating revenues	(9.6)	(6.7)
Number of employees at period-end	(1) 4,107	4,053

(1) Number of employees at December 31, 2003.

Gross operating revenues for the three months ended March 31, 2004 were 225 million, a decrease of 4 million or 1.7% compared to 229 million for the three months ended March 31, 2003.

Gross operating profit increased by 4 million or 36.4% from 11 million in the three months ended March 31, 2003 to 15 million in the three months ended March 31, 2004. This improvement was principally due to the increase in the value of production (+ 20 million) arising from the advancement of development activities for Corporate and Wireline, partially offset by an increase of 12 million in operating expenses.

Gross operating margin increased from 4.8% in the three months ended March 31, 2003 to 6.7% in the three months ended March 31, 2004.

Operating loss decreased by 7 million from a loss of 22 million in the three months ended March 31, 2003 to a loss of 15 million in three months ended March 31, 2004.

As of March 31, 2004, the Information Technology Group had 4,053 employees, with a reduction of 54 units compared to December 31, 2003.

Olivetti Tecnost Group

The following table sets forth, for the periods indicated, certain financial and other data for the Olivetti Tecnost Business Unit.

	Three Months ended March 31,	
Olivetti Tecnost Group	**2003**	**2004**
	(millions of Euro, except percentages and employees)	
Gross operating revenues	158	144
Gross operating profit	2	7
% of gross operating revenues	1.3	4.9
Operating income (loss)	(5)	2
% of gross operating revenues	(3.2)	1.4
Number of employees at period-end	(1) 2,395	2,346

(1) Number of employees at December 31, 2003.

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Gross operating revenues for the three months ended March 31, 2004 were 144 million, a decrease of 14 million or 8.9% compared to 158 million for the three months ended March 31, 2003. Excluding the effect of exchange rate fluctuations and changes in the scope of consolidation (referring in particular to the termination of activities in Latin America), organic growth was 3.6% (an increase of 5 million).

Gross operating profit increased by 5 million from 2 million in the three months ended March 31, 2003 to 7 million in the three months ended March 31, 2004, principally due to the restructuring operations implemented during 2003 which resulted in a decrease in overheads. As a result, gross operating margin increased from 1.3% in the three months ended March 31, 2003 to 4.9% in the three months ended March 31, 2004.

Operating loss in the three months ended March 31, 2003 was 5 million compared with an operating income of 2 million in the three months ended March 31, 2004.

As of March 31, 2004, the Olivetti Tecnost Business Unit had 2,346 employees, with a reduction of 49 units compared to December 31, 2003.

Cautionary Statement for Purposes of the Safe Harbor Provisions of the United States Private Securities Litigation Reform Act of 1995.

The foregoing discussion in Item 5. Operating and Financial Review and Prospects and the following discussion under Item 11. Quantitative and Qualitative Disclosures About Market Risk contains forward-looking statements which reflect management s current views with respect to certain future events, trends and financial performance. Actual results may differ materially from those projected or implied in the forward-looking statements. Further, certain forward-looking statements are based upon assumptions of future events and trends which may not prove to be accurate. The following important factors could cause our actual results to differ materially from those projected or implied in any forward-looking statements:

- the continuing impact of increased competition in a liberalized market, including competition from global and regional alliances formed by other telecommunications operators in our core Italian domestic fixed-line and wireless markets;
- our ability to introduce new services to stimulate increased usage of our fixed and wireless networks to offset declines in the traditional fixed-line voice business due to the continuing impact of regulatory required price reductions, market share loss, pricing pressures generally and shifts in usage patterns;
- the level of demand for telecommunications services, particularly wireless telecommunications services in the maturing Italian market and for new higher value added products and services such as broadband;
- our ability to achieve cost-reduction targets in the time frame established or to continue the process of rationalizing our non-core assets;
- the success of our customer loyalty and retention programs, particularly in the fixed line business, and the impact of such programs on our revenues;
-

the impact of regulatory decisions and changes in the regulatory environment, including implementation of recently-adopted EU directives in Italy;

- the impact and consequences of the Merger;
- the impact of the slowdown in Latin American economies and the slow recovery of economies generally on our international business focused on Latin America and on our foreign investments and capital expenditures;
- the continuing impact of rapid or disruptive changes in technologies;
- the impact of political and economic developments in Italy and other countries in which we operate;
- the impact of fluctuations in currency exchange and interest rates;
- our ability to successfully implement our 2004-2006 Industrial Plan;
- our ability to successfully achieve our debt reduction targets;
- our ability to successfully roll out our UMTS networks and services and to realize the benefits of our investment in UMTS licenses and related capital expenditures;

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- our ability to successfully implement our internet and broadband strategy both in Italy and abroad;
- our ability to achieve the expected return on the significant investments and capital expenditures we have made and continue to make in Latin America;
- the amount and timing of any future impairment charges for our licenses, goodwill or other assets; and
- the impact of litigation or decreased mobile communications usage arising from actual or perceived health risks or other problems relating to mobile handsets or transmission masts.

The foregoing factors should not be construed as exhaustive. Due to such uncertainties and risks, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

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QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

The following discussion should be read in conjunction with the Summary of Accounting Polices in the Notes to the Consolidated Financial Statements and in conjunction with Note 29 of Notes to the Consolidated Financial Statements, which provides a summarized comparison of the nominal amounts, carrying values and market values of derivative and non-derivative financial instruments and other information relating to those instruments. In the normal course of business, the financial position of the Telecom Italia Group is subject to interest rate and foreign exchange rate risks. These market risks principally relate to the Telecom Italia Group s outstanding debt and non-Euro denominated assets and liabilities. The Telecom Italia Group uses derivatives mainly for the management of its debt positions, primarily interest rate swaps (IRS) and interest rate options (IRO) to reduce interest rate exposure on fixed-rate and floating-rate bank loans and bonds, and cross-currency and interest rate swaps (CCIRS) and currency forwards to convert various currency loans mainly in U.S. dollars into the functional currencies of the various subsidiaries. The following discussion is based on the amounts of indebtedness as derived from our Italian GAAP financial statements. See Note 29 of Notes to the Consolidated Financial Statements for a further discussion of items which, for purposes of U.S. GAAP, are considered to be debt.

Debt Policy

The Telecom Italia Group s debt used to support the financing of its domestic and international businesses contains an element of market risk from changes in interest and currency rates. With respect to interest rates applicable to medium and long-term debt, the Telecom Italia Group s policy is to utilize both floating rate and fixed rate with a different range of maturities. The Telecom Italia Group s policy is intended to optimize the cost of funding/risk exposure mix, utilizing as providers of funds domestic and international capital markets and supranational agencies such as the European Investment Bank. The Telecom Italia Group policies address the use of financial derivatives, including the approval of counterparties and the investment of excess liquidity. These policies are intended to minimize financial risks and obtain more favorable terms from the counterparts. In addition, Telecom Italia has a centralized treasury that provides assistance to its subsidiaries worldwide and usually operates as the Telecom Italia Group s main banker, allocating resources according to needs. The centralized treasury also gives support in negotiating credit lines and financial operations in general.

The table below sets forth, for the periods indicated, the aggregate principal amount of long-term debt (including current portion) payable in each year through 2008 and thereafter.

	2004	2005	2006	2007	2008	Thereafter	As of December 31, 2003 Total	As of December 31, 2002 Total
					(millions of Euro)			
Fixed Rate Debt	3,801	1,640	5,824	3,155	518	11,050	25,988	28,922
Floating Rate Debt	5,488	368	673	390	2,123	5,111	14,153	8,332
Total	**9,289**	**2,008**	**6,497**	**3,545**	**2,641**	**16,161**	**40,141**	**37,254**

As of December 31, 2003, the fair value of such outstanding debt amounted to approximately 42,689 million. The financial debt s market value is estimated on the basis of the present value as of December 31, 2003 of the future cash flows.

The table below sets forth, for the periods indicated, the aggregate principal amount of long-term debt outstanding at year-end (excluding current portion of long-term debt) and the average interest rate, broken down into fixed and floating.

	Year ended December 31,						
	2003	2004	2005	2006	2007	2008	Thereafter
	(millions of Euro, except for percentages)						
Long-Term Fixed Rate Debt	20,995	19,920	14,698	11,547	11,032	8,171	5,338
Average Fixed Rate	4.95%	4.77%	4.18%	5.01%	5.06%	4.78%	5.13%
Long-Term Floating Rate Debt Swapped into Fixed Rate Debt	1,162	600					
Average Swapped into Fixed Rate	3.01%	3.50%					
Average Total Fixed Rate	4.85%	4.73%	4.18%	5.01%	5.06%	4.78%	5.13%
Floating Rate Debt	8,567	8,218	7,561	7,186	5,074	4,063	4,041
Total Long-Term Debt	**30,724**	**28,738**	**22,259**	**18,733**	**16,106**	**12,234**	**9,379**

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As of December 31, 2003, approximately 86% of the Telecom Italia Group s long-term debt was denominated in Euro, while the remainder, 4,459 million, was denominated in foreign currencies primarily US dollars, Pound Sterling, Brazilian Reais, Chilean Peso and Japanese Yen. After taking into account the Company s derivative financial instruments, the Company s long-term debt is not materially exposed to fluctuations in foreign exchange rates. At December 31, 2003, approximately 35% of the long-term debt carried a floating rate.

Market Risk Policy

The Telecom Italia Group s policies regarding market risk consists of the following:

- the Centralized Treasury determines the maximum level of interest rate and foreign exchange rate risk to which the Telecom Italia Group should be exposed. An internal committee meets on a regular basis to monitor the activities and the level and value of the current market risk exposures. The Centralized Treasury, operating as a service center, supplies financial services and actively supports the Telecom Italia Group subsidiaries according to their requirements and local circumstances;
- the Telecom Italia Group uses derivative financial instruments to manage these financial market risks, and has established polices to handle and mitigate the adverse effects of these exposures; and
- the Telecom Italia Group continually evaluates the credit quality of counterparties to minimize the risk of non-performance. The counterparties to derivative contracts are generally highly rated banks and financial institutions and such counterparties are continually monitored in order to minimize the risk of non-performance.

Financial Instruments

Interest Rate and Foreign Exchange Risk Management

The Telecom Italia Group seeks to minimize market risk of its operating and financing activities and according to the evaluation of its exposures, selectively enters into derivatives instruments. Since Telecom Italia s corporate objective is pursued through its commercial operations, meaning the sale of telecommunications and media services, unwanted foreign exchange and interest rate exposures are normally hedged, provided the risks would affect Telecom Italia s cash flows.

The Telecom Italia Group is exposed to market risks arising from changes in interest rates, primarily in the Euro zone, in the United States and in Latin America. The Telecom Italia Group defines the optimal mixture of fixed and floating-rate debt in each currency and enters into financial derivatives to adjust the risk profile to the defined target mixture. Interest rate swaps IRS and IRO are therefore used to reduce the interest rate exposure on fixed-rate and floating-rate notes, bonds and bank loans. The Telecom Italia Group uses CCIRS and foreign currency forwards to convert foreign currency loans mainly in US dollars and Euro into the functional currencies of the various subsidiaries. As a result of these hedge activities, the Telecom Italia Group as of December 31, 2003 was not subject to any material foreign exchange risk in its financial debt nor in its commercial operations.

To determine the market value of the financial derivatives, the Telecom Italia Group uses various pricing models. The market value of interest rate swaps and of cross currency and interest rate swaps reflects the difference between the fixed rate to be paid/received and the interest rate (having the same expiry date as the swap) assessed on the basis of the market environment on the evaluation date. The market value of the cross currency and interest rate swaps depends also on the difference between the reference foreign exchange rate on the trade date and the foreign exchange rate on the valuation date.

With regard to IRSs and IROs, they involve or can involve the exchange of flows of interest calculated on the applicable notional principal amount at the agreed fixed or variable rates at the specified maturity date with the counterparties. This principal amount does not represent the amount exchanged between the parties and therefore does not constitute a measure of exposure to credit risk, which is instead limited to the amount of interest or interest differentials to be received at the interest date.

The same applies to CCIRSs which involve the exchange of capital, in the respective currencies of denomination, in addition to the settlement of periodic interest flows, at maturity and eventually at another date.

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Derivative instruments on debt positions

The following tables give a description of the Telecom Italia Group financial derivative contracts outstanding as of December 31, 2003 to manage the debt positions. The notional amount is net of compounded derivatives. Whenever a derivative is set up on another derivative, the notional amount is reported once and the net effect of the two compounded derivatives is considered. The notional amount of closed or maturing transactions (i.e.: transactions for which cash flows are certain) is not reported since cash flows are not at risk any longer. However the mark to market valuation includes the contribution of the above mentioned transactions.

	Notional amount/ Capital exchanged at 12/31/2003	Market value of derivatives at 12/31/2003 (a)	Market value of underlying debt positions at 12/31/2003 (b)	Market value of debt including related derivatives at 12/31/2003 (c)=(b-a)	Market value of derivatives at 12/31/2002
			(millions of Euro)		
Interest rate swaps and interest rate options	9,665	(16)	9,884	9,900	120
Cross-currency and interest rate swaps and Currency forward	4,217	(349)	4,063	4,412	38
Total	13,882	(365)	13,947	14,312	158

As of December 31, 2003, derivative instruments on debt positions, are classified as follows by maturity:

	2004	2005	2006	2007	2008	Thereafter	Total	Market value of underlying debt positions at 12/31/2003

					(millions of Euro)			
Derivatives on Debt Positions	2,710	843	1,234	1,300	1,100	6,695	13,882	13,947

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The following tables set forth a description of the Telecom Italia Group financial derivative contracts outstanding as of December 31, 2003 used to hedge debt positions.

