

PORTUGAL TELECOM SGPS SA

Form 6-K

April 18, 2008

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 6-K

**Report of Foreign Private Issuer
Pursuant to Rule 13a-16 or 15d-16 of the
Securities Exchange Act of 1934**

**For the month of April 2008
Commission File Number 1-13758**

PORTUGAL TELECOM, SGPS, S.A.

(Exact name of registrant as specified in its charter)

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

(Address of principal executive office)

Indicate by check mark whether the registrant files or will file annual reports under cover Form 20-F or Form 40-F.

Form 20-F x

Form 40-F o

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes

No

Annual report 2007

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The terms "PT", "Portugal Telecom Group", "PT Group", "Group" and "Company" refer to Portugal Telecom and its subsidiaries or any of them as the context.

Portugal Telecom

Portugal

| | |
|-------------------------------|---|
| Wireline | <ul style="list-style-type: none"> • Retail [PT Comunicações 100%] • Large corporates voice and data [PT Corporate 100%] • SMEs voice and data [PT Prime 100%] • ISP and broadband services [PT.COM 100%] |
| Euro 1,962 million (revenues) | |

| | |
|-------------------------------|--|
| Mobile | <ul style="list-style-type: none"> • TMN 100% |
| Euro 1,543 million (revenues) | |

Main international assets

| | | | Revenues (Euro million) |
|-----------------------------|-----------------------|---------------------------------------|--------------------------------|
| Vivo 31.38% | • Brazil | • Mobile | 2,463 |
| Médi Télécom 32.18% | • Morocco | • Mobile | 438 |
| Unitel 25% (*) | • Angola | • Mobile | 649 |
| CTM 28% | • Macao | • Wireline, mobile, Internet and data | 207 |
| MTC 34% (*) | • Namibia | • Mobile | 118 |
| CVT 40% (*) | • Cape Verde | • Wireline, mobile, Internet and data | 68 |
| CST 51% (*) | • São Tomé e Príncipe | • Wireline, mobile, Internet and data | 8 |
| Timor Telecom 41.12% | • East Timor | • Wireline, mobile, Internet and data | 23 |
| UOL 29% | • Brazil | • ISP, contents and Internet | 197 |

(*) These stakes are held by Africatel, which is controlled 78% by PT.

Support companies

Systems and IT [PT Sistemas de Informação 100%]; Innovation, research and development [PT Inovação 100%];

Backoffice and shared services [PT PRO 100%]; Procurement [PT Compras 100%];

Call centres and telemarketing services [PT Contact 100%]; Pension funds management [Previsão 82.05%]

Message to Shareholders

Dear Shareholders,

The end of the takeover bid over Portugal Telecom, that had been ongoing for over a year, was a key event of the beginning of 2007. As such, from 2 March 2007, the board of directors, with the full support of the shareholders, initiated the execution of the proposed remuneration package which included the payment of dividends, together with a share buyback programme and the spin-off of PT Multimédia.

At the present time, and considering the dividend proposal on this year's results, we can state that we have achieved, on the expected timing, over 80% of what we had promised without compromising the company's financial position, its investment capacity and, therefore, its future.

The spin-off was the key element for the liberalisation of the telecoms sector in Portugal

PT Multimédia's spin-off was proposed by PT in August 2006 and was not the Result of any regulation or legal imposition. As of November 13 2007, Portugal Telecom ceased to hold any shares in PT Multimedia, a measure that we consider to be beneficial to the telecommunications market in Portugal, since promotes competition.

With the spin-off, we have actively changed the competitive arena in Portugal and were responsible for the most important boost to competition ever witnessed in our market. Currently, in any of the telecoms segments where we operate voice, broadband or TV the two largest operators taken together have a dimension that is comparable to PT, which definitely overcomes the idea that our company holds a dominant market position in Portugal.

Brazil is and will continue to be an important market for Portugal Telecom

Vivo is currently the largest mobile operator in Brazil, and this position was further consolidated during 2007. The mature relationship that we maintain with our partner Telefónica was crucial in increasing the value of our holding and carrying out difficult but essential changes with a view to enhance Vivo's competitiveness. The implementation of GSM, which we delivered in record time, is a good example of this, as it has allowed us to overcome a disadvantage to our competitors. At the present time, over 85% of our new clients are on GSM, and around 34% of the 34.4 million Vivo customers use this technology.

In August 2007, Vivo acquired Telemig, the mobile operator of the state of Minas Gerais, guaranteeing control of more than 4 million customers in the third richest state in Brazil. Also worth highlighting is the acquisition of 1,9 Ghz licenses for the regions of Brazil where Vivo did not yet operate, achieving full national coverage. In addition, Vivo secured 3G coverage for the entirety of its operational area in December, bringing in the means to consolidate its strong competitive position.

As a result of the faultless carrying out of these projects Vivo is today stronger and more competitive than a year ago, with very encouraging growth prospects.

Reinforced investment in Africa with the creation of Africatel and partnership with Helios

We have always stated that the African markets are an important part of our international strategy. In August 2007 we realised this commitment through a partnership with Helios Investment Partners, who have acquired a 22% stake on Africatel, the PT Group company that holds our interests in the sub-saharian region of the continent.

Through this strategic partnership with Helios we intend to continue developing and consolidating our operations in Africa, putting together our holdings and market knowledge to Helios' strengths in the region and the financial discipline that such investors bring with them.

Africa is a market experiencing exponential growth, and we will continue to endeavor to translate such growth into value for our shareholders. We will be extremely selective on identifying opportunities for expansion, ensuring that we have an international strategy that truly delivers shareholder value.

Fixed-mobile convergence: structural changes to the business in Portugal

Regarding our operations in Portugal, we have initiated the implementation of a fixed and mobile convergence strategy. We are transforming our organisation in order to face this

challenge and taking the necessary steps for the combined management of the business in Portugal. PT Portugal is underway and, in 2007, we started offering our clients integrated fixed-mobile telecommunication solutions.

The decision to launch a television service was also taken and is one of the highlights of 2007. This new area of business, where we are currently investing and will continue to do so in the coming years, is a key element of our strategy for residential customers going forward, a market segment where competition is already very strong and Portugal Telecom sees its commercial operations limited by an asymmetric regulatory framework.

Nevertheless, the commitment of our employees, this company's capacity to innovate and launch new services, its investment capacity, the reach and coverage of our distribution, maintenance and client support networks, lead me to be optimistic towards the future.

We continue to be largest investor in the information society in Portugal

I must also emphasise Portugal Telecom's contribution to the development of our country's information society. This year we have invested nearly 240 million euros in e-initiatives such as e.escolas. We distributed around 68 thousand portable computers with Internet connection to young students, fostering the access to new technologies.

In terms of training and development, I also highlight PT's commitment to the CMU programme in Portugal, which involves an investment of 5 million euros over five years. The retraining of our staff has also been a priority and in 2007, as part of the New Opportunities scheme, 664 of our collaborators saw the skills acquired throughout their professional life certified, giving a positive contribution to the development of the company and the country.

The year 2007 has closed the takeover bid cycle

The management team which I lead is pleased with the results achieved over the last two years and with the response given by our staff and shareholders to the challenges faced, which demonstrated a clear and continuing support to this team.

PT is a reference and a leader in the development of the information society in Portugal. We have high ambitions for the future, not just in the domestic market, but also abroad. With the superior quality of our human resources, I am certain that we will continue to contribute positively to the development of the countries where we operate and to create value to our shareholders.

Henrique Granadeiro

Chairman and CEO

01 Financial review

Consolidated income statement (1)

Euro million

| | 2007 | 2006 | Δ 07/06 |
|--|---------|---------|---------|
| Operating revenues | 6,148.4 | 5,765.3 | 6.6% |
| Wireline | 1,843.5 | 1,953.0 | (5.6)% |
| Domestic mobile • TMN | 1,464.6 | 1,426.2 | 2.7% |
| Brazilian mobile • Vivo (1) | 2,462.9 | 2,104.7 | 17.0% |
| Other | 377.3 | 281.4 | 34.1% |
| Operating costs, excluding depreciation and amortisation | 3,791.7 | 3,528.3 | 7.5% |
| Wages and salaries | 638.1 | 633.5 | 0.7% |
| Post retirement benefits | (65.1) | (72.1) | (9.8)% |
| Direct costs | 907.3 | 724.9 | 25.2% |
| Cost of products sold | 656.1 | 580.6 | 13.0% |
| Support services | 233.6 | 202.1 | 15.6% |
| Marketing and publicity | 147.2 | 138.3 | 6.5% |
| Supplies and external services | 945.6 | 928.5 | 1.8% |
| Indirect taxes | 201.8 | 175.9 | 14.7% |
| Provision and adjustments | 127.0 | 216.6 | (41.4)% |
| EBITDA (2) | 2,356.7 | 2,237.0 | 5.3% |
| Depreciation and amortisation | 1,123.1 | 1,130.7 | (0.7)% |
| Income from operations (3) | 1,233.6 | 1,106.3 | 11.5% |
| Other expenses (income) | 317.9 | 129.2 | 146.0% |
| Curtailement costs, net | 275.6 | 19.0 | n.m. |
| Gains on disposal of fixed assets, net | (2.8) | (5.1) | (45.7)% |
| Other costs, net | 45.1 | 115.4 | (60.9)% |
| Income before financial results and taxes | 915.7 | 977.1 | (6.3)% |
| Financial expenses (income) | (116.8) | 118.4 | n.m. |
| Net interest expenses | 197.4 | 220.1 | (10.3)% |
| Net foreign currency exchange losses/(gains) | 12.4 | (4.5) | n.m. |
| Gains on financial assets and other investments, net | (248.8) | (18.3) | n.m. |
| Equity in earnings of associated companies, net | (126.1) | (130.6) | (3.4)% |
| Net other financial expenses | 48.3 | 51.8 | (6.7)% |
| Income before income taxes | 1,032.5 | 858.6 | 20.3% |
| Provision for income taxes | (243.3) | 21.4 | n.m. |
| Income from continuing operations | 789.2 | 880.0 | (10.3)% |
| Net income from discontinued operations | 45.5 | 74.1 | (38.7)% |
| Losses (income) attributable to minority interests | (92.8) | (87.4) | 6.3% |
| Consolidated net income | 741.9 | 866.8 | (14.4)% |

(1) Considering a Euro/Real average exchange rate of 2.6661 in 2007 and 2.7315 in 2006. (2) EBITDA = operating income + depreciation and amortisation. (3) Operating income = income before financial results and taxes + work force reduction program costs + losses on disposals of fixed assets, net + other costs, net.

Consolidated operating revenues

Consolidated operating revenues increased by 6.6% y.o.y in 2007 to Euro 6,148 million, reflecting the higher contribution from: (1) Vivo (Euro 358 million), due to the positive impact of the change in the interconnection regime (July 2006) as well as customer and ARPU growth; (2) TMN (Euro 38 million) on the back of the 9.8% y.o.y. increase in the number of customers, particularly in postpaid and wireless broadband; and (3) other businesses (Euro 96 million) primarily explained by MTC (Euro 79 million), which has been consolidated since September 2006 only, and the increase in revenues of other fully consolidated subsidiaries. These effects were partially offset by the reduction in the contribution from the wireline business (Euro 109 million), mainly as a result of the impact of continued line loss and pricing pressure on retail revenues, notwithstanding the improvement in wholesale and data and corporate revenues.

Consolidated operating revenues - standalone revenues by segment (1) Euro million

| | 2007 | 2006 | Δ 07/06 |
|---------------------------------|----------------|----------------|-------------|
| Wireline | 1,962.4 | 2,071.8 | (5.3)% |
| Domestic mobile • TMN | 1,542.9 | 1,502.4 | 2.7% |
| Brazilian mobile • Vivo (1) | 2,463.0 | 2,104.7 | 17.0% |
| Other and eliminations | 180.1 | 86.4 | 108.4% |
| Total operating revenues | 6,148.4 | 5,765.3 | 6.6% |

(1) Considering a Euro/Real average exchange rate of 2.6661 in 2007 and 2.7315 in 2006.

Consolidated operating costs

Consolidated operating costs amounted to Euro 4,915 million in 2007, an increase of 5.5% y.o.y. On a constant currency basis, operating costs would have increased by 4.2% y.o.y. in 2007.

Consolidated operating costs (1)

Euro million

| | 2007 | 2006 | Δ 07/06 | % Rev. |
|--|---------|---------|---------|--------|
| Wages and salaries | 638.1 | 633.5 | 0.7% | 10.4% |
| Post retirement benefits | (65.1) | (72.1) | (9.8)% | (1.1)% |
| Direct costs | 907.3 | 724.9 | 25.2% | 14.8% |
| Telecommunications costs | 739.6 | 567.8 | 30.3% | 12.0% |
| Directories | 68.0 | 74.4 | (8.6)% | 1.1% |
| Other | 99.7 | 82.7 | 20.5% | 1.6% |
| Costs of products sold | 656.1 | 580.6 | 13.0% | 10.7% |
| Support services | 233.6 | 202.1 | 15.6% | 3.8% |
| Marketing and publicity | 147.2 | 138.3 | 6.5% | 2.4% |
| Supplies and external services | 945.6 | 928.5 | 1.8% | 15.4% |
| Indirect taxes | 201.8 | 175.9 | 14.7% | 3.3% |
| Provisions and adjustments | 127.0 | 216.6 | (41.4)% | 2.1% |
| Operating costs, excluding depreciation and amortisation | 3,791.7 | 3,528.3 | 7.5% | 61.7% |
| Depreciation and amortisation | 1,123.1 | 1,130.7 | (0.7)% | 18.3% |
| Total operating costs | 4,914.8 | 4,659.0 | 5.5% | 79.9% |

(1) Considering a Euro/Real average exchange rate of 2.6661 in 2007 and 2.7315 in 2006.