Interest rate swaps and interest rate options

At December 31, 2003, the Telecom Italia Group companies had IRS and IRO contracts relating to financial liabilities recorded in the financial statements, for total principal equal to the notional principal amount of 9,665 million. Details of such contracts are set forth in the table below. References to CHF are to Swiss Francs.

	Maturities							
Interest Rate Derivatives	**2004**	**2005**	**2006**	**2007**	**2008**	**Thereafter**	**Total**	**Mark to Market**
				(millions of Euro)				
Euro Interest Rate Swaps								
Receive variable, pay fixed								
Amount	1	12	300				**313**	**-2**
Average pay rate	4.25%	4.71%	2.87%					
Average receive rate	Euribor 3 M	Euribor 3 M	3m Euribor					
Euro Interest Rate Swaps								
Receive variable, pay variable								
Amount	69	121	132				**322**	**2**
Average pay rate	6m Euribor + 24 bp	6m Euribor - 3 bp	6m Euribor - 2 bp					
Average receive rate	Rendiob, Euribor (1)	Rendiob, Bot, Rendistato(1)	Rendiob, Bot, Rendistato(1)					
Euro Interest Rate Swaps								
Receive fixed, pay fixed								
Amount						500	500	
Average pay rate						4.75% until Feb. 2004; 4.71% thereafter		
Average receive rate						5%(2)		
Amount						1,000	1,000	
Average pay rate						5.73%(3)		
Average receive rate						6.12%		
Amount						500	500	
Average pay rate						2.65%(4)		
Average receive rate						5%(5)		
Amount						500	500	
Average pay rate						6.06%(6)		
Average receive rate						7.25%(7)		
Amount						250	250	
Average pay rate						4.33% until Feb. 2004; thereafter 4.08%(8).		
Average receive rate						5%(9)		
Sub-total						**2,750**	**2,750**	**19**

CHF Interest Rate Swaps					
Receive fixed, pay variable					
Amount			64	**64**	**-6**
Average pay rate			6m CHF Libor + 230 bp.		
Average receive rate			5.62%		
Euro Interest Rate Swaps					
Receive fixed, pay variable					
Amount	1,500	450	750	2,700	
Average pay rate	2Y Euro swap in arrears + 178 bp	3 m Euribor + 362 bp (10)	CMS 2 Y Euro in arrears + 115.22 bp (11).		
Average receive rate	5.37%	6.5%	6.12%		
Amount			250	250	
Average pay rate			6m Euribor in arrears + 240.5 bp(12).		
Average receive rate			6.57%(13)		
Amount	500			500	
Average pay rate	3m Euribor in arrears + 159.3 bp (14)				
Average receive rate	5.37%				
Sub-total	**2,000**	**450**	**1,000**	**3,450**	**11**

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Interest Rate Derivatives	2004	2005	2006	2007	2008	Thereafter	Total	Mark to Market
				Maturities				
				(millions of Euro)				
Quanto Swaps								
Amount	200	500	600	350			**1,650**	**-30**
Average pay rate	2Y Usd CMS in arrears + 99 bp	2Y Usd CMS in arrears (15)	6m USD Libor + 94.5 bp (16)	6 m USD Libor in arr. + 331.6 bp (17)				
Average receive rate	5.37%	3m Euribor	3m Euribor	6.5% for each week in which 10Y $CMS>3.5 %				
USD Euro Quanto Spread Option								
Amount			200	500			**700**	**-8**
Average pay rate			3m Euribor + 59.5 bp (19).	5.19% (18)				
Average receive rate			3m Euribor + 125bp	6.5% (20)				
CHF Euro Quanto Spread Option								
Amount					250		**250**	**3**
Average pay rate					min (2*12m CHF arr., 12m Eur arr).			
Average receive rate					5.87%			
USD Interest Rate Swaps Receive variable, pay fixed								
Amount		107					**107**	**-4**
Average pay rate		5.0%						
Average receive rate		USD Libor						
USD Interest Rate Collar								
Amount		59					**59**	**-1**
Average cap strike rate (purchased)		7.1%						
Average floor strike rate (sold)		4.0%						
Total	**2,270**	**799**	**1,232**	**1,300**	**250**	**3,814**	**9,665**	**-16**

(1) Rolint, Robot, Rendint and Rendibot are customary domestic Italian measures for medium/long-term debt.
(2) With the additional sale of a cap at 7.10% on the six month Libor in USD effective from August 2007.
(3) Sale of a cap at 7.75% starting July 2007; sale of a floor at 3.25% starting July 2007.
(4) Starting February, 2005 the quarterly fixed rate (2.65%) could be replaced by the 3M Libor set in arrears whenever the latter exceeds 7%.
(5) Starting February, 2006: 5.00% for each week in which 5Y Euro Swap > 1Y Eur Swap.
(6) On 100 million 5.48% until April 2006 and thereafter 5.48% if 3m USD Libor <= 8% otherwise 3m USD Libor + 40.63 bp.
(7) Starting April 2005 7.25% accruing for each week in which 10Y CMS >= 2Y CMS.
(8) Alternatively, 3m GBP Libor in arrears -63.8 bp if 3m GBP Libor in arrears <= 7%.
(9) Starting February, 2005: 5% for each week in which (5Y USD CMS 5Y GBP CMS)<100 bp.
(10) 5.78% until January 2004, 5.86% until July 2004.

(11) Purchase of a cap at 5.29% set in arrears semiannually; sale of a cap at 7.75% on the 2Y USD swap rate set in arrears semiannually starting July 2005; sale of a floor with an annual rising rate from 3.25% to 4.25% set in arrears semiannually starting July 2004.
(12) 5.638% until Jan. 2004; 6 m Euribor + 263 bp from Jan. 2004 to Jul. 2004; purchase of a cap on 6 m Euribor at 4.15%; sale of a cap on 6 m USD Libor at 7.70%; sale of a floor on 6 m Euribor with an annual rising rate from 2.5% to 3.5%.
(13) Starting July 2005 6.575% for each week in which 5Y CMS > 1Y CMS.
(14) Sale of a floor for 450 million at 3.25%.
(15) 3,53% up to March, 2004.
(16) Starting January 2004 6 m USD Libor + 53.925 bp; purchase of a digital cap triggered when the semiannual rate in USD set in arrears is higher than 3.75%; sale of a cap at 4.25% on the semiannual rate in USD set in arrears; sale of a floor on the semiannual rate in USD set in arrears and with annual rising interest rates.
(17) 5.61% until April 2004.
(18) Starting April 2004, the higher between 6 m Euribor in arrears and 6 m USD Libor in arrears, + 216.32 bp.
(19) Starting January 2004, the higher between 12 m Euribor in arrears and 12 m USD Libor in arrears, + 52.5 bp.
(20) Starting April 2004 6.5% for each week in which 10Y $ CMS > 3.5%.

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Cross-currency and interest rate swaps and Currency forward

At December 31, 2003, the Telecom Italia Group companies had CCIRS and Currency Forward contracts relating to financial liabilities recorded in the financial statements, for total principal equal to a notional principal amount of 4,217 million. Details of such contracts are set forth in the table below. References to JPY are to Japenese Yen, BRL to Brazilian Reais, CLP to Chilean Pesos, and PEN to Peruvian Nuevo Sol.

	Maturities							
Foreign Exchange Derivatives	**2004**	**2005**	**2006**	**2007**	**2008**	**Thereafter**	**Total**	**Mark to Market**
	(millions of Euro)							
CCIRS								
Receive fixed USD, pay variable Euro								
Amount					851		**851**	**-63**
Average pay rate					3m Euribor +52.9 bp			
Average receive rate					4.0%			
CCIRS								
Receive fixed USD, pay fixed Euro								
Amount						2,558	**2,558**	**-233**
Average pay rate						5.4%		
Average receive pay						5.6%		
CCIRS								
Receive dual currency (fixed USD rate, JPY principal at maturity), pay fixed Euro(2)								
Amount						174	**174**	**-20**
Average pay rate						6.08%(1)		
Average receive rate						5.0%		
CCIRS								
Receive fixed Yen, pay variable Euro(2)								
Amount						148	**148**	**6**
Average pay rate						6m Euribor + 224 bp		
Average receive rate						3.6%		
CCIRS								
Receive variable GBP, pay variable Euro								
Amount	79						**79**	**-6**
Average pay rate	3m Euribor + 11 bp							
Average receive rate	3m GBP Libor +10 bp							
CCIRS								
Receive fixed USD, pay variable BRL								
Amount	51	17	2				**70**	**3**
Average pay rate	CDI(3)	CDI(3)	CDI(3)					
Average receive rate	exchange rate variation + spread	exchange rate variation + spread	exchange rate variation + spread					
Currency Forwards Buy USD, Sell CLP								
Amount	151						**151**	**-12**
Average Contractual Exchange Rate	649							

Currency Forwards Buy USD, Sell UF(4)								
Amount	118	10					**128**	**-22**
Average Contractual Exchange Rate	0.042	0.042						
Currency Forwards Buy USD, Sell PEN								
Amount	41	17					**58**	**-2**
Average Contractual Exchange Rate	3.5	3.5						
Total	**440**	**44**	**2**	**0**	**851**	**2,880**	**4,217**	**-349**

(1) 6.13% until October, 2004.
(2) The cross currency protection structure is conditional on Telecom Italia S.p.A. being in good standing.
(3) The CDI is the customary domestic Brazilian measure of overnight interest rate. As of December 31, 2003 this rate was around 16.27%.
(4) The UF (Unidad de Fomento) is the customary domestic Chilean measure of interest rates linked to the inflation rate.

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Derivative instruments on financial assets and on short-term treasury operations

The Telecom Italia Group also entered into derivative contracts to manage the interest rate and foreign currency risk on its financial assets (bonds, bonds bought back and intercompany loans) and on short-term treasury operations for a principal amount of approximately 1,529 million.

Description	Equivalent notional amount (millions of euro)
Currency Forward transactions finalized by Olivetti International S.A.	294
Currency Forward transactions finalized by Olivetti Finance N.V. (on bonds of Japanese yen 20 billion 2002/2032)	162
Currency Forward transactions finalized by Telecom Italia Finance S.A.	190
Currency Forward transactions finalized by Telecom Italia S.p.A.	241
Currency Forward transactions finalized by TIM S.p.A.	7
IRS and Currency Forward transactions finalized by Telecom Italia Finance, Olivetti Finance N.V. and Olivetti International S.A.	635
Total	**1,529**

The market value of derivatives on financial assets and short-term treasury operations as of December 31, 2003 was a net realized loss of approximately 13 million compared to a net realized gain of 53 million as of December 31, 2002. Such market value has been measured by discounting at December 31, 2003, for each transaction, the product between (i) the amount purchased/sold and (ii) the difference between the contractual exchange rate and the forward exchange rate as of December 31, 2003 having the same maturity date.

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Item 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

Directors

The following are the members of the Board of Directors of Telecom Italia as of June 1, 2004. All of them were elected at the Telecom Italia shareholders meeting held on May 6, 2004 for a three-year term, which will expire at the annual shareholders meeting to be called to approve the Company s financial statements for the year ended December 31, 2006. At the May 6, 2004 shareholders meeting the number of directors was set at 19.

Name	Age	Position	Appointed
Marco Tronchetti Provera	56	Chairman(1)	2004
Gilberto Benetton	62	Deputy Chairman(1)	2004
Carlo Orazio Buora	58	Managing Director(1)	2004
Riccardo Ruggiero	43	Managing Director General Manager(2)	2004
Paolo Baratta(3)	64	Director	2004
John Robert Sotheby Boas(3)	67	Director	2004
Giovanni Consorte	56	Director	2004
Domenico De Sole(3)	60	Director	2004
Francesco Denozza(3)	56	Director	2004
Luigi Fausti(3)	74	Director	2004
Guido Ferrarini(3)	53	Director	2004
Jean Paul Fitoussi(3)	62	Director	2004
Gianni Mion	60	Director	2004
Massimo Moratti	58	Director	2004
Marco Onado(3)	63	Director	2004
Renato Pagliaro	47	Director	2004
Pasquale Pistorio(3)	68	Director	2004
Carlo Alessandro Puri Negri	51	Director	2004
Luigi Roth(3)	63	Director	2004

(1) Appointed by the Board of Directors on May 6, 2004.
(2) Appointed as General Manager by the Board of Directors on August 4, 2003. Appointed as Managing Director by the Board of Directors on May 6, 2004.
(3) Independent Director. For details on the criteria applied to determine independence, see Item 10. Additional Information Corporate Governance Board of Directors Independent Directors .

As of June 1, 2004, the Secretary of the Board of Directors was Francesco Chiappetta.

According to article 13 of the Bylaws, the Board set up two committees from among its members: the Internal Control and Corporate Governance Committee and the Remuneration Committee. Both these committees are charged with giving advice and making proposals to the Board as a whole.

The members of the Internal Control and Corporate Governance Committee are Guido Ferrarini, Francesco Denozza, Domenico De Sole and Marco Onado.

The members of the Remuneration Committee are Luigi Fausti, Pasquale Pistorio and Paolo Baratta.

For a detailed description of Telecom Italia s corporate governance, including activities, responsibilities and organization of the Board of Directors, see Item 10. Additional Information Corporate Governance .

Biographical Data

The following are the selected biographical data of the Directors.

Marco Tronchetti Provera: Marco Tronchetti Provera was born in Milan, in 1948. Mr. Tronchetti Provera has been Telecom Italia Chairman since September 27, 2001. Mr. Tronchetti Provera began his career in 1973 working in the family maritime transport business and establishing a financial holding company. In 1986 he joined the Pirelli Group, a world leader in the production of tyres, energy and telecommunications infrastructure. In 1992 he took over responsibility for operations. Mr. Tronchetti is also Chairman of Pirelli & C. S.p.A., of Olimpia S.p.A. and of Camfin S.p.A., Deputy Chairman of Confindustria, a Director of Luigi Bocconi University, of Teatro alla Scala Foundation, Chairman of the Council for Relations between Italy and the United States, of the Silvio Tronchetti Provera Foundation, member of the European Round Table of Industrialists, of the Italian Group of the Trilateral Commission, of the International Advisory Board of Allianz, of the

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International Council of J.P. Morgan, of the New York Stock Exchange European Advisory Committee and of the Assonime Steering Committee.

Gilberto Benetton: Gilberto Benetton was born in Treviso, in 1941. Mr. Benetton has been Telecom Italia Deputy Chairman since September 27, 2001. He began his activity in 1965 with his brothers Giuliana, Luciano and Carlo. The Benetton Group is now active in 120 countries in the world. Mr. Benetton is also Deputy Chairman of Olimpia S.p.A, Chairman of Edizione Holding S.p.A., Autogrill S.p.A., Ragione s.a.p.a., Verde Sport S.p.A., Vice Chairman of Fondazione Benetton, Director of Benetton Group S.p.A., Area Nord Concessionaria di Pubblicità, Banca Antonveneta, Pirelli S.p.A., Mediobanca S.p.A., Schemaventotto S.p.A., Sep S.p.A., HMS Host Corp., Lloyd Adriatico S.p.A., Autostrade S.p.A., Beni Stabili S.p.A., and Abertis Infraestructuras S.A..

Carlo Orazio Buora: Carlo Orazio Buora was born in Milan, in 1946. Mr. Buora has been Chief Executive Officer of Telecom Italia since November 7, 2001, and currently is Chairman of TIM S.p.A. He is also Managing Director of Pirelli & C. S.p.A. He began working in finance with the BNL Group. Afterwards he became head of Finance and Administration at Merloni Finanziaria and Chief Financial Officer at Snia Viscosa. In 1984 he joined the Fiat Group. In 1989 he was appointed Deputy General Manager of Telettra and subsequently General Manager of the Benetton Group, a position he held until 1991. In November 1991 he joined the Pirelli Group as central manager for finance and administration and was appointed General Manager in 1992. In 1999 he became a general partner of Pirelli & C. S.a.p.a. and in 2001 was appointed Managing Director of Pirelli & C. S.p.A. Mr. Buora is also a Director of Pirelli & C. Real Estate S.p.A., of Olimpia S.p.A., of RCS Mediagroup S.p.A., of Ras S.p.A., and of Mediobanca S.p.A. Mr. Buora has been Deputy Chairman of F.C. Internazionale S.p.A. since January 2004.

Riccardo Ruggiero: Riccardo Ruggiero was born in Naples, Italy, in 1960. Since October 1, 2001 Mr. Ruggiero has been Head of the Telecom Italia Group Wireline Business Unit. On May 7, 2002 he was appointed General Manager of Telecom Italia and on September 5, 2002 he was appointed Managing Director. He began his career in 1986 as sales manager of Fininvest S.p.A. Between 1988 and 1990 he was sales and marketing manager of the Italian branch of AT&T. In 1990 he joined the Olivetti Group, where he held various positions: in 1992 he was appointed Vice President of Organizzazione Oliservice, with responsibility for international clients and the commercial development of telecommunications services worldwide, and in 1994 of Olivetti Telemedia, with responsibility for commercial development and market expansion. In 1996 he was appointed managing director of Infostrada S.p.A. (with responsibility for the market, infrastructure and personnel functions) and was later appointed Managing Director of Italia On Line. In July 2001, Mr. Ruggiero joined the Telecom Italia Group as Head of the Telecom France Business Unit, with the brief of managing and developing Group business on the French market through the company s participating interests.

Paolo Baratta: Paolo Baratta was born in Milan in 1939. Mr. Baratta has been Director of Telecom Italia since May 6, 2004. In 1967 he began doing economic research at the Associazione per lo sviluppo dell industria nel Mezzogiorno (Svimez) in Rome. In 1979 he became a Director of the Istituto per il Credito alle Imprese di Pubblica Utilità (ICIPU) and then Deputy Chairman. From 1980 to 1992 he was Chairman of ICIPU, Consorzio di Credito per le Opere Pubbliche (CREDIOP), Deputy Chairman of Nuovo Banco Ambrosiano (later Banco Ambrosiano Veneto) and the Italian Bankers Association (ABI). In addition to being a Director of various companies, he was Chairman of the Centro Beneduce per gli Studi in Campo Bancario e Assicurativo. In 1993 he became Minister for Privatizations with responsibility for the reorganization of the system of state holdings. In 1993-94 he was Minister for Foreign Trade and Minister for Industry ad interim. In 1995-96 he was Minister for Public Works and Minister for the Environment. From 1997 to 2000 he was chairman of Bankers Trust S.p.A. and from 1998 to 2000 Chairman of the Venice Biennale. He is a member of the Società Italiana degli Economisti and currently is Chairman of the Comitato Venezia Internazionale, the Centro per la Proprietà Intellettuale di Venezia and the Fondazione Lorenzo Valla. He is also a Director of Banca Finmat Euroamerica, Svimez-Roma, the Fondo per l Ambiente Italiano (FAI) and the Istituto per gli Studi Storici in Naples.

John Robert Sotheby Boas: John Robert Sotheby Boas was born in London in 1937. Mr. Boas has been Director of Telecom Italia since May 6, 2004. He joined Price Waterhouse & Co. in 1964 as a chartered accountant. From 1965-66 he worked for ICI in the Overseas Treasurer s Department and in 1966 he moved to SGWarburg & Co., where he was concerned with mergers and acquisitions, IPOs and bond issues. He was appointed Director in 1971 and Deputy Chairman in 1990. During the 1990s he worked on developing the company s business in continental

Europe, with specific responsibility for Italy. Following the acquisition of SGWarburg by Swiss Bank Corporation, he was Managing Director of SBC Warburg until he retired in 1997. He continued to act as a consultant for UBS Warburg until April 30, 2004. At present he is a non-executive Director of Invesco Continental Smaller Companies Trust PLC.

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Giovanni Consorte: Giovanni Consorte was born in Chieti, in 1948. Mr. Consorte has been Director of Telecom Italia since August 4, 2003. He began working in 1973 with the Montedison Group in the analysis, budget and investment control field. In 1976 he was hired by the Cooperatives League, where he coordinated projects for reorganization and change management at consumer cooperatives and the development of new business initiatives. In 1979 he joined the Planning, Organization and Control Department of Unipol Assicurazioni S.p.A. Where he was promoted from manager to central manager and subsequently to general manager. He was subsequently appointed Deputy Chairman and Managing Director and, in July 1996, Chairman and Managing Director. In addition to the positions of Chairman and Managing Director of Unipol Assicurazioni and Finsoe S.p.A., he is Deputy Chairman and Managing Director of Unipol Banca S.p.A. and Unipol Merchant Banca per le Imprese, Chairman of MeieAurora S.p.A., Deputy Chairman of Winterthur Assicurazioni S.p.A., Winterthur Vita S.p.A. and Hopa S.p.A.; he is also a Director of Carisbo S.p.A., Snia S.p.A., Sorin Group, Euresa Holding S.p.A. and as from 2003 Telecom Italia. Mr. Consorte is a member of the Executive Committee of A.N.I.A. (the Italian Association of Insurance Companies), the Management and Board of the Lega Nazionale Cooperative e Mutue, and the Scientific Committee of Nomisma. He is also a member of the General Council of Assonime (the Association for Italy s Limited Liability Companies) and a Director of the Ramazzini European Foundation.

Domenico De Sole: Domenico De Sole was born in Rome in 1944. Mr. De Sole has been Director of Telecom Italia since May 6, 2004. In 1970 he moved to the United States, where he became a partner with the law firm Patton, Boggs & Blow. In 1984 he joined the Gucci Group as Chief Executive Officer of Gucci America Inc. and in 1995 he became head of operations for the entire Gucci Group as President and Chief Executive Officer of Gucci Group NV until April 2004. During this period Gucci Group was listed on the New York and Amsterdam stock exchanges (1995), beat off a hostile takeover bid (1999), acquired Yves Saint Laurent, Sanofi Beauté and Sergio Rossi in 1999, Boucheron, Alexander McQueen and Bedat & Co in 2000 and Bottega Veneta, Stella McCartney and Balenciaga in 2001. Mr. De Sole is a Director of Procter & Gamble (member of Audit and Governance and Nominating Committees) and Bausch & Lomb (member of Audit and Management Committees). He is a member of the Advisory Board of the Harvard Law School.

Francesco Denozza: Francesco Denozza was born in Turin, in 1946. Mr. Denozza has been Director of Telecom Italia since November 7, 2001. Mr. Denozza is also Professor of Commercial Law at the University of Milan, lawyer and Co-editor of the legal review Giurisprudenza Commerciale . Mr. Denozza is author of several publications.

Luigi Fausti: Luigi Fausti was born in Ancona, in 1929. Mr. Fausti has been Director of Telecom Italia since November 7, 2001. He is also Director of MONRIF S.p.A., of Poligrafici Editoriale S.p.A. di Bologna and Chairman of Patrimonio Immobiliare dello Stato S.p.A. Mr. Fausti began his career in 1947 in Banca Commerciale Italiana where he was Executive Officer and General Director of several branches and in 1990 he became Chief Executive Officer of the bank, in 1994 Vice-Chairman and Chief Executive Officer, in 1997 Chairman and in 1999 Honorary Chairman. He received an honoris causa economics degree from Naples University.

Guido Ferrarini: Guido A. Ferrarini was born in Genoa in 1950. Mr. Ferrarini has been Director of Telecom Italia since June 12, 2001. Mr. Ferrarini is also Director of Autostrade S.p.A. and Deputy Chairman of the European Corporate Governance Institute, Bruxelles. He is professor of Financial Markets Law at the University of Genova School of Law, Director of Center of Law and Finance, legal expert and lawyer, Member of Board of Trustees IASC Foundation of London, Advisor of the Corporate Governance Committee of Borsa Italiana S.p.A., Chairman of TLX S.p.A. (a new Italian investment exchange), Co-director of Rivista delle Società (Giuffrè) and honorary professor of University College School of Law, London. Mr. Ferrarini is the author of several publications.

Jean Paul Fitoussi: Jean-Paul Fitoussi was born in la Goulette (Tunisia) in 1942. Mr. Fitoussi has been Director of Telecom Italia since May 6, 2004. Mr. Fitoussi is Professor of Economics at the Institut d Études Politiques in Paris, where has taught since 1982 and whose Scientific Committee he now chairs. He is currently President of the Observatoire Français des Conjonctures Economiques (OFCE), an economic research and forecasting institute. Mr. Fitoussi graduated *cum laude* in Law and Economics from the University of Strasbourg with a thesis on inflation, equilibrium and unemployment. He began his academic career as an assistant professor at the University of Strasbourg. Between 1979 and 1983 he taught at the European University Institute, Florence, and in 1984 was visiting professor at the University of California, Los Angeles. Since 1998 he has been a member of the board of the École Normale Supérieure. In 1997 he became a member of the Prime Minister s Council for Economic Analysis. In 1996 he was named to the Commission Économique de la Nation. He was secretary of the International Economic

Association beginning in 1984 and has been an expert for the Economic and Monetary Committee of the European Parliament. Between 1990 and 1993 he was Chairman of the Economic Council of the European Bank for Reconstruction and Development. In the field of publishing, Mr. Fitoussi is managing editor of the Revue et Lettre de L OFCE and serves on the scientific committee of the Revue Française d Economie, the editorial board of Labour and of The International Journal of Development Planning Literature, and the scientific committee of International Labour Review and Critique Internationale. His writing appears regularly in newspapers in France and abroad and he is commentator for La Repubblica and Le Monde. Since 2002 he has been Director of the Fondation Nationale des Sciences Politiques. In the field of research, Mr. Fitoussi has concentrated on inflation theory, unemployment, foreign trade and the role of macroeconomic policy. As president of the OFCE and founder of its International Economic Policy Group (of which he is a member alongside Anthony Atkinson, Olivier Blanchard, John Flemming, Edmond Malinvaud, Edmund Phelps and Robert Solow), he has made numerous contributions to the current economic policy debate, particularly on the issues of economic integration and transition.

Gianni Mion: Gianni Mion was born in Vó, a town near Padua, in 1943. Mr. Mion has been Director of Telecom Italia since November 7, 2001. He is currently Vice President of TIM S.p.A., Director of Telecom Italia Media S.p.A. and Olimpia, Chief Executive Officer of Edizione Holding S.p.A., Director of Benetton Group S.p.A., Autogrill S.p.A., 21 Investimenti, Autostrade S.p.A., Sagat S.p.A., and Banca Antonveneta S.p.A. Mr. Mion is also a Registered Auditor.