Wages and salaries _ Wages and salaries increased by 0.7% y.o.y. in 2007 to Euro 638 million, primarily as a result of the increase in the contributions from Vivo (Euro 13 million) and MTC (Euro 7 million), which has been consolidated since September 2006 only. These effects were partially offset by the 7.0% y.o.y decrease in wages and salaries for the wireline business as a result of the ongoing redundancy programme and the focus on containing wage increases. Wages and salaries accounted for 10.4% of consolidated operating revenues.

Post retirement benefits costs _ Post retirement benefit costs (PRB) were Euro 65 million negative (gain) in 2007, as compared to Euro 72 million negative in 2006. In 2007, post retirement benefit costs included prior year service gains amounting to Euro 110 million, mainly related to the vested rights resulting from some changes introduced in the Social Security Rules (Dec-Law 187/2007 and Law 52/2007) in order to guarantee the long-term financial sustainability of the Portuguese social security system. In 2006, post retirement benefit costs included prior year service gains amounting to Euro 151 million mainly related to the reduction in health care benefits (Euro 127 million), in connection with the changes made to Portugal

Telecom's Health Care Plan in order to maintain its long-term sustainability and financing. Excluding prior year service gains, post retirement benefit costs would have decreased from Euro 78 million in 2006 to Euro 46 million in 2007, primarily explained by the reduction in service costs, following the decrease in healthcare obligations occurred at the end of 2006, and also due to the reduction in interest costs and the increase in expected return on assets, in line with the decrease in the unfunded obligations.

Direct costs _ Direct costs increased by 25.2% y.o.y to Euro 907 million in 2007 and accounted for 14.8 of consolidated operating revenues. Telecommunications costs, which are the main component of direct costs, increased by 30.3% to Euro 740 million in 2007, with the reduction in telecommunication costs at the wireline (Euro 3 million) and domestic mobile (Euro 9 million) businesses, primarily due to lower wireline traffic volumes and lower fixed-to-mobile and mobile-to-mobile interconnection rates in Portugal, being more than offset by the increase in telecommunications costs at Vivo (Euro 168 million), mainly due to the end of the partial Bill & Keep interconnection regime (Euro 127 million).

Cost of products sold _ Cost of products sold increased by 13.0% y.o.y in 2007 to Euro 656 million. Excluding the impact of the appreciation of the Real against the Euro (Euro 11 million), costs of products sold would have increased by 11.2% y.o.y to Euro 645 million in 2007, in line with increased commercial activity in the domestic and Brazilian mobile businesses, including the introduction of the GSM by Vivo, which was partially offset by lower handset prices, benefiting from the appreciation of the Real against the Dollar.

Support services _ Support services increased by 15.6% y.o.y in 2007 to Euro 234 million and represented 3.8% of consolidated operating revenues. This growth is primarily explained by the increase in support services from Vivo (Euro 28 million) and TMN (Euro 11 million), in line with higher commercial activity in both businesses.

Marketing and publicity _ Marketing and publicity increased by 6.5% y.o.y. in 2007 to Euro 147 million, primarily due to higher contributions from TMN (Euro 4 million) and Vivo (Euro 2 million), in line with increased commercial activity in both businesses, and also due to the increase in the contribution from MTC (Euro 4 million), which has been fully consolidated since September 2006 only. Marketing and publicity expenses accounted for 2.4% of consolidated operating revenues.

Supplies and external services _ Supplies and external expenses increased by 1.8% y.o.y in 2007 to Euro 946 million. Commissions, which are the main component of supplies and external services, remaining stable at Euro 264 million. The increase in other supplies and external services, is primarily explained by higher contributions from Vivo (Euro 10 million) and MTC (Euro 7 million), which has been consolidated since September 2006 only. The increase in the contribution of Vivo is primarily explained by the appreciation of the Real against the Euro (Euro 5 million) and by the increases of electricity expenses related to the GSM network and legal fees. Supplies and external services accounted for 15.4% of consolidated operating revenues.

Indirect taxes _ Indirect taxes, which mainly include spectrum fees (TMN and Vivo) and other taxes, increased from Euro 176 million in 2006 to Euro 202 million in 2007, mainly due to the

increase in spectrum fees at Vivo and TMN in line with the growth in the customer base of both businesses.

Provisions and adjustments _ Provisions and adjustments decreased from Euro 217 million in 2006 to Euro 127 million in 2007. The decrease in this cost item is primarily related to decreases of Euro 59 million and Euro 32 million at Vivo and wireline business, respectively, mainly due to a reduction in doubtful accounts receivable at both businesses and also due to a one-off provision recorded by Vivo in 2006 (Euro 30 million) resulting from billing problems associated with the system migration to a unified platform. In 2007, provisions and adjustments accounted for 2.1% of consolidated operating revenues.

Depreciation and amortisation _ Depreciation and amortisation costs decreased by 0.7% y.o.y. in 2007 to Euro 1,123 million, with the reduction at the wireline business (Euro 32 million) being partially offset by higher contributions from Vivo (Euro 17 million), mainly due to the appreciation of the Real against the Euro (Euro 13 million), and from MTC (Euro 7 million), which has been consolidated since September 2006 only. This cost item accounted for 18.3% of consolidated operating revenues.

EBITDA

EBITDA by business segment (1) (2)

Euro million

| | 2007 | 2006 | Δ 07/06 |
|-----------------------------|---------|---------|---------|
| Wireline | 1,008.8 | 1,072.9 | (6.0)% |
| Domestic mobile • TMN | 679.0 | 658.7 | 3.1% |
| Brazilian mobile • Vivo (1) | 595.0 | 496.2 | 19.9% |
| Other | 73.9 | 9.2 | n.m. |
| Total EBITDA (2) | 2,356.7 | 2,237.0 | 5.3% |
| EBITDA margin (%) | 38.3 | 38.8 | (0.5pp) |

(1) Considering a Euro/Real average exchange rate of 2.6661 in 2007 and 2.7315 in 2006. (2) EBITDA = income from operations + depreciation and amortisation

EBITDA increased by 5.3% y.o.y in 2007 to Euro 2,357 million, equivalent to an EBITDA margin of 38.3%, a decrease of 0.5 p.p. y.o.y. EBITDA growth in the period was driven primarily by growth in mobile businesses and an increase in other businesses. Although part of the improvement in Vivo EBITDA is explained by the impact of a one-off provision recorded in 2006 (Euro 30 million), underlying EBITDA increased by 17.0% y.o.y in local currency on the back of the strong increase in top-line. TMN EBITDA increased by 3.1% y.o.y driven by robust customer growth, in voice and data, combined with strict cost control, notwithstanding increased commercial activity (+20.8% increase in net additions). Wireline EBITDA decreased by 6.0% y.o.y, mainly as a result of the decrease in prior years service gains in 2007. Excluding this impact, Wireline EBITDA would have decreased by 2.6% y.o.y in 2007, with the 1.3pp improvement in underlying EBITDA margin resulting from the continued reduction in personnel-related and other operating costs. Other EBITDA increased from Euro 9 million in 2006 to Euro 74 million in 2007, mainly as a result of the increase in the contribution of MTC (Euro 38 million), which was only fully consolidated since September 2006, and the increase in EBITDA of other fully consolidated subsidiaries.