Massimo Moratti: Massimo Moratti was born in Boscochiesanuova, a town near Verona, in 1945. Mr. Moratti has been Director of Telecom Italia since November 7, 2001. He is also Director of Angelo Moratti di Gianmarco e Massimo Moratti & C. S.a.p.a., Chief Executive Officer of Saras S.p.A. Raffinerie Sarde, Chairman of Sarint S.A., Director of Interbanca S.p.A., and of Pirelli S.p.A..

Marco Onado: Marco Onado was born in Milan in 1941. Mr. Onado has been Director of Telecom Italia since May 6, 2004. He was a professor at the University of Modena from 1972 to 1984, then at the University of Bologna until 2001. Currently he teaches at Bocconi University. He has been a Visiting Professor at the University College of North Wales and Brown University in Providence, Rhode Island. From 1993 to 1998 he was a CONSOB Commissioner and in this capacity he was a member of the Draghi Committee for the reform of company law and of the Euro Committee. He also participated in the work of the International Organization of Securities Commissions (IOSCO). He was also a member of the Preda Committee, which drafted the Code of Conduct for listed companies in 2000 and the updated version in 2002. He is a member of the Società Italiana degli Economisti, the Scientific Committee of the Ente per gli Studi Monetari, Bancari e Finanziari Luigi Einaudi, and Prometeia Associazione per le Previsione Econometriche. He also sits on the editorial board of several specialized reviews and is a columnist for the financial newspaper Il Sole 24 Ore . During his career he has been a director of various financial institutions. At present he is a member of the Council of the Consiglio Nazionale dell Economia e del Lavoro (CNEL), designated by the President of the Republic.

Renato Pagliaro: Renato Pagliaro was born in Milan in 1957. Mr. Pagliaro has been Director of Telecom Italia since May 6, 2004. A registered auditor, in 1981 he joined Mediobanca Banca di Credito Finanziario S.p.A., where he has held positions of increasing responsibility. In April 2003 he was appointed Co-General Manager and Secretary to the Board of Directors of Mediobanca. Mr. Pagliaro is a Director and member of the Executive Committee of RCS Mediagroup S.p.A. and Compass S.p.A. He is also a Director of Ferrari S.p.A., SelmaBipiemme Leasing S.p.A. and Cofactor S.p.A.. Since 1993 he has been a member of the Board of Auditors of Istituto Europeo di Oncologia S.r.l..

Pasquale Pistorio: Pasquale Pistorio was born in Agira, Enna Province, in 1936. Mr. Pistorio has been Director of Telecom Italia since May 6, 2004. Mr. Pistorio graduated in Electronic Engineering, with a specialization in electronics from the Polytechnic Institute of Turin in 1963. He began his career as a salesman and in 1967 he joined Motorola in Italy, rising through the ranks to become Director of International Marketing in 1977. Based in Phoenix, Arizona, he was appointed Vice President of Motorola Corporation and in 1978 he was promoted to General Manager of Motorola s International Semiconductor Division, responsible for the design, manufacturing and marketing activities for all regions outside of the United States. In July 1980 Mr. Pistorio returned to Italy to become President and Chief Executive Officer of the SGS Group, Italy s only microelectronics company. His success in transforming the company into a profitable, versatile maker of semiconductors led the SGS Group in May 1987 to its merger with Thomson Seminconducteur to form SGS-Thomson Microelectronics. As President and Chief Executive Officer of the new company, Mr. Pistorio was responsible for developing a diversified portfolio of products concentrated on high-growth applications and creating a global network of strategic alliances. The company was listed on the New York and Paris stock exchanges in December 1994 and in Milan in June 1998. He currently serves on the board of MEDEA+, the European programme for advanced technological research that is the successor to MEDEA (Microelectronics for

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European Applications), and of JESSI (Joint European Sub-micron Silicon Initiative). Mr. Pistorio has been an ardent environmentalist throughout his career: his advocacy of the social responsibility of business also extends to his efforts against the Digital Divide. As a member of the Information and Communications Task Force created by the United Nations, he is helping to develop proposals to draw firms attention and resources to meeting this new global challenge.

Carlo Alessandro Puri Negri: Carlo Alessandro Puri Negri was born in Genoa, in 1952. Mr. Puri Negri has been Director of Telecom Italia since November 7, 2001. Mr. Puri Negri is also Director of Aon Italia S.p.A., Grandi Stazioni S.p.A., Olimpia S.p.A. and Permasteelisa S.p.A.. He is Deputy Chairman and Chief Executive Officer of Pirelli & C. Real Estate S.p.A., Deputy Chairman of Camfin S.p.A. and Pirelli & C. S.p.A. and is Chairman of Pirelli & C. Ambiente S.p.A. Since 2003 Mr. Puri Negri has been a Director of Istituto Europeo di Oncologia S.r.l. and a member of Real Estate Int. Advisory Board of Harvard University. He is also Director and Executive Committee member of Capitalia S.p.A..

Luigi Roth: Luigi Roth was born in Milan in 1940. Mr. Roth has been Director of Telecom Italia since May 6, 2004. He began his career with various tasks in the Pirelli Group, which he left to join Metropolitana Milanese as head of the Planning Department. From 1980 onwards he ran a number of medium-sized firms in the manufacturing and property sectors as General Manager or Managing Director. From 1986 until 1993 he was Managing Director of Finanziaria Ernesto Breda S.p.A. and then, until 2001, Chairman and Managing Director of Breda Costruzioni Ferroviarie S.p.A. In addition, from 1996 to 1998 he was also Chairman of Società Ferrovie Nord Milano S.p.A. and Società Ferrovie Nord Milano Esercizio S.p.A. From May 1998 to December 2000, Mr. Roth was also managing director of Ansaldo Trasporti S.p.A. and set up the Transport Sector of Finmeccanica S.p.A. In January 2001 he became Chairman of the Milan Fair Foundation, which controls Fiera Milano S.p.A. and Sviluppo Sistema Fiera. He is Chairman of CartaFacile S.p.A., Deputy Chairman of Cassa Depositi e Prestiti S.p.A. and Director of IntesaBCI Gestione Crediti S.p.A., Banca BMB S.p.A. and Bocconi University in Milan.

Executive Officers

As of May 31, 2004, the executive officers of Telecom Italia and their respective ages, positions and year of appointment as executive officers were as follows:

Name	Age	Position	Appointed
Marco Tronchetti Provera	56	Executive Chairman (1)	2001
Carlo Orazio Buora	58	Managing Director (1)	2001
Riccardo Ruggiero	43	Managing Director (1)	
		General Manager of Telecom Italia	2002
			2002
		Head of Wireline Business Unit	2001
Giuseppe Sala	46	General Manager of Telecom Italia	2003
Central Functions:			
Gustavo Bracco	56	Head of Human Resources	2001
Enrico Parazzini	60	Head of Finance, Administration and Control	2001
Francesco Chiappetta	43	General Counsel	2002
Germanio Spreafico	51	Head of Purchasing	2001
Business Units:			
Enrico Parazzini	60	Head of Internet and Media Business Unit	

		Managing Director of Telecom Italia Media	2003
Marco De Benedetti	41	Head of Mobile Business Unit	2003
		Managing Director of TIM	1999
			1999
Giuseppe Nino Tronchetti Provera (2)	36	Head of Information Technology Market Business Unit	2002
		Deputy Chairman of Finsiel	2002

(1) Confirmed in the office by the Board of Directors on May 6, 2004.

(2) As of June 1, 2004 Salvatore Pinto took over as Head of the Information Technology Market Business Unit.

The following are the selected biographical data of the executive officers, other than Directors:

For the biographical data of Mr. Ruggiero please see above under Directors .

Gustavo Bracco: Mr. Bracco was born in Turin, Italy, on May 18, 1948. On October 1, 2001, he became Head of Telecom Italia Group Human Resources. Mr. Bracco began his career at Fiat in 1972, working for the

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Trade Union Relations Central Management. In 1976, he was appointed Personnel Manager at the Mirafiori factory. In 1977, he transferred to Toro Assicurazioni as Head of Industrial Relations and Labour Disputes, under the aegis of Central Personnel Management. He joined the Turin Industrial Union in 1979, where he worked until 1982, initially at the Research Office before moving to the Trade Union Service, where he rose through the ranks to the position of Head. Between 1983 and 1987, he worked at Cinzano, Saiag and Carello, with responsibility for Personnel and External Relations. In 1988, he returned to the Fiat Group as Head of Personnel and Organization at the Engine Control Division. He took on the same role at CEAC in 1991 and at Fidis in 1994. He was appointed Head of Group Trade Union Relations in 1996. In 1998, Mr. Bracco went to work in London for New Holland as Head of Personnel and Organization, a position he subsequently filled in Chicago for Case-New Holland. He joined Pirelli in December 2000 as Group Head of Human Resources.

Francesco Chiappetta: Mr. Chiappetta was born in Rome, Italy, on September 13, 1960. Mr. Chiappetta was appointed Telecom Italia S.p.A General Counsel on August 1, 2002. He is also the Secretary to the Telecom Italia Board of Directors. Mr. Chiappetta began his career in 1983 at CONSOB, Italy s stock market and corporate regulatory body. Over the next ten years he held a number of positions at this organization, including Chief of the Regulation Office. Between 1998 and July 2001 he worked as Deputy General Manager for Assonime, the Association of Italian corporations, with responsibility for company law and capital market. In August 2001 he joined the Pirelli & C. Group as Head of Legal and Corporate Affairs, a position he filled until joining the Telecom Italia Group. From 1989 to 2003 he worked in academia, holding courses and lectures at leading Italian universities including La Sapienza in Rome, Università di Roma Tre and the Luigi Bocconi University in Milan. Mr. Chiappetta has widely published both on company and securities law. At the present time he his also Chairman of the Company Law Working Group of Unice (Union of Industrial and Employers Confederation of Europe).

Marco De Benedetti: Mr. De Benedetti was born in Turin, Italy on September 9, 1962. On July 2, 1999 he was appointed TIM Chief Executive Officer. Mr. De Benedetti began his career with the marketing department of Procter & Gamble. From 1987 to 1989, he worked in Merger and Acquisitions for Wasserstein, Perella & Co., a New York merchant bank. He joined Olivetti in 1990 as assistant to the Chief Executive Officer of Olivetti System & Networks. He was later promoted to Marketing and Services Manager. In December 1992, he was appointed General Manager of Olivetti Portugal. In September 1994, he became Chief Executive Officer of Olivetti Telemedia, subsequently also taking on the chairman s role. In October 1996, he was named Chairman of Infostrada. In 1997, he was appointed Chief Executive Officer. Since March 1998 he has served as Olivetti Group Central Manager for Telecommunications Strategies. Mr. De Benedetti is also Chairman of TIM Brasil Serviços e Partecipaçoes S.A., Director of TIM International N.V., TT & TIM, Iletisim Hizmetleri A.S., Telecom Italia America Latina S.A., and also Director of Cofide S.p.A..

Enrico Parazzini: Mr. Parazzini was born in Milan, Italy, on March 18, 1944. He became Head of Telecom Italia Group Finance, Administration and Control on October 1, 2001. Mr. Parazzini began his career in 1968 as a Junior Auditor at Arthur Andersen. In 1969, he was hired by the Finance Department at General Electric. In 1970, he joined Honeywell Information Systems Italia. Over the next 20 years he was promoted through the company, holding the positions of Financial Planning Manager from 1975 to 1980, Administration and Control Manager from 1981 to 1986, and Chief Financial Officer from 1987 to 1990. In 1991, after Honeywell sold its business to the Bull Group, Mr. Parazzini was appointed General Manager of Administration, Control, IT Systems and Logistics. He joined Pirelli as Group Controller in May 1992. He took active part in the process of group restructuring, with special reference to reform of the planning and control system. Between 1996 and 1999, he was Head of Administration, Group Acquisitions and Risk Management. He was appointed Chief Financial Officer of the Cables and Systems division in 2000. Mr. Parazzini is currently Managing Director of Telecom Italia Media, Chairman of Telecom Italia International, Holding Media e Comunicazione, LA 7 Televisioni, MTV Italia, Matrix, Webfin Finanziaria Web and Board member of TM news, TI Latam, Finsiel, TI Audit, Italtel Holding, Italtel. Since 1994 he has worked as a visiting lecturer on the Multinational Group Planning and Control Course at the Luigi Bocconi University of Milan.

Giuseppe Sala: Mr. Sala was born in Milan, Italy, on May 28, 1958. Mr. Sala was appointed General Manager of the Wireline Business Unit of Telecom Italia on June 16, 2003. In 1994 he was appointed Head of Strategic Planning and Control of Pirelli s Tyres Sector. In 1998, Mr. Sala became Managing Director of Italian Tyres Division Pirelli S.p.A., and in 2001 he filled the position of Senior Vice President Operations Tyres Sector of Pirelli s Group. From March 2002 until September 2002 Mr. Sala held the position of Chief Financial Officer of TIM S.p.A.. In October 2002 he was appointed Assistant to the Chairman of the Telecom Italia Group.