Net income

Curtailment costs, net _ Curtailment costs amounted to Euro 276 million in 2007, including a cost of Euro 289 million related to the reduction of 1,004 employees and a gain of Euro 14 million related with the settlement of benefits. In 2006 curtailment costs amounted to Euro 19 million due to the booking of net gains of Euro 209 million related to the termination of the protocol with the national healthcare system. Work force reduction programme costs in 2006 amounted to Euro 228 million corresponding to the reduction of 772 employees.

Net interest expenses _ Net interest expenses decreased by 10.3% y.o.y to Euro 197 million in 2007, mainly as a result of the reduction in the average cost of debt in Portugal and Brazil, as well as the decrease in Vivo's average net debt in the period, and notwithstanding the increase in PT's average net debt in the period due to the execution of the share buyback. Excluding Brazil and the interest cost associated with PTM equity swap (settled in the second quarter of 2007), PT's the average cost of debt was 3.7% in 2007, as compared to 3.8% in 2006.

Net foreign currency exchange losses/(gains) _ Net foreign currency exchange losses amounted to Euro 12 million in 2007, as compared to net foreign currency exchange gains of Euro 4 million in 2006. In 2007 and 2006, this item included mainly foreign currency losses related to dividends receivable from Unitel (denominated in US Dollars), following the devaluation of the US Dollar against the Euro in both periods, and foreign currency gains related to Vivo's US Dollar debt not swapped to Reais, in connection with the appreciation of the Real against the Dollar in both periods.

Gains on financial assets and other investments, net _ Net gains on financial assets amounted to Euro 249 million in 2007, as compared to net gains of Euro 18 million in 2006. This caption includes mainly the following: (1) the sale of 22% of Africatel (gain of Euro 111 million in 2007), the holding company that aggregates all of PT's interests in Africa excluding Médi Télécom; (2) equity swap contracts on PT Multimedia shares (gains of Euro 77 million in 2007, as compared to 10 million in 2006); (3) the financial settlement of equity swaps over PT's own shares (gains of Euro 32 million in 2007, as compared to Euro 24 million in 2006); and (4) the disposal of the investment in BES (gain of Euro 36 million in 2007).

Equity in earnings of associated companies, net _ Equity in earnings of associated companies decreased 3.4% to Euro 126 million in 2007, as compared to Euro 131 million in 2006, on the back of the reduction in the contribution from Médi Télécom (Euro 3 million in 2007 vs. Euro 46 million in 2006) resulting primarily from the recognition in 2006 of tax losses carried forward from previous years. This item included mainly PT's share in the earnings of Unitel in Angola (Euro 92 million in 2007, as compared to Euro 82 million in 2006), CTM in Macao (Euro 17 million in 2007, as compared to Euro 15 million in 2006) and UOL (Euro 13 million in 2007, as compared to Euro 6 million in 2006).

Net other financial expenses _ Net other financial expenses decreased 6.7% to Euro 48 million in 2007, as compared to Euro 52 million in 2006 and included mainly banking services, commissions, financial discounts and other financing costs. The reduction in this cost item is primarily explained by the financial taxes paid by Vivo in 2006, in connection with its debt restructuring occurred in that period.

Provision for income taxes _ Provision for income taxes amounted to Euro 243 million in 2007, as compared to a gain of Euro 21 million in 2006. The increase in this caption is primarily explained by the recognition in 2006 of: (1) a tax credit amounting to Euro 53 million, following the liquidation of a holding company, (2) a Euro 142 million gain related the reduction of deferred tax liabilities resulting from the voluntary taxation of certain capital gains, and (3) tax losses from previous periods amounting to Euro 134 million at Vivo following the completion of its corporate restructuring. Adjusting for these one-off effects, provision for income taxes would have been Euro 308 million in 2006, with the adjusted effective tax rate falling from 36% in 2006 to 24% 2007 mainly as a result: (1) the reduction in allowances for deferred taxes on tax losses generated by Vivo, following the corporate restructuring completed in the end of 2006; (2) the reduction in the statutory tax rate in Portugal from 27.5% in 2006 to 26.5% in 2007; and (3) the booking of non-taxable capital gains in 2007 related to the disposals of 22% of Africatel and of the investment in shares of BES.

Net income from discontinued operations _ Net income from discontinued operations includes the results of companies that have been disposed during the reportable periods, and the after-tax gains obtained with the sale of these investments. Following the approval of the spin-off of PT Multimedia in PT 's Annual General Meeting hold on 27 April 2007, this business was reported as a discontinued operation in all reportable periods, in accordance with IFRS rules. As a result, the earnings of PT Multimedia before minority interest until the conclusion of the spin-off process that occurred in November 2007 were included in this caption. In 2007, this caption

included costs related to the spin-off process amounting to Euro 18 million, net of tax, in connection with employee, organisational and IT restructuring costs.

Minority interests _ Income attributable to minority interests increased to Euro 93 million in 2007 from Euro 87 million in 2006, mainly due to the increase in income attributable to the minority interests of MTC (from Euro 9 million in 2006 to Euro 23 million in 2007), which has been consolidated since September 2006 only, and Africatel (Euro 10 million in 2007), following the disposal of a 22% stake of this investment in July 2007. These effects were partially offset by the decrease in the income attributable to minority interests of Vivo (from Euro 34 million in 2006 to Euro 15 million in 2007), primarily explained by the share of minority interests in the tax gains booked by Vivo in 2006.

Net income _ Net income decreased by 14.4% y.o.y in 2007 to Euro 742 million, primarily as a result of the increase in curtailment costs in 2007 and lower provision for income taxes in 2006, which more than offset the increase in EBITDA and higher net financial gains.

Capex

Capex by business segment (1)

Euro million

| | 2007 | 2006 | Δ 07/06 |
|-----------------------------|-------|-------|---------|
| Wireline (2) | 292.1 | 238.5 | 22.5% |
| Domestic mobile • TMN (3) | 182.9 | 188.6 | (3.0)% |
| Brazilian mobile • Vivo (1) | 359.9 | 386.8 | (7.0)% |
| Other | 64.4 | 53.8 | 19.7% |
| Total capex | 899.3 | 867.7 | 3.6% |
| Capex as % of revenues (%) | 14.6 | 15.1 | (0.4pp) |

(1) Considering a Euro/Real average exchange rate of 2.6661 in 2007 and 2.7513 in 2006. (2) Includes the capitalisation of Euro 43 million related with transponder satellite capacity for the DTH offer. (3) Excludes the commitments under the terms of the UMTS licence (Euro 242 million in 2007).

Capex amounted to Euro 899 million in 2007, equivalent to 14.6% of revenues. The increase in Wireline capex was primarily due to: (1) network upgrades to provide greater bandwidth, in part related to IPTV services launched in June 2007; (2) the capitalisation of transponder satellite capacity for the DTH offer, and (3) client-related capex. This increase was partially offset by the decrease in Vivo and TMN's capex, with this being directed mostly towards build up of network capacity and 3G/3.5G coverage. Capex at Vivo was directed towards the GSM/EDGE overlay as well as network coverage and capacity. Other capex includes capex related to consolidated businesses not included in the main segments and support companies. In 2007, other capex increased to Euro 64 million, as compared to Euro 54 million in 2006, mainly as a result of the consolidation of MTC (Euro 17 million) from September 2006.

Cash flow

EBITDA minus Capex by business segment (1)

Euro million

| | 2007 | 2006 | y.o.y |
|-----------------------------|---------|---------|---------|
| Wireline | 716.7 | 834.3 | (14.1)% |
| Domestic mobile • TMN | 496.1 | 470.1 | 5.5% |
| Brazilian mobile • Vivo (1) | 235.1 | 109.4 | 114.9% |
| Other | 9.5 | (44.6) | n.m. |
| Total EBITDA minus Capex | 1,457.4 | 1,369.3 | 6.4% |

(1) Considering a Euro/Real average exchange rate of 2.6661 in 2007 and 2.7315 in 2006.

EBITDA minus Capex _ EBITDA minus Capex increased by 6.4% y.o.y to Euro 1,457 million in 2007. On a combined basis, the domestic businesses accounted for approximately 83% of total EBITDA minus Capex.

| Free cash flow | Euro million | | |
|---|--------------|-------------|--------------|
| | 2007 | 2006 | y.o.y |
| Operating free cash flow | 1,432.8 | 1,586.6 | (9.7)% |
| Net disposal (acquisition) of financial investments | 238.5 | (142.3) | n.m. |
| Interest paid | (234.3) | (311.0) | (24.7)% |
| Contributions and payments related to PRBs | (167.2) | (278.5) | (40.0)% |
| Financial settlement of PTM equity swap | 94.5 | 0.0 | n.m. |
| Income taxes paid | (206.5) | (47.9) | n.m. |
| Other cash movements (1) | 83.8 | 17.9 | n.m. |
| Free cash flow | 1,241.6 | 824.9 | 50.5% |

(1) In 2007, other cash movements included Euro 149 million related to dividends received, mainly from PTM (Euro 54 million) and Unitel (Euro 73 million).

Operating free cash flow _ In 2007, operating free cash flow decreased by 9.7% y.o.y to Euro 1,433 million. The reduction in operating cash flow is explained by the working capital investment in 2007, versus a divestment in 2006, primarily as a result of higher commercial activity at TMN and Vivo.

Free cash flow _ Free cash flow increased from Euro 825 million in 2006 to Euro 1,242 million in 2007, primarily as a result of: (1) the increase in net disposal of financial investments, mainly due to disposals of Africatel and BES in 2007 amounting to Euro 117 million and Euro 110 million, respectively, as compared to the investment in MTC of Euro 109 million in 2006; (2) the cash settlement of the PTM equity swap in 2007 (Euro 94 million); (3) lower interest paid, and (4) lower contributions and payments related to post retirement benefits, as a result of the Euro 87 million reimbursement made in 2007 by PT Prestações, the fund created to cover

healthcare responsibilities, on account of healthcare expenses paid by PT in previous years. These effects were only partially offset by higher income taxes paid, as PT's tax losses carried forward were fully used in 2006. The reduction in interest paid from Euro 311 million in 2006 to Euro 234 million in 2007, is primarily explained by the fact that PT paid in 2006 the last annual interest installment (Euro 52 million) on the Eurobond repaid in 2006 and by the decrease in Vivo's interest payments following its debt restructuring undertaken in 2006.

Consolidated balance sheet (1)

Euro million

| | 31 December 2006 | 31 December 2006 |
|---|-------------------------|-------------------------|
| Cash and equivalents | 1,834.9 | 2,083.7 |
| Accounts receivable, net | 1,441.8 | 1,417.0 |
| Inventories, net | 160.6 | 130.3 |
| Financial investments | 565.3 | 631.5 |
| Intangible assets, net | 3,383.1 | 3,490.9 |
| Tangible assets, net | 3,585.4 | 3,942.0 |
| Post retirement benefits | 134.1 | 134.1 |
| Other assets | 910.7 | 1,050.5 |
| Deferred tax assets and prepaid expenses | 1,106.2 | 1,291.4 |
| Total assets | 13,122.2 | 14,171.2 |
| Accounts payable | 1,108.9 | 1,115.1 |
| Gross debt | 6,216.8 | 5,840.3 |
| Post retirement benefits | 1,463.9 | 1,807.6 |
| Other liabilities | 1,878.4 | 1,995.7 |
| Deferred tax liabilities and deferred income | 372.3 | 306.5 |
| Total liabilities | 11,040.4 | 11,065.2 |
| Equity before minority interests | 1,338.2 | 2,255.2 |
| Minority interests | 743.6 | 850.8 |
| Total shareholders' equity | 2,081.8 | 3,106.0 |
| Total liabilities and shareholders' equity | 13,122.2 | 14,171.2 |

(1) Considering the Euro/Real exchange rate of 2.5963 at the end of 2007 and 2.8118 at the end of 2006.

Assets and liabilities _ The decrease in assets and liabilities in 2007 is primarily explained by the conclusion of the spin-off process of PT Multimedia occurred on November 2007.

The net exposure to Brazil _ The net exposure (assets minus liabilities) to Brazil amounted to R\$ 7,525 million as at 31 December 2007 (Euro 2,898 million at the Euro/Real exchange rate prevailing as at 31 December 2007). The assets denominated in Brazilian Reais in the balance sheet as at 31 December 2007 amounted to Euro 5,454 million, equivalent to approximately 41.6% of total assets.

Gearing ratio _ The gearing ratio [net debt / (net debt + shareholders' equity)] increased to 67.8% as at 31 December 2007, from 54.7% as at 31 December 2006, while the shareholders' equity plus long-term debt to total assets ratio increased from 53.4% to 53.7%. As at 31 December 2007, the net debt to EBITDA ratio was 1.9 times and EBITDA cover was 11.9 times.