Germanio Spreafico: Mr. Spreafico was born in Lecco, Italy on September 20, 1952. He was appointed Head of Telecom Italia Group Purchasing on October 1, 2001. He began his career in 1977 at the Pirelli Financial Division, where he worked for 10 years, during which time he was promoted through various positions in domestic and international finance and ultimately took charge of Italian market financial operations. Subsequent

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to this he moved to the Cable sector, initially as Chief Financial Officer of the Italian company, before taking on the same role for the French company. In 1997, he became Chief Financial Officer of the Group Cable Industry Holding Company, where he also took on the position of Chief Purchasing Officer. At the present time, Mr. Spreafico is Chairman of Telenergia S.r.l., Consorzio Energia, and Deputy Chairman of Pirelli Cavi & Sistemi S.p.A., the holding company for the Pirelli Group Cable division, of which he was Head of Administration and Control and, from February 2000, Head of Purchasing.

Giuseppe Tronchetti Provera: Mr. Tronchetti Provera was born in Rome, Italy, on April 3, 1968. He has been head of the Telecom Italia Group Information Technology Market Business Unit since January 15, 2002 until June 1, 2004. Mr. Tronchetti Provera began his career at McKinsey & Company, where for five years he worked as a Senior Management Consultant at a number of offices across Europe, working in industries such as air transport, energy, mobile telephony, steel, television media and insurance. In 1997, he founded Cam Tecnologie, of which he is Deputy Chairman. The company develops technologies and products for the Energy Industry and the Environment. He is also Director of Camfin S.p.A.. Since 1999, he has served as Deputy Chairman of the Kyoto Club. He sits on the boards of Malgara Chiari & Forti S.p.A. and MCC Capitalia. He is currently Board member of Banksiel, Insiel and, since November 2003, Olivetti Tecnost S.p.A., where he is in charge of several strategic projects such as the re-launching of the I-Jet Division and enhancing the value of the brand name. In February 2003 he was appointed President of the Rome District of Audiovisuals and ICT.

Board of Auditors

The following table lists the members of the Telecom Italia Board of Auditors, as of May 21, 2004, including the Alternate Auditors, with their respective positions and year of appointment. The current Telecom Italia Board of Auditors was appointed by the Olivetti General Meeting on May 26, 2003.

Name	Position	Appointed
Ferdinando SUPERTI FURGA	Chairman	2003
Rosalba CASIRAGHI(1)	Auditor	2003
Paolo GOLIA(1)(2)	Auditor	2003
Salvatore SPINIELLO	Auditor	2003
Gianfranco ZANDA(3)	Auditor	2003
Enrico LAGHI	Alternate Auditor	2003
Enrico Maria BIGNAMI(1)(2)	Alternate Auditor	2003

(1) Elected by minority shareholders.
(2) Reappointed in 2003; member of the Board of Auditors since 2000.
(3) Reappointed in 2003; member of the Board of Auditors since 1997.

The positions held by the members of the Board of Auditors in other listed companies are shown below:

Ferdinando Superti Furga	Director of Ipi S.p.A. and Risanamento S.p.A.; member of the Board of Auditors of Arnoldo Mondadori Editore S.p.A. and Edison S.p.A.
Rosalba Casiraghi	
Paolo Golia	
Salvatore Spiniello	

	Director of Fondiaria Sai S.p.A.; Chairman of the Board of Auditors of Immobiliare Lombarda S.p.A.; member of the Board of Auditors of Edison S.p.A.
Gianfranco Zanda	Member of the Board of Auditors of Tim S.p.A.

For a detailed description of Telecom Italia s corporate governance, including activities and responsibilities of the Board of Auditors (acting as Audit Committee of the Company), see Item 10. Additional Information Corporate Governance .

External Auditors

According to Italian law, the Shareholders Meeting held on May 6, 2004 appointed Reconta Ernst & Young as the audit firm of the Company, taking into consideration the favorable opinion of the Board of Auditors.

Italian audit principles require that, in cases of corporate groups, the audit firm of the parent company should carry out the audit of the group s most important entities in terms of the nature of operations, in such a way that it can act as the main group audit firm and express a professional evaluation of the financial statements in their entirety. In addition, the specific procedure set forth by the Company (the Group Procedure for the

Appointment of External Auditors) provides that the auditor of Telecom Italia is the principal auditor of the entire group headed by Telecom Italia and consequently is the auditor to be preferred in conferral of appointments by subsidiaries for mandatory auditing.

As a result, as of May 6, 2004 the Ernst & Young audit network has been selected according to applicable rules and procedures as the only audit firm for all of the companies of the Telecom Italia Group.

Employees

The following table sets out the number of employees of the Telecom Italia Group at December 31, 2003 by Business Unit:

	Number of employees at end of period	
	2002	**2003**
Wireline	53,935	50,766
Mobile	18,702	18,888
South America(1)	5,461	5,049
Internet & Media	7,715	2,029
IT Market	5,506	4,827
IT Group	5,039	4,107
Olivetti Tecnost	4,527	2,395
Other Activities	5,735	5,126
Consolidated Total	**106,620**	**93,187**

(1) The data refers to Entel Chile group, Entel Bolivia group, the company Telecom Italia America Latina and the Business Segment South America of Telecom Italia.

As of December 31, 2003, the Telecom Italia Group employed 93,187 persons. Compared to December 31, 2002 total employment was lower by 13,433 units, due to turnover which reduced personnel by 4,604 units and changes in the scope of consolidation which reduced personnel by 8,829 units. The reductions attributable to the change in the scope of consolidation were mainly due to:

- the disposals in the Internet and Media Business Unit (a total decrease of 5,686 units, 5,402 units of which related to the disposal of New Seat);
- the disposals in the Olivetti Tecnost Business Unit (a total decrease of 2,132 units, of which 1,266 units relating to the sale of a factory in Mexico and 474 units relating to the closing of operations in Latin America);
- the sale of Netikos (207 units), included in IT Market Business Unit;

- the sale of TE.SS (404 units), included in Other Activities;

- the outsourcing of the logistics business segment of the Wireline Business Unit (337 units), the facility s activities of Olivetti Multiservices (208 units in Other Activities), the Information Technology activities of the Desktop Management (582 units in IT Group and 22 units in IT Market) and Corporate Solutions (380 units in IT Group and 21 units in Olivetti Tecnost).

Such decrease was partly offset by the Group s acquisitions of HanseNet (381 units, included in Wireline), Tm News (55 units, included in Internet and Media) and Top Services (21 units in Olivetti Tecnost).

The following table set out the number of employees of the Telecom Italia Group at December 31, 2003 broken down by geographical area and function:

	Manager	Professional	White-collar	Blue-collar	Total
Italy	1,727	4,847	70,089	1,406	78,069
Rest of Europe	44	319	1,930	1	2,294
North America	15	38	206	2	261
Central and South America	154	724	11,591	43	12,512
Australia, Africa and Asia	5	23	23	0	51
Telecom Italia Group Total	**1,945**	**5,951**	**83,839**	**1,452**	**93,187**

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Telecom Italia Group employees in Italy are represented by two categories of labor unions, one for managerial staff and another one for non-managerial staff. Employment agreements in Italy are generally collectively negotiated at national level between the national employers associations and the labor unions and, for medium and large companies, also at company level. Renewals of collective agreements are subject to general guidelines agreed upon between the Italian Government, the employers associations and trade unions. These guidelines establish that salary increases negotiated at national level should not exceed agreed upon inflation rates. Individual companies may enter into additional contracts, in order to link collective bonuses to the company s productivity or profitability.

Approximately 2% of the Telecom Italia Group s employees held executive positions as of December 31, 2003.

Employment contracts for managerial staff are ruled by a national collective agreement that expired in December 2003 and is presently under renewal. National collective agreement compensation clauses were renewed in March 2003.

The compensation clauses of the national collective agreement for non-managerial staff were renewed in July 2003 and the rest of the agreement will expire in December 2004. The compensation provisions of these collective agreements cover all employees rather than those of Information Technology Market, Olivetti Tecnost Group and Telecom Italia Media Group.

As for Telecom Italia, in July 2003 an agreement was reached about the collective bonus for years 2003-2006.

A major agreement, signed in June 2003, permits the collective dismissal of 2,500 employees during 2003 and 2004, on an individual consensus basis. The agreement is related to the implementation of the Industrial Plan.

These agreements confirm a tradition of constructive relations with the labour unions.

In Italy all employees are covered by public health care and pension schemes. Telecom Italia Group employees may elect to be covered by additional health care and pension plans. Assilt, the health care fund for Telecom Italia Group employees, reimburses the medical expenses of 220,000 people (employees, retirees and their families).

Telemaco, previously the pension fund of the Telecom Italia Group, has become in 2003 the pension fund of the companies which apply the National Collective Agreement for Telecommunications, with more than 58.000 members.

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COMPENSATION OF DIRECTORS, OFFICERS AND MEMBERS OF THE BOARD OF AUDITORS

Compensation of Directors

Prior to the Merger, Old Telecom Italia and Olivetti were managed by their own Board of Directors.

Olivetti s directors, recognizing that Telecom Italia would have been inherently different from Olivetti, determined that it would be appropriate that the direction of Telecom Italia remain entrusted essentially to the directors of Old Telecom Italia. Accordingly, the members of the Olivetti Board of Directors declared that, upon effectiveness of the Merger, they would consider their mandate as directors of Olivetti to be essentially completed. At the April 15, 2003 meeting of the Olivetti Board of Directors, the members of the Olivetti Board of Directors tendered their resignation with effect from the date of effectiveness of the Merger (apart from one director who resigned effective as of April 16, 2003).

At the Olivetti shareholders meeting held on May 26, 2003, the Olivetti shareholders appointed a new Board of Directors that essentially reproduced the Old Telecom Italia Board at the time and, upon effectiveness of the Merger, became the Board of Directors of Telecom Italia. The term of such Board of Directors expired in 2004 after the approval of the 2003 financial statements. On May 6, 2004 a new Board of Directors was elected. See above under Directors .

Below we set forth the compensation paid in 2003 to (i) Directors of Old Telecom Italia; (ii) Directors of Olivetti; (iii) Directors of Telecom Italia in office during fiscal year 2003 who were not confirmed by the Telecom Italia s shareholders meeting of May 6, 2004 and (iv) Directors elected on May 6, 2004 who were also Directors of Telecom Italia in office at the end of 2003.

(i) The total compensation paid to the Board of Directors of Old Telecom Italia from January 1 to August 3, 2003 was 9,593 thousand.

(ii) The total compensation paid to the Board of Directors of Olivetti from January 1 to August 3, 2003 was 2,109 thousand.

(iii) The total compensation paid for the fiscal year 2003 to Directors in office from the date of effectiveness of the Merger and who have not been confirmed by the General Meeting of May 6, 2004 was 238 thousand.

The following table lists the Directors appointed by the Telecom Italia s Shareholders meeting of May 6, 2004 who were in office at the end of 2003 and the compensation they received for the fiscal year 2003:

Name	Position	Period	Compensation base	Bonus	Non cash benefit	Other Compensation

				(thousands of euro)		
Marco TRONCHETTI PROVERA	Chairman	1/1 -12/31/2003	3,094(1)	1,200(2)		
Gilberto BENETTON	Deputy Chairman	1/1 -12/31/2003	134(3)			
Carlo Orazio BUORA	Managing Director	1/1 -12/31/2003	3,654(4)	2,200(5)		80(6)
Riccardo RUGGIERO	Managing Director	1/1 -12/31/2003	324(7)			
	General Manager	1/1 -12/31/2003		1,844(8)	8(9)	934(10)
Giovanni CONSORTE	Director	4/8 -12/31/2003	43			
Francesco DENOZZA	Director	1/1 -12/31/2003	103(11)			
Luigi FAUSTI	Director	1/1 -12/31/2003	186(12)			
Guido FERRARINI	Director	1/1 -12/31/2003	155(13)			
Gianni MION	Director	1/1 -12/31/2003	134(14)			157(15)
Massimo MORATTI	Director	1/1 -21/31/2003	103(11)			
Carlo A. PURI NEGRI	Director	1/1 -12/31/2003	134(16)			

(1) 1,607 thousand for the office of Chairman of Old Telecom Italia; 338 thousand for the office of Deputy Chairman and Managing Director in Olivetti; 1,149 thousand for the office of Chairman in Telecom Italia.

(2) Remuneration for the office of Chairman in Old Telecom Italia.

(3) 60 thousand for the office of Deputy Chairman in Old Telecom Italia; 31 thousand for the office of Deputy Chairman in Olivetti; 43 thousand for the office of Deputy Chairman in Telecom Italia.

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(4) 1,934 thousand for the office of Managing Director in Old Telecom Italia; 338 thousand for the office of Managing Director in Olivetti; 1,382 thousand for the office of Managing Director in Telecom Italia.
(5) 1,200 thousand for the office of Managing Director in Old Telecom Italia and 1,000 thousand for the office of Managing Director in Telecom Italia.
(6) Remuneration for the office of Chairman in the subsidiary TIM not received but paid over to Telecom Italia.
(7) 189 thousand for the office of Managing Director in Old Telecom Italia (approximately 60 thousand of which was not received by Mr. Ruggiero) and 135 thousand for the office of Managing Director in Telecom Italia (approximately 43 thousand of which was not received by Mr. Ruggiero).
(8) 694 thousand for the office of General Manager in Old Telecom Italia and 1,150 thousand for the office of General Manager in Telecom Italia.
(9) 5 thousand for the office of General Manager in Old Telecom Italia and 3 thousand for the office of General Manager in Telecom Italia.
(10) Compensation for employment, of which 545 thousand paid by Old Telecom Italia and 389 thousand paid by Telecom Italia.
(11) 60 thousand paid by Old Telecom Italia and 43 thousand paid by Telecom Italia.
(12) The amount includes remuneration received as a member of the Remuneration Committee and of the Internal Audit and Corporate Governance Committee and consists of 90 thousand (for the office of Director and member of the Remuneration Committee of Old Telecom Italia) and 96 thousand (for the office of Director and member of the Remuneration Committee and Internal Audit and Corporate Governance Committee of Telecom Italia).
(13) The amount includes remuneration received as a member of the Internal Audit and Corporate Governance Committee and is composed of 90 thousand paid by Old Telecom Italia and 65 thousand paid by Telecom Italia.
(14) Remuneration not received but paid over to Edizione Holding; of which 60 thousand was paid by Old Telecom Italia; 31 thousand by Olivetti and 43 thousand by Telecom Italia.
(15) Remuneration for the office of Director in the subsidiary Telecom Italia Media and of Deputy Chairman in the subsidiary TIM not received but paid over to Edizione Holding.
(16) 60 thousand was paid by Old Telecom Italia, 31 thousand by Olivetti and 43 thousand by Telecom Italia.