Consolidated net debt

| Change in net debt | Euro million | |
|---|--------------|---------|
| | 2007 | 2006 |
| Net debt (initial balance) | 3,756.6 | 3,672.5 |
| Less: PTM Net debt as at 31 December 2006 | 178.9 | 0.0 |
| Less: Free cash flow | 1,241.6 | 824.9 |
| Less:PTM free cash flow | 0.0 | (74.0) |
| Commitments under the UMTS license | 241.7 | 0.0 |
| Translation effect on foreign currency debt | 32.6 | (12.1) |
| Dividends paid (1) | 552.7 | 552.2 |
| Acquisitions of treasury shares (2) | 1,158.3 | 62.1 |
| Extraordinary contribution to pension fund | 117.0 | 302.3 |
| Other | (56.6) | (69.5) |
| Net debt (final balance) | 4,381.8 | 3,756.6 |
| Change in net debt | 625.3 | 84.1 |
| Change in net debt (%) | 16.6% | 2.3% |

(1) In 2007, this item included dividends paid by PT (Euro 517 million) and certain of its subsidiaries. (2) In 2007, this item corresponds to the notional amount of equity swaps contracted over 117.7 million PT shares, in connection with the share buyback programme announced by the Board of Directors on 20 February 2007 and approved at the AGM of 27 April 2007.

Net debt _ Consolidated net debt as at 31 December 2007 increased to Euro 4,382 million, as compared to Euro 3,757 million as at 31 December 2006. The increase in net debt over the period is primarily explained by: (1) the share buyback, currently under execution; (2) the recognition of the investments in UMTS commitments, and (3) the extraordinary contribution to the pension fund.

Consolidated net debt

Euro million

| | 31 December 2007 | 31 December 2006 | Change | Change (%) |
|---|------------------|------------------|---------|------------|
| Short-term | 1,256.1 | 1,372.7 | (116.6) | (8.5)% |
| Bonds | 96.3 | 0.0 | 96.3 | n.m. |
| Bank loans | 431.3 | 406.9 | 24.4 | 6.0% |
| Other loans | 324.0 | 749.9 | (425.9) | (56.8)% |
| Commitments under the UMTS license | 55.9 | 0.0 | 55.9 | n.m. |
| Liability with equity swaps on own shares | 323.2 | 187.6 | 135.6 | 72.3% |
| Financial leases | 25.5 | 28.4 | (2.9) | (10.3)% |
| Medium and long-term | 4,960.7 | 4,467.4 | 493.3 | 11.0% |
| Exchangeable bonds | 689.4 | 0.0 | 689.4 | n.m. |
| Bonds | 3,061.7 | 3,133.6 | (71.9) | (2.3)% |
| Bank loans | 940.9 | 1,103.3 | (162.4) | (14.7)% |
| Commitments under the UMTS license | 144.7 | 0.0 | 144.7 | n.m. |
| Other loans | 0.0 | 0.3 | (0.3) | n.m. |
| Financial leases | 124.0 | 230.2 | (106.2) | (46.1)% |
| Gross debt | 6,216.8 | 5,840.2 | 376.6 | 6.4% |
| Cash and equivalents | 1,834.9 | 2,083.7 | (248.8) | (11.9)% |
| Net debt | 4,381.8 | 3,756.6 | 625.3 | 16.6% |

Total debt _ As at 31 December 2007, 79.8% of total debt was medium and long-term, while 64.0% of total debt was at fixed rates. As at 31 December 2007, 85.7% of total debt was denominated in Euros, 0.1% in US Dollars and 14.1% in Brazilian Reais. PT's rating was confirmed as Baa2 by Moody's and BBB- by S&P, both with stable outlook, on 5 March 2007 and 16 March 2007, respectively. The total undrawn amount of PT's domestic commercial paper lines and standby facilities stood at Euro 1,451 million as at 31 December 2007. The amount of available cash from the domestic operations plus the undrawn amount of PT's domestic commercial paper lines and standby facilities totalled Euro 2,672 million at the end of December 2007.

The 50% share of Vivo's net debt, proportionally consolidated by PT, amounted to Euro 370 million as at 31 December 2007. Approximately 95% of Vivo's net debt is either Real-denominated or has been swapped into Reais.

Net debt maturity profile

Euro million

| Maturity | Net debt | Notes |
|--------------------|----------|---|
| 2008 | (578.9) | Net cash position |
| 2009 | 1,122.5 | Includes a Euro 880 million Eurobond issued in April 1999 |
| 2010 | 226.3 | |
| 2011 | 159.8 | |
| 2012 | 1,282.2 | Includes a Euro 1,000 million Eurobond issued in March 2005 |
| 2013 | 67.4 | |
| 2014 | 881.6 | Includes a Euro 689 million related to the exchangeable bonds issued in August 2007 |
| 2015 | 225.4 | |
| 2016 | 0.0 | |
| 2017 and following | 995.4 | Includes a Euro 500 million Eurobond issued in March 2005 (matures in 2017) and a Euro 500 million Eurobond issued in June 2005 (matures in 2025) |
| Total | 4,381.8 | |

Cost of debt and maturity _ PT's average cost and maturity of net debt in 2007 was 4.9% and 6.7 years, respectively, including loans obtained in Brazil and denominated in Reais. Excluding Vivo's debt and the interest cost associated with the equity swap over PT Multimedia shares, PT's average cost of debt was 3.7% in 2007. The maturity of the net debt excluding Brazil also amounted to 6.7 years at 31 December 2007.

Debt ratings

| | Current | Outlook | Last change |
|-------------------|---------|----------|---------------|
| Standard & Poor's | BBB- | Stable | 16 March 2007 |
| Moody's | Baa2 | Stable | 5 March 2007 |
| Fitch Ratings | BBB | Negative | 5 March 2007 |

Ratings _ Following the failure of the tender offer, rating agencies confirmed PT's rating of BBB- (S&P), Baa2 (Moody's) and BBB (Fitch).

Post retirement benefits

PBO _ As at 31 December 2007, the projected benefit obligations (PBO) of PT's post retirement benefits, including pensions, healthcare obligations and salaries to pre-retired and suspended employees, amounted to Euro 4,203 million. The PBO was computed based on a discount rate of 5.25% for pension and healthcare obligations, and 4.75% for the obligations related to the payment of salaries to pre-retired and suspended employees. PT's post retirement benefits plans are closed to new participants since 1994 for pensions and 2000 for healthcare.

| Post retirement benefits obligations | Euro million | | |
|---|--------------|-----------|---------|
| | 2007 | 2006 | Change |
| Pension obligations | 2,762.1 | 3,073.8 | (311.7) |
| Salaries to suspended and pre-retired employees | 985.7 | 997.7 | (12.0) |
| Healthcare obligations | 455.3 | 491.1 | (35.8) |
| Projected benefit obligation (PBO) | 4,203.0 | 4,562.6 | (359.6) |
| Market value of funds | (2,899.1) | (2,908.1) | 9.0 |
| Gross unfunded obligation | 1,304.0 | 1,654.4 | (350.5) |
| Unrecognised prior years service gains | 25.9 | 19.1 | 6.8 |
| Net liability for post retirement benefits | 1,329.9 | 1,673.5 | (343.6) |
| After-tax unfunded obligations | 958.4 | 1,216.0 | (257.6) |

Change in plans _ In 2007, following the introduction of changes to the Social Security rules (DL 187/2007 and Law 52/2007) and adjustments introduced by PT to the growth rate used to calculate pension complements, the PBO was reduced by Euro 122 million. The impact of this reduction includes Euro 110 million related to vested rights that were recognised as prior year service gains and Euro 11 million related to unvested rights, which are deferred and amortised over the average working life of active employees. In addition, PT settled the Marconi Melhoria plan, which resulted in a reduction of unfunded liabilities by Euro 14 million, recognised as curtailment gains. In summary, gross unfunded obligations amounted to Euro 1,304 million at the end of 2007, whilst after tax unfunded obligations stood at Euro 958 million.

Change in gross unfunded obligations

Euro million

| | 2007 | 2006 | Change | Change (%) |
|--|---------|---------|---------|------------|
| Gross unfunded obligations (initial balance) | 1,654.4 | 2,635.9 | (981.4) | (37.2)% |
| Changes in the consolidation perimeter | 0.0 | 2.5 | (2.5) | |
| Post retirement benefits costs (PRBs) (1) | (63.1) | (72.1) | 9.0 | |
| Prior years service gains not recognized in net income | (11.1) | (19.1) | 7.9 | |
| Curtailed cost (2) | 293.2 | 7.4 | 285.8 | |
| Contributions and payments (3) | (284.2) | (580.8) | 296.6 | |
| Net actuarial losses | (285.2) | (319.4) | 34.2 | |
| Gross unfunded obligations (final balance) | 1,304.0 | 1,654.4 | (350.4) | (21.2)% |
| After-tax unfunded obligations | 958.4 | 1,216.0 | (257.6) | (21.2)% |

(1) In 2007, the post retirement benefits gain recorded in the income statement amounted to Euro 65 million, including a gain of Euro 2 million related to the amortisation of prior years service gains on unvested rights. (2) In 2007 curtailment cost recorded in the income statement amounted to Euro 276 million, and excludes Euro 15 million related to the spin-off of PTM which were recorded under discontinued operations and includes a gain of Euro 2 million related to the extraordinary recognition of deferred prior years service gains. (3) In 2007 this caption included: (i) Euro 38 million of regular contributions; (ii) Euro 175 million of payments of salaries to pre-retired and suspended employees and other; (iii) Euro 61 million of net refunds related to healthcare benefits, and (iv) Euro 117 million of an extraordinary contributions to the pensions funds.

Gross unfunded obligations _ The decrease in the gross unfunded obligations by Euro 351 million in 2007 to Euro 1,304 million is primarily explained by: (1) the net actuarial gains booked in the period in the amount of Euro 285 million; (2) the reduction and settlement of benefits in the amount of Euro 135 million, and (3) the Euro 117 million extraordinary contribution made in 2007, notwithstanding the Euro 291 million work force reduction costs incurred in the period.

Net actuarial gains _ Net actuarial gains in 2007 include the impacts of the changes in actuarial assumptions (Euro 151 million) and of the differences between those actuarial assumptions and real data (Euro 134 million). The change in actuarial assumptions corresponds to the net effect of: (i) the increase in the discount rate from 4.75% to 5.25% for pension liabilities and from 4.25% to 4.75% for salary liabilities, reflecting the evolution of market yields; (ii) the reduction in the salary growth rate from 2.25% to 2.00%; and (iii) the increase in the inflation rate from 1.75% to 2.00%.

Post retirement benefits costs

Euro million

| | 2007 | 2006 |
|---|---------|---------|
| Service cost | 17.8 | 28.7 |
| Interest cost | 208.9 | 217.5 |
| Expected return on assets | (179.4) | (167.7) |
| Prior years service gains (1) | (112.3) | (150.6) |
| Post retirement benefits costs | (65.1) | (72.1) |
| Curtailed costs related to PRBs | | |
| PBO related | 291.7 | 227.8 |
| Recognition of deferred prior years service gains | (2.3) | 0.0 |
| Settlement of benefits | (13.8) | (208.9) |
| Curtailed costs, net | 275.6 | 19.0 |

(1) In 2007, this item includes Euro 110 million related to vested rights and Euro 2 million related to the amortisation of prior years service gains on unvested rights.

Post retirement benefit costs _ Post retirement benefit costs were Euro 65 million negative (gain) in 2007, compared with a gain of Euro 72 million in 2006, mainly as a result of the decrease in prior years service gains of Euro 40 million recorded in the period. The decrease in service cost in 2007 is explained primarily by the reduction in healthcare obligations that occurred at the end of 2006, while the decrease in net interest cost is explained by the narrowing of the unfunded gap.

Shareholders' equity (excluding minority interests)

Shareholders' equity _ As at 31 December 2007, shareholders' equity excluding minority interests amounted to Euro 1,338 million, a decrease of Euro 917 million during 2007.

| Change in shareholders' equity (excluding minority interests) | Euro million |
|--|--------------|
| | 2007 |
| Equity before minority interests (initial balance) | 2,255.2 |
| Net income | 741.9 |
| Currency translation adjustments (1) | 204.1 |
| Net actuarial gains, net of tax effect | 209.6 |
| Dividends paid | (516.5) |
| Spin-off of the Multimedia business | (405.3) |
| Acquisition of treasury stock (2) | (1,158.3) |
| Market value of the exchangeable bond option | 57.1 |
| Hedge accounting of financial instruments and change in the fair value of available for sale investments (3) | (20.3) |
| Other (4) | (29.4) |
| Equity before minority interests (final balance) | 1,338.2 |
| Change in equity before minority interests | (917.0) |
| Change in equity before minority interests (%) | (40.7)% |

(1) This item is primarily related to the appreciation of the Real against the Euro from 2.8118 as at 31 December 2006 to 2.5963 as at 31 December 2007. (2) This item is related to the notional amount of equity swaps contracted during the period over 117.7 million own shares. (3) In 2007, this item includes Euro 36 million corresponding to the offset of the gain obtained on the disposal of the investment in the shares of Banco Espírito Santo recorded in the income statement in 2Q07. (4) This item includes primarily Euro 28 million related to price resets on existing equity swap contracts on own shares.