All of the executive officers contracts (with the exception of those of Messrs. Marco Tronchetti Provera, Carlo Orazio Buora, Riccardo Ruggiero and Giuseppe Nino Tronchetti Provera) contain the following clauses:

- if the Company terminates the work relationship (with the exception of a termination for good cause) and the executive officer waives certain rights to which he is entitled pursuant to applicable Italian law, the Company will pay to the executive officer a separation allowance providing for between two and four years of salary plus, in certain cases, a lump sum corresponding to the average of bonus compensation received in the three years (or shorter period) preceding his termination; and

- if the executive officer terminates the work relationship for good cause determined by a change reducing the responsibilities and tasks assigned to the executive officer, then such executive officer will be entitled to an amount corresponding to 50% of the amount as calculated above.

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The following tables list the stock options held by Mr. Riccardo Ruggiero and Mr. Giuseppe Sala as General Managers of Telecom Italia. Applicable Italian law requires disclosure of individual compensation in the form of stock options for members of the Board of Directors and for General Managers. The compensation in the form of stock options for Mr. Ruggiero and Mr. Sala were disclosed pursuant to legislative Decree No. 58/98 in the Telecom Italia Group s home jurisdiction Annual Report for the year ended December 31, 2003. See also below Options to Purchase Securities from Registrant .

		Options existing at 1/1/2003			New options granted during the year			Options exercised during the year			Options expired during the year	Options existing at 12/31/2003		
(A)	(B)	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)=1+4-7-10	(12)	(13)
First and last name	**Post held**	**No. options**	**Exercise average price**	**Average expiration date**	**No. options**	**Exercise average price**	**Average expiration date**	**No. options**	**Exercise average price**	**Market average price at exercise**	**No. options**	**No. options**	**Exercise average price(*)**	**Average expiration date**
Riccardo Ruggiero	A.D./ D.G.	750,000	3.177343	2007								750,000	3.177343	2007
		750,000	3.177343	2008							750,000			
		150,000	2.788052	2008								150,000	2.788052	2008
		150,000	2.788052	2009								150,000	2.788052	2009
		200,000	2.788052	2010								200,000	2.788052	2010

(*) Average subscription price of the shares resulting from the exercise of the options.

Following the Merger, each option entitles the holder to subscribe to 3.300871 Shares; the subscription price of the Shares has been modified, dividing the original exercise price by the assignment ratio (3.300871). To understand the table, the value of the average subscription price of the Shares referred to dates preceding the date of effectiveness of the Merger (August 4, 2003) has been adjusted on the basis of the assignment ratio and is, therefore, homogeneous with the price regarding the Shares of Telecom Italia.

		Options existing at 1/1/2003			New options granted during the year			Options exercised during the year			Options expired during the year	Options existing at 12/31/2003		
(A)	(B)	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)=1+4-7-10	(12)	(13)
First and last name	**Post held**	**No. options**	**Exercise average price**	**Average expiration date**	**No. options**	**Exercise average price**	**Average expiration date**	**No. options**	**Exercise average price**	**Market average price at exercise**	**No. options**	**No. options**	**Exercise average price(*)**	**Average expiration date**
Giuseppe Sala	General Manager	480,000(*)	5.07	1/3 up until May 2008, 1/3 up until May 2009 and 1/3 up until May 2010								480,000	5.07	1/3 up until May 2008, 1/3 up until May 2009 and 1/3 up until May 2010

(*) Relates to TIM options regarding a stock option plan allotted to the Director of Finance and Control of TIM.

Compensation of Executive Officers

The total compensation paid by Telecom Italia or by any of the Telecom Italia Group subsidiaries in 2003 to the executive officers was 10,299,572.

Compensation of Members of the Board of Auditors

In accordance with Italian law, there was no requirement to change the members of the Olivetti Board of Auditors pursuant to the Merger. At the Olivetti shareholders meeting of May 26, 2003, the Olivetti shareholders elected a new Board of Auditors which was the same as the Board of Auditors of Old Telecom Italia. As a result of the Merger and Old Telecom Italia not being the surviving company, the Board of Auditors of Olivetti, as elected on May 26, 2003, became the Board of Auditors of Telecom Italia.

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The table below sets forth compensation paid to the Board of Auditors of Old Telecom Italia, of Olivetti and of Telecom Italia.

The total compensation paid to the Board of Auditors of Old Telecom Italia from January 1, 2003 until and including August 3, 2003 was 481 thousand.

The total compensation paid to the Board of Auditors of Olivetti from January 1, 2003 until and including May 26, 2003 was 152 thousand.

The members of the Board of Auditors who were appointed by the Olivetti shareholders meeting on May 26, 2003 and upon effectiveness of the Merger become the Auditors of Telecom Italia received the following compensation:

Name	Position	Period	Compensation base	Bonus	Non cash benefit	Other Compensation
Ferdinando SUPERTI FURGA	Chairman	5/27-12/31/2003	93			
Rosalba CASIRAGHI	Acting Auditor	5/27-12/31/2003	70			
Paolo GOLIA	Acting Auditor	5/27-12/31/2003	70			
Salvatore SPINIELLO	Acting Auditor	5/27-12/31/2003	70			
Gianfranco ZANDA	Acting Auditor	5/27-12/31/2003	70			35(1)

(1) Remuneration for the office of Chairman of the Board of Statutory Auditors in the subsidiary IT Telecom and Acting Auditor in the subsidiaries Finsiel and TIM.

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OPTIONS TO PURCHASE SECURITIES FROM REGISTRANT

The Board of Directors of Old Telecom Italia during 2003 acknowledged:

- the forfeiture, as of April 2003, of the options remaining from the second lot of the 2001 Stock Option Plan (30,855,000 options remaining) following failure to reach the performance criteria calculated on the basis of the stock price of the Old Telecom Italia ordinary shares during the months of March 2002 and March 2003 and the corresponding values of the Dow Jones Eurostoxx TLC Index;

- the forfeiture, as of July 2003, of the options remaining from the third lot of the 2000 Stock Option Plan (9,900,004 options remaining) following failure to reach the performance criteria calculated on the basis of the stock price of the Old Telecom Italia ordinary shares during the months of June 2002 and June 2003 and the corresponding values of the Dow Jones Eurostoxx TLC Index.

The exercise of all Old Telecom Italia options was suspended from May 12, 2003, the 10th day of trading on the stock exchange preceding the date of the first call of the Shareholders Meeting with respect to the Merger, until August 4, 2003, the date of effectiveness of the Merger.

With reference to the Merger, Telecom Italia succeeded to all the stock option plans previously in force at Old Telecom Italia and Olivetti: the 1999 Stock Option Plan , the 2000 Stock Option Plan , the 2001 Stock Option Plan , the 2002 Stock Option Plan and the 2002 Top Stock Option Plan for Old Telecom Italia and the Three year 2002-2004 Stock Option Plan and the Three year February 2002 December 2004 Stock Option Plan for Olivetti.

Holders of the corresponding options have retained the right to subscribe at the price established at the time of the grant, the original number of shares stated in the respective regulations, adjusted to give effect to the Merger. The Merger assignment ratio established for the shareholders of the two companies is equal to 0.471553 ordinary shares for each Olivetti ordinary share and 3.300871 shares for each Old Telecom Italia share.

Therefore, although the price per option did not change, the number of underlying shares (previously corresponding to one ordinary share for each option) that can be subscribed to by exercising each option was adjusted by multiplying the number of shares by the Merger assignment ratio.

As a consequence of this, the subscription price of each ordinary share resulting from the exercise of the options for each Plan has also been adjusted by dividing the exercise price already established by the Merger assignment ratio.

In cases in which the application of the Merger assignment ratio to the various lots results in less than a whole number of shares, the holder of the options has the right to subscribe for each lot up to the full amount of shares rounded down to the nearest unit, exercising only a corresponding quota-part of the options. Following the exercises of options after the date of the Merger, residual options with fractional parts now exist.

On December 31, 2003 the exercise period of the first lot of the 1999 Stock Option Plan expired. The lot was fully exercised, with the exception of the residual options with fractional parts resulting from the above described operations which, as of the same date, consequently expired.

In compliance with the recommendations contained in CONSOB Communication No. 11508 of February 15, 2000, the key features of the stock option plans in force during 2003 are summarized in the following table. In order to ensure understanding in the reading thereof the values indicated (market prices and subscription prices of the shares resulting from the exercise of the options) regarding the amounts, exercises, forfeitures, expirations before the date of effectiveness of the Merger, have been adjusted on the basis of the Merger assignment ratios and thus made consistent with the prices regarding the ordinary shares of Telecom Italia.

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	(Amount in euro)	Options existing at 1/1/2003	New options granted during the year	Options exercised during the year	Options expired and not exercised or forfeited during the year	Options extinguished during the year due to termination of service	Options existing at 12/31/2003	of which exercisable at 12/31/2003
1999 Plan	No. of options	8,471,500		3,959,579.956	18.801		4,511,901.243	4,511,901.243
	Merger Assignment ratio	3.300871		3.300871	3.300871		3.300871	3.300871
	Subscription price	2.057033		2.057033	2.057033		2.057033	2.057033
	Market price	2.182		2.390(*)	2.374		2.374	
2000 Plan	No. of options	20,600,000			9,900,004		10,699,996	10,699,996
	Merger Assignment ratio	3.300871			3.300871		3.300871	3.300871
	Subscription price	4.185259			4.185259		4.185259	4.185259
	Market price	2.182			2.376		2.374	
2001 Plan	No. of options	63,507,500			30,855,000	312,500	32,340,000	32,340,000
	Merger Assignment ratio	3.300871			3.300871	3.300871	3.300871	3.300871
	Subscription price	3.177343			3.177343	3.177343	3.177343	3.177343
	Market price	2.182			1.952	2.060(*)	2.374	
2002 Plan	No. of options	28,076,000				1,789,500	26,286,500	8,065,500
	Merger Assignment ratio	3.300871				3.300871	3.300871	3.300871
	Average subscription price	2.908293				2.928015	2.906951	2.907420
	Market price	2.182				2.258(*)	2.374	
TOP 2002 Plan	No. of options	11,800,000				460,000	11,340,000	3,465,000
	Merger Assignment ratio	3.300871				3.300871	3.300871	3.300871
	Subscription Price	2.788052				2.788052	2.788052	2.788052
	Market price	2.182				2.070(*)	2.374	
2002 2004	No. of options (**)	800,000					800,000	533,332
	Merger Assignment ratio	0.471553					0.471553	0.471553
		7.015118					7.015118	7.015118
		2.075					2.374	

Plan						
	Subscription Price					
	Market price					
Feb.2002 - Dec.2004 Plan	No. of options (***)	7,030,000	1,090,000	5,940,000	3,960,008
	Merger Assignment ratio	0.471553	0.471553	0.471553	0.471553
		5.333441	5.333441	5.333441	5.333441
	Subscription price	2.075	2.299(*)	2.374	
	Market price				

(*) Weighted average price.
(**) Refers to 1,330,000 warrants assigned.
(***) Refers to 29,000,000 warrants authorized of which 26,475,000 assigned.

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Plan	Merger Assignment ratio	Subscription price of the resulting shares (euro)	Number of options granted at 12/31/2003 and exercisable from 2001	2002	2003	2004	2005	Total	Maximum period of options
1999	3.300871	2.057033		4,511,901.243				4,511,901.243	December 31, 2004
2000	3.300871	4.185259	5,349,998	5,349,998				10,699,996	5 years beginning from each year
2001	3.300871	3.177343		32,340,000				32,340,000	April 15, 2007
2002	3.300871	2.928015			7,753,500	7,497,000	9,996,000	25,246,500	5 years beginning from each year
	3.300871	2.409061			252,000	252,000	336,000	840,000	
	3.300871	2.339080			60,000	60,000	80,000	200,000	
2002 TOP	3.300871	2.788052			3,465,000	3,375,000	4,500,000	11,340,000	5 years beginning from each year
2002 -2004	0.471553	7.015118		266,666(1)	266,666(1)	266,668(1)		800,000	December 15, 2004
Feb. 2002 Dec. 2004	0.471553	5.333441		1,980,004(2)	1,980,004(2)	1,979,992(2)		5,940,000	December 31, 2004

(1) Exercisable during the period from November 1 to December 15 of each year, or could be also accumulated and exercised at any time following each annual exercise period until the exercise period expiry date.

(2) Exercisable during the period December 1 to December 31 of each year, or could be also accumulated and exercised at any time following each annual exercise period until the exercise period expiry date.

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Item 7. MAJOR SHAREHOLDERS AND RELATED-PARTY TRANSACTIONS

MAJOR SHAREHOLDERS

The Olimpia Shareholders Agreements.

The information contained herein on the Olimpia shareholders agreements has been taken from publicly available information filed by the parties involved therein with regulatory authorities. So far as Telecom Italia is aware, no facts have been omitted herein which would render the information misleading. No further or other responsibility in respect of such information is accepted by Telecom Italia.

There are shareholders agreements among Olimpia s shareholders.

In particular, shareholders agreements were entered into between Pirelli S.p.A. (now Pirelli and C. S.p.A.) and Edizione Holding S.p.A. (whose obligations and rights were subsequently assigned to Edizione Finance International S.A.) on August 7, 2001, as amended on September 14, 2001 and February 13, 2002 (hereinafter the Agreements). Shareholders agreements were entered into also between Pirelli, IntesaBci S.p.A. (now Banca Intesa S.p.A.) and UniCredito on September 14, 2001 and subsequently amended on September 26, 2001, October 24, 2001 and December 16, 2003 (hereinafter Agreements with the Banks). In addition, following a term sheet executed on December 16, 2002, shareholders agreements were entered into between Pirelli, Edizione, Unicredito and Intesa (collectively, the Former Olimpia Shareholders), Olimpia and Hopa on February 21, 2003, as amended on January 23, 2004 (hereinafter the Agreements with Hopa).

The Agreements and the Agreements with the Banks have a duration of three years and can be renewed at each expiration date. The renewal period is three years for the Agreements and two years for the Agreements with the Banks. On April 24, 2004, a notice was published stating that the Agreements with the Banks were renewed until October 4, 2006. The Agreements with Hopa have a three-year term as from May 9, 2003, subject to extension by mutual agreement of the parties thereto. If the Agreements with Hopa are not renewed, the partial demerger of Olimpia and Holinvest will occur, according to terms and conditions set forth in the Agreements with Hopa, and Hopa will receive a premium of at least 0.35 per Olivetti share (or financial instrument), such a sum to be updated in order to take into account the Merger.

The Agreements and the Agreements with the Banks deal with the nomination of the Board of Directors of Olimpia, Olivetti, Old Telecom Italia (now Telecom Italia, as the company resulting from the Merger), TIM and SEAT (now Telecom Italia Media: please see Item 4. Information on the Telecom Italia Group Business Significant Developments during 2003). They identify the key issues on which the board resolutions of such companies have to decide in accordance with the Agreements and the Agreements with the Banks. The Agreements and the Agreements with the Banks also discuss the rules for the resolution of disagreements among the contracting parties on key issues (the so-called deadlock situations). In addition, the Agreements and the Agreements with the Banks govern the consequences among the parties of any change in the structure of control of Pirelli (in the Agreements with the Banks) and of Edizione or of Pirelli (in the Agreements); and grant the parties the right to purchase or sell (puts and calls) Olimpia shares in the event of withdrawal from the agreements themselves.

The provisions relating to the nomination of the members of the Boards of Directors of Olivetti, Old Telecom Italia, TIM and SEAT are set forth below. In connection with the composition of the Boards of Directors of such companies, the parties to the Shareholders Agreements have agreed to use their best efforts, within the limits established by law, in order to cause:

the nomination by Edizione of one-fifth of the Boards of Directors, without taking into account the directors whose designation is reserved by law or applicable bylaws to the market or other parties;

- the nomination of one director by Intesa;
- the nomination of one director by Unicredito;
- the nomination of the vice-president of the Boards of Directors from among the directors nominated by Edizione; and
- in the event of the establishment of an Executive Committee, the election of one member of the Executive Committee from among the directors nominated by Edizione. See Item 6. Directors, Senior Management and Employees Directors .

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Under the Agreements with Hopa, Hopa has the right to appoint one Olimpia director and the Former Olimpia Shareholders must use their best efforts in order to cause a director designated by Hopa nominated to the Board of Directors of Olivetti, Old Telecom Italia, TIM and SEAT, with a corresponding reduction in the number of Pirelli nominees. See Item 6. Directors, Senior Management and Employees Directors .

Hopa does not have the right to veto any decision taken by the board of directors or shareholders of Olimpia. In the event of a disagreement between the former Olimpia Shareholders and Hopa with respect to the passage of a resolution by either the Extraordinary Shareholders Meeting or the Board of Directors of Olimpia concerning certain matters (including (i) the determination as to how Olimpia will vote its Olivetti, and now Telecom Italia, shares at an Extraordinary Shareholders Meeting of the Company, (ii) the purchase or sale of securities exceeding a certain amount and (iii) failure of Olimpia to maintain a debt to equity ratio of 1:1), Hopa may cause the partial demerger of Olimpia, in which event Olimpia may cause the partial demerger of Holinvest. In the event of any such partial demerger transactions, Hopa would receive its proportional share of Olimpia s assets and liabilities (determined in accordance with the Agreements with Hopa) and Olimpia will receive its proportional share of Holinvest s assets and liabilities (determined in accordance with the Agreements with Hopa). Except under certain extraordinary circumstances (including the failure of Olimpia to hold at least 25% of Olivetti s share capital now the corresponding stake in Telecom Italia s ordinary share capital or to maintain a debt to equity ratio of 1:1 after a specified cure period), no such partial demerger transactions may be implemented prior to the third anniversary of the merger of Holy S.r.l. (a wholly-owned subsidiary of Hopa) into Olimpia, which took place on May 9, 2003.

Hopa is granted certain co-sale rights in the event Pirelli reduces its equity interest in Olimpia.

Hopa, Holinvest and Hopa controlling companies (the Hopa companies), the Former Olimpia Shareholders and their respective controlling and controlled companies agreed not to acquire any additional Olivetti Shares except (i) in the case of Pirelli, in connection with the exercise of certain existing call options and swap agreements referred to in the Agreements with Hopa, (ii) in the case of Edizione, Unicredito and Intesa, as currently permitted, respectively, under the Agreements and the Agreements with the Banks, and (iii) in the case of the Hopa companies, as permitted under the Agreements with Hopa.

As a result of the Merger no shareholder controls the Company. Olimpia is the largest shareholder in Telecom Italia, with a stake equal to as of May 6, 2004 approximately 17%. Under the voto di lista system for the election of directors, a greater than 1% shareholder or group of shareholders may put forward a slate of directors for election to the Board. As a result of this system 15 of the directors elected at the shareholders meeting of May 6, 2004 are candidates put forward by Olympia. See Item 10. Additional Information Corporate Governance Board of Directors Appointment .

There are no arrangements known to the Company the operation of which may result in any shareholder obtaining a controlling interest in Telecom Italia.

Shareholders Ownership

Board of Directors

The following table shows the ownership, as of August 3, 2003, of the Telecom Italia Group s shares by the Directors of Olivetti :

Olivetti ordinary shares	11,711
Old Telecom Italia Shares	550
Old Telecom Italia Savings Shares	6,839
TIM ordinary shares	9,155

The Directors of Old Telecom Italia and Telecom Italia who were not reappointed by the General Meeting of May 6, 2004 held the following shares, as of December 31, 2003:

TIM ordinary shares	10,000

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The following table shows the ownership of Telecom Italia and TIM shares, as of May 6, 2004, by the Directors of Telecom Italia who were reappointed (or appointed) by the General Meeting of May 6, 2004:

Name	Company	Number of shares held as of August 4, 2003	Number of shares purchased	Number of shares sold	Number of shares held as of May 6, 2004
Giovanni CONSORTE	Telecom Italia Savings Shares	33,088		33,088	0
	Telecom Italia Media ordinary shares	40,183			40,183
Luigi FAUSTI	TIM ordinary shares	50,000			50,000
Luigi ROTH (appointed)	Telecom Italia Shares(1)				11,553
	TIM ordinary shares(1)				14,300
	Telecom Italia Media ordinary shares(1)				726
Pasquale PISTORIO	Telecom Italia Shares				889,000
	Telecom Italia Shares(1)				660,000

(1) Shares held indirectly.

Board of Auditors

The following table shows the ownership, as of May 26, 2003 of the Old Telecom Italia Group s shares by the Members of the Board Auditors of Olivetti (in office from January 1 until and including May 26, 2003):

Old Telecom Italia Shares	15,650
Old Telecom Italia Saving Shares	20,000
TIM ordinary shares	26,206

The following table shows certain information, as of the date of respective appointment, of ownership of the Old Telecom Italia Group s shares by the Members of the Board Auditors of Olivetti (in office as of May 26, 2003) and of Old Telecom Italia (in office as of May 24, 2003):

Old Telecom Italia Shares	18,000
Old Telecom Italia Savings Shares	68,000
TIM ordinary shares	16,270
TIM savings shares	10,000

The following table shows certain information, as of May 6, 2004 of ownership of the Telecom Italia Group s shares by the Auditors of Telecom Italia:

Name	Company	Number of shares held as of August 4, 2003	Number of shares acquired	Number of shares sold	Number of shares held as of May 6, 2004

Paolo GOLIA	TIM ordinary shares	0	15,555	0	15,555
Salvatore SPINIELLO	Telecom Italia Shares(1)	59,415	23,577	0	82,992
	Telecom Italia Savings Shares(1)	224,458	10,000	0	234,458
	TIM ordinary shares	10,000(2)	0	0	10,000
	TIM savings shares	10,000(2)	0	10,000	0
Ferdinando SUPERTI FURGA	TIM ordinary shares	6,270(2)	0	0	6,270

(1) Resulting from the application of the exchange ratio between Old Telecom Italia and Telecom Italia shares.

(2) Shares held as of the date of appointment (May 24, 2003).

As of May 6, 2004 no member of the Board of Directors or Board of Auditors beneficially owned more than 0.00331% of the Shares or Savings Shares.

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The following table shows certain information, as of May 6, 2004, about the ownership of the Company s Shares and Savings Shares by the Company s directors and executive officers as a group and by the members of the Board of Auditors as a group.

Title of Class	Owner	Number Owned	% of class
Shares	Directors and executive officers as a group (19 Directors and 8 Executive Officers)	1,566,020	0.01519
	Board of Auditors as a group (5 persons)	82,992	0.00081
Savings Shares	Directors and executive officers as a group (19 Directors and 8 Executive Officers)	98,693	0.00170
	Board of Auditors as a group (5 persons)	234,458	0.00404

Telecom Italia has a Code of Conduct for Insider Dealing that sets out the disclosure requirements and rules applicable to transactions involving financial instruments issued by the Company and its subsidiaries carried out by persons who, as a consequence of their position in the Company, have access to material information (taken to mean information on matters capable of producing significant changes in the outlook for the profitability, financial position and/or balance sheet of the Company and the Telecom Italia Group and likely, if made public, to have a significant effect on the price of the listed securities in question). To this end the relevant persons include amongst others Directors, executive officers and Statutory Auditors.

The criteria applied in drafting the Code are consistent with the basic principles underpinning the Company s system of corporate governance: rigour, transparency and alignment with best international practice. The key features of the Code are:

- flexibility in identifying the persons subject to the disclosure obligations, to take account of situations where persons may have temporary access to inside information;
- immediate disclosure to the market of transactions whose amount, aggregated with the amounts of other transactions carried out in the three preceding months and not yet declared to the Company, exceeds 80,000;
- quarterly disclosure of transactions whose cumulative amount is more than 35,000 and less than 80,000;
- extension of the disclosure obligations to the exercise of stock options and pre-emption rights and all transactions involving securities issued by companies belonging to the Telecom Italia Group, even when carried out under a contract for the management of an investment portfolio under which the investor renounces the right to give instructions;
- black-out periods during which, in general, persons subject to the disclosure obligations may not carry out transactions.

In the event of non-compliance, the Code provides for severe penalties; where the offender is a Director or a member of the Board of Auditors, the Board of Directors may propose the revocation of his/her appointment at the next shareholders meeting. If the offender (including an executive officer) is an employee, penalties set forth by applicable laws and collective agreements will apply.

Continuing Relationship with the Treasury

Since December 9**,** 2002, the Treasury has not held a direct holding in Telecom Italia. However, the Treasury continues to be in a position to exert certain powers with respect to Telecom Italia through the exercise of the special powers included in Telecom Italia s Bylaws. Such powers were established in 1997 according to Law 474/1994, when Telecom Italia formerly controlled by the Italian Treasury was privatized.

On May 22, 2003, taking into account the proposed Merger, a Decree by the Minister for Economy and Finance, in agreement with the Minister for Productive Activities, stated the exact wording of Telecom Italia s bylaws to be adopted in connection with Merger with reference to the special powers: in particular, the decree maintained the power of approving the acquisition of major shareholdings in the company s voting capital and the power of veto as currently provided for in Telecom Italia s bylaws. On the other hand the power of approving major shareholders agreements and the power of appointment by the Treasury of one Director and one Statutory Auditor were relinquished.

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According to the aforementioned decree, the special powers included in Telecom Italia s Bylaws as adopted in connection with the Merger are as follows:

- *Approval of Material Acquisitions of Shares.* The State has the authority to approve/disapprove of the acquisition of material interests in the share capital of Telecom Italia (which is defined as 3% of the voting share capital). The Board of Directors is required to notify all such acquisitions to the Ministry for Economy and Finance. Until approval, the purchaser of the Shares may not vote the Shares and, in case of disapproval or the expiration of the 60-day term within which the Minister has to make a decision, the purchaser is obligated to resell the Shares within one year.

- *Veto Power over Major Changes.* The State has veto power on resolutions to dissolve the company, approve mergers, demergers or disposition of the business, transfer the registered office abroad, change the corporate purposes or amend or modify the special powers.

Presently, the exercise of special powers by the Government with respect to privatized companies (including Telecom Italia) is governed by an ad hoc decree (the Golden Share Decree).

In particular, following the issuance by the EU of a directive on May 4, 1999, on February 11, 2000, the Italian Government issued the Golden Share Decree. Pursuant to the Golden Share Decree, the Italian Government can use its special powers to protect the vital interests of the State and respond to indispensable reasons of general interest, including public law and order, public security, public health and national defense. The Italian Government will exercise such special powers in compliance with the principles of Italian and European Community laws, and in any case in line with the objectives of the privatization process, and the protection of competition and the market and having regard for non-discrimination principles. Such powers must be suitable and proportional to achieving the indispensable objectives of general interest described above. The Golden Share Decree provides that the Italian Government may exercise its special powers to prevent acquisitions of shares of privatized companies if such acquisitions (i) are not transparent and would not ensure full disclosure with respect to controlling share ownerships of the companies whose shares are being acquired and the objectives and industrial plans proposed by the buyers of the target companies, (ii) compromise the liberalization and market competition or are not in line with the company s privatization goals, or entails situations of conflict of interests which could compromise the company s mission with respect to the objectives of public interest, (iii) entail objective risks of being affected by criminal organizations, or involve the company in unlawful activities, (iv) jeopardize conservation of the special powers of the State, or (v) represent a considerable risk of serious harm to the vital interests of the State described above, including the supply of essential raw materials and goods, the supply of essential public services and the security of related installations and networks and, further, the development of advanced technological sectors.

In December 2003, Law 350/2003 significantly modified the rules governing the special powers of the Italian Government with respect to privatized companies. In particular, the Government will no longer have the power to approve/disapprove of the acquisition of material interests in the share capital of such companies, but will be able to object to it only within a ten-day time limit, in case of prejudice caused to vital State interests and every time there is the need to defend subsequent undeniable reasons of public interest. The new rules are not effective and require implementation through decrees still to be issued which amongst others will specify to which privatized companies the special powers will continue to apply.

According to the powers entrusted to the Board of Directors pursuant to article 12 of the Bylaws, Telecom Italia s Bylaws will be amended at such time in order to conform to the new statutory provisions regarding special powers, as soon as the aforementioned decrees are issued.

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RELATED-PARTY TRANSACTIONS

The Telecom Italia Group enters into transactions with affiliates, and various related parties. The following related party transactions relate to transactions between Telecom Italia and its subsidiaries and the Telecom Italia Group s affiliates as well as the members of the Board of Directors and the companies in which they hold corporate office or significant responsibility. Transactions between members of the Telecom Italia Group are excluded as they are eliminated on consolidation. All such transactions are within the Telecom Italia Group s normal operations and were conducted on an arm s length basis in accordance with specific regulatory provisions.

The following related party transactions are reflected in the statement of operations for the years ended December 31, 2001, 2002 and 2003, respectively:

	Related party transactions in the year ended December 31,					
	2001		2002		2003	
Items	**In the aggregate**	**Main transactions with affiliates**	**In the aggregate**	**Main transactions with affiliates**	**In the aggregate**	**Main transactions with affiliates**
Operating revenues	954 million	Refers mainly to: Astrolink (296 million), Brasil Telecom (120 million), Nortel Inversora group (119 million), Teleleasing (82 million), Auna group (63 million), Sky Italia (formerly Stream) (55 million) and Lottomatica (123 million)	306 million	Refers mainly to: Teleleasing (105 million), Brasil Telecom (48 million), Sky Italia (formerly Stream) (42 million), Auna group (18 million), Telecom Argentina (18 million) and Telekom Srbija (17 million)	275 million	Refers mainly to: Teleleasing (166 million), Sky Italia (formerly Stream) (22 million), Shared Service Center (21 million), Telecom Argentina (12 million) and Telekom Austria (12 million)
Cost of materials and other external charges	596 million	Refers mainly to: rent payable to IM.SER (199 million) and Telemaco Immobiliare (77 million); and TLC service costs from ETEC S.A. Cuba (79 million)	475 million	Refers mainly to: rent payable to IM.SER (153 million) and Telemaco Immobiliare (37 million); TLC service costs from ETEC S.A. Cuba (77 million); and maintenance and assistance contracts from Italtel (40 million) and Siemens Informatica (24 million)	399 million	Refers mainly to: rent payable to Tiglio I (81 million) and Tiglio II (24 million); TLC service costs to ETEC S.A. Cuba (112 million) and Telekom Austria (22 million); and maintenance and assistance contracts from Shared Service Center (45 million), Siemens Informatica (34 million), Teleleasing (11 million) and Italtel (22 million)

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Items	2001 In the aggregate	2001 Main transactions with affiliates	2002 In the aggregate	2002 Main transactions with affiliates	2003 In the aggregate	2003 Main transactions with affiliates
	Related party transactions in the year ended December 31,					
Other income, net	25 million	Mainly relates to cost recoveries for personnel on loan to certain affiliates	9 million	Mainly relates to cost recoveries for personnel on loan to certain affiliates	14 million	Mainly relates to cost recoveries for personnel on loan to certain affiliates
Financial income and expense, net	Expense for 8 million	Includes accrued interest income on loans made to certain affiliates (22 million); interest expense payable to Teleleasing for financial leasing transactions (30 million)	Expense for 9 million	Includes accrued interest income on loans made to certain affiliates (14 million); interest expense payable to Teleleasing for financial leasing transactions (23 million)	Income for 13 million	Includes accrued interest income on loans made to certain affiliates (24 million); interest expense payable to Teleleasing for financial leasing transactions (11 million)

The following related party transactions are reflected on the balance sheets as of December 31, 2002 and 2003:

Items	2002 In the aggregate	2002 Main transactions with affiliates	2003 In the aggregate	2003 Main transactions with affiliates
	Related party transactions in the year ended December 31,			
Loans in long-term investments	456 million	Refers mainly to medium/long term loans made to Aria Is Tim (313 million), Tiglio I (70 million), Telegono (34 million) and Tiglio II (30 million)	122 million	Refers mainly to medium/long term loans made to Aria-Is Tim (336 million written down by 279 million), Aree Urbane (31 million) and Telegono (15 million)
Trade accounts receivables and other current assets	222 million	Comprises mainly receivables from Sky Italia (formerly Stream) (71 million), Telekom Srbija (21 million net of provision), Teleleasing (38 million) and Consorzio Telcal (14 million)	149 million	Comprises mainly receivables from Sky Italia (formerly Stream) (44 million written down by 27 million), Teleleasing (49 million) and Shared Service Center (11 million)

Trade accounts payable and other current liabilities	405 million	Refers to payables for supply contracts connected with operating and investment activities. They include: payables to the Italtel Group (150 million), Siemens Informatica (40 million), Teleleasing (17 million) and advances from Consorzio Telcal (103 million)	146 million	Refers to payables for supply contracts connected with operational and investment activities. They include: payables to the Italtel group (54 million), Siemens Informatica (23 million) and Mirror International Holding (24 million) for capital subscribed and not yet paid

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	Related party transactions in the year ended December 31,			
	2002		2003	
Items	**In the aggregate**	**Main transactions with affiliates**	**In the aggregate**	**Main transactions with affiliates**
Long-term and short-term debt	406 million	Refers mainly to payables for finance leases to Teleleasing (393 million)	42 million	Refers mainly to payables for finance leases to Teleleasing (26 million), Shared Service Center (6 million) and Edotel (4 million)
Short-term financial receivables	35 million	Comprises short-term loans made to TI Sparkle (formerly TMI) group companies (14 million) and Golden Lines (10 million net of provisions)	30 million	Comprises short-term loans made to Teleleasing (13 million), TMI Canada (8 million) and TIN Web (5 million)
Long-term and short-term contracts	110 million	Refers mainly to activities on behalf of Consorzio Telcal for the Telematico Calabria Plan		
Guarantees and collateral	935 million	Comprises sureties provided on behalf of Aria Is Tim (537 million), Consorzio Csia (85 million) and Sky Italia (formerly Stream) (72 million), Tiglio I (27 million) as well as collateral on behalf of Aria Is Tim (110 million)	976 million	Comprises sureties provided on behalf of Aria Is Tim (672 million), Consorzio Csia (81 million), Tiglio I (46 million) as well as collateral on behalf of Aria Is Tim (107 million)
Capital expenditures	441 million	Mainly consists of acquisitions of telephone exchanges from the Italtel group (406 million) and computer projects from Siemens Informatica (19 million)	403 million	Mainly consists of acquisitions of telephone exchanges from the Italtel group (346 million) and computer projects from Siemens Informatica (13 million)

Moreover, related party transactions in the year ended December 31, 2003 include:

Items	**In the aggregate**	**Nature of the transaction**
Purchases and sales commitments	37 million	

Refers to commitments with Teleleasing (5 million) under operating leases and with ETEC S.A. Cuba (32 million) for the capital increases

In addition, during 2003, the buildings leased from Teleleasing under financial leasing contracts, already recorded in tangible assets in the preceding financial statements, were purchased.

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Other related party transactions for the year ended December 31, 2003: Pirelli group, Edizione Holding group, Unipol group, Banca Intesa group, Unicredito group and others

Related party transactions, excluding transactions among group companies, also include transactions entered into during 2003 between the Telecom Italia Group with the Pirelli group, the Edizione Holding group, the Unipol group, the Banca Intesa group, the Unicredito group and the companies associated with Director Mr. Massimo Moratti as follows.

The following related party transactions are reflected in the statement of operations for the year ended December 31, 2003:

Items	In the aggregate	Nature of the transaction
Operating revenues	63 million	Refers mainly to computer services and the supply of energy services to the Pirelli group (34 million) and telephone services to the Pirelli group (5 million), the Edizione Holding group (9 million), the Banca Intesa group (4 million), the Unicredito group (2 million), the Unipol group (8 million) and companies associated with Director Mr. Massimo Moratti (1 million)
Cost of materials and other external charges	55 million	Refers mainly to R&D expenditures and information technology and tax consulting services and matters regarding intellectual property rendered by the Pirelli group (44 million), insurance services to the Unipol group (10 million) and the commissions paid to the Edizione Holding group for the sale of prepaid telephone cards (1 million)

The following related party transactions are reflected on the balance sheet as of December 31, 2003:

Items	In the aggregate	Nature of the transaction
Trade accounts receivables and other current assets	20 million	Refers mainly to the above-mentioned telephone services rendered to the Pirelli group (13 million), to the Edizione Holding group (3 million), to the Banca Intesa group (2 million) and to the Unipol group (2 million)
Trade accounts payable and other current liabilities	30 million	Mainly includes supply transactions connected with services rendered and investment activities with the Pirelli group (principally cables)
Capital expenditures	30 million	Refers to purchases of telecommunications cables (27 million) and leasehold improvements (3 million) from the Pirelli group

Short-term financial receivables	707 million	Refers to the liquid assets of the Group deposited with the Banca Intesa group (608 million) and the Unicredito group (99 million)
Financial debt	392 million	Financial exposure of the Group to the Banca Intesa group (341 million) and the Unicredito group (51 million)
Acquisition of investments	2 million	Purchase by Telecom Italia S.p.A of a 5% stake in EPIClink S.p.A. from Pirelli S.p.A.
Disposal of business segments	4 million	Gain on contribution, by Olivetti, of the Facility Management business segment to Pirelli & C. Real Estate
Derivatives	88 million	Hedging contracts and forward currency agreements put into place with the Banca Intesa group

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Moreover, there were the following transactions:

- in 2003, TIM and Telecom Italia disposed of telephone cards to Autogrill S.p.A. (Edizione Holding group) for subsequent sale to the general public for an equivalent amount of 22 million, the commission due to Edizione Holding group for the sale of telephone cards amounted to 1 million;
- on July 28, 2003, IT Telecom S.p.A. contributed its business segment Corporate Solution to Pirelli Informatica s share capital. Pirelli Informatica changed in Shared Service Center (SCC), a consortium with limited liability held as of December 31, 2003 by IT Telecom S.p.A. (45%), Olivetti Tecnost S.p.A. (5%) and Pirelli S.p.A. (50%);
- on July 21, 2003, the spin-off of Tiglio I and Tiglio II in Ortensia was concluded. Such transaction became effective on July 25, 2003;
- in March 2004 TIM conferred to Shared Service Center a business segment operating in the development and maintenance of SAP applications.

Other related party transactions for the years ended December 31, 2002 and 2001: Pirelli group and Edizione Holding group

Related party transactions, excluding transactions among group companies, also included transactions between the Telecom Italia Group with the Pirelli group and the Edizione Holding group in 2002 as follows.

The following related party transactions were reflected in the statement of operations for the year ended December 31, 2002:

Items	In the aggregate	Nature of the transaction
Operating revenues	26 million	Mainly refers to telephone services to Pirelli group (8 million) and to Edizione Holding (16 million) and to information services to Pirelli group (2 million)
Cost of materials and other external charges	23 million	These essentially refer to R & D expenditures and the supply of services in the IPR field to Pirelli group (21 million) and to Edizione Holding group (2 million)