Distributable reserves _ Pursuant to Portuguese legislation, the amount of distributable reserves is determined according to the standalone financial statements of the company prepared in accordance with Portuguese GAAP. Distributable reserves decreased from Euro 2,728 million in 2006 to Euro 1,856 million in 2007.

| Change in distributable reserves | Euro million |
|--|--------------|
| | 2007 |
| Distributable reserves (initial balance) | 2,727.8 |
| Dividends paid | (516.5) |
| Spin-off of the Multimedia business | (374.7) |
| Net income under Portuguese GAAP | 613.5 |
| Share capital restructuring | 440.3 |
| Acquisition of treasury shares (1) | (1,050.3) |
| Other | 16.5 |
| Distributable reserves (final balance) | 1,856.5 |
| Change in distributable reserves in the period | (871.3) |
| Change in distributable reserves in the period (%) | (31.9)% |

(1) In 3Q07, PT acquired 103 million own shares for a total amount of Euro 1,050 million, through the exercise of the physical settlement option of equity swaps contracted under the share buyback programme currently being executed.

02 Business performance

Domestic market

Wireline

Operating revenues _ Wireline operating revenues decreased by 5.3% y.o.y in 2007 to Euro 1,962 million, with the reduction in retail revenues more than offsetting the increase in wholesale and data and corporate revenues in the period.

Wireline income statement (1)

Euro million

| | 2007 | 2006 | y.o.y |
|--|---------|---------|---------|
| Operating revenues | 1,962.4 | 2,071.8 | (5.3)% |
| Retail | 1,023.2 | 1,173.5 | (12.8)% |
| Voice | 841.1 | 993.2 | (15.3)% |
| Data and other | 182.1 | 180.3 | 1.0% |
| Wholesale | 486.9 | 464.2 | 4.9% |
| Data and corporate | 265.6 | 250.5 | 6.0% |
| Other wireline revenues | 186.7 | 183.6 | 1.7% |
| Operating costs, excluding D&A | 953.6 | 998.9 | (4.5)% |
| Wages and salaries | 252.9 | 272.0 | (7.0)% |
| Post retirement benefits | (65.3) | (71.6) | (8.7)% |
| Direct costs | 354.0 | 356.1 | (0.6)% |
| Commercial costs | 90.8 | 83.3 | 9.0% |
| Other operating costs | 321.2 | 359.1 | (10.5)% |
| EBITDA (2) | 1,008.8 | 1,072.9 | (6.0)% |
| EBITDA, excluding exceptional items (3) | 898.5 | 922.3 | (2.6)% |
| Depreciation and amortisation | 323.6 | 355.5 | (9.0)% |
| Income from operations (4) | 685.2 | 717.3 | (4.5)% |
| EBITDA margin | 51.4% | 51.8% | (0.4pp) |
| EBITDA margin, excluding exceptional items | 45.8% | 44.5% | 1.3pp |
| Capex (5) | 292.1 | 238.5 | 22.5% |
| Capex as % of revenues | 14.9% | 11.5% | 3.4pp |
| EBITDA minus Capex | 716.7 | 834.3 | (14.1)% |

(1) Includes intragroup transactions.

(2) EBITDA = income from operations + depreciation and amortisation.

(3) Adjusts for prior years service gains related to vested rights in the amount of Euro 110 million in 2007 and Euro 151 million in 2006.

(4) Income from operations = income before financials and income taxes + curtailment costs + losses (gains) on disposal of fixed assets + net other costs.

(5) Includes the capitalisation of Euro 43 million related with transponder satellite capacity for the DTH offer.

Retail revenues _ Retail revenues fell by 12.8% y.o.y in 2007 on the back of continued competition from other fixed operators as well as increasing competition from mobile operators, both in voice and broadband. Voice revenues decreased by 15.3% y.o.y in 2007, as a result of line loss and increasing pricing pressure, particularly in unbundled local loop (ULL) areas. Data revenues increased by 1.0% y.o.y, notwithstanding the decrease in ADSL retail customers, due to the database cleanup undertaken at the end of the year, and the increasing pricing pressure in broadband, from both fixed and mobile operators.

Wholesale revenues _ Wholesale revenues increased by 4.9% y.o.y in 2007, primarily as a result of the growth in wholesale line rental and ULL on the back of increasing ULL accesses (+48.7% y.o.y).

Data and corporate revenues _ Data and corporate revenues increased by 6.0% y.o.y in 2007, as a result of continued focus on providing corporate customers more advanced and customised solutions combining telecoms and IT. The growth in the period was underpinned by the increase in revenues from VPN and circuits, as well as from outsourcing, network management and IT/SI solutions.

Other revenues _ Other revenues increased by 1.7% y.o.y in 2007, with the the growth in portal revenues (+49.2% y.o.y) and in equipment sales (+23.6% y.o.y) more than offsetting the decrease in directories (-9.9% y.o.y).

EBITDA _ EBITDA amounted to Euro 1.009 million in 2007, decreasing by 6.0% y.o.y. The reduction in EBITDA is explained primarily by decrease in prior years service gains from Euro 151 million in 2006 to Euro 110 million in 2007. Excluding the impact of this exceptional item, underlying EBITDA would have decreased by 2.6% y.o.y, with the 1.3pp improvement in underlying EBITDA margin resulting from the continued reduction in personnel-related and other operating costs. In effect, in 2007, wages and salaries decreased by 7.0% y.o.y while other operating costs decreased by 10.5% y.o.y. The net reduction in headcount in 2007 reached 827 employees, improving the efficiency ratio to 657 lines per employee in 2007 from 613 in 2006.

Capex _ Capex amounted to Euro 292 million in 2007, equivalent to 14.9% of operating revenues, and included Euro 43 million related to the capitalisation of the long-term contracts for transponder satellite capacity for the DTH offer, which will be made available in the Summer of 2008. Capex was directed mainly towards: (1) network upgrades to provide greater bandwidth to customers; (2) network capacity and information systems to provide IPTV services (soft launch in the second quarter of 2007), and (3) client-related capex as a result of investments in terminal equipment for both residential and corporate clients. EBITDA minus Capex amounted to Euro 717 million in 2007.

ADSL _ ADSL retail accesses decreased to 652 thousand in 2007, as a result of the database cleanup (mainly related to inactive prepaid broadband customers) of 103 thousand. Adjusting for this impact, ADSL net additions in the period reached 70 thousand. Voice lines fell by 9.2% y.o.y to 3,010 thousand, as a result of 136 thousand net disconnections of traffic-generating

lines (an improvement over 2006 with net disconnections of 285 thousand) and the 170 thousand net disconnections of carrier press-selection lines. In terms of competitors' lines, voice-only lines (carrier pre-selection + wholesale line rental) decreased by 172 thousand in 2007, while ULL lines increased by 95 thousand. The growing presence of GSM-based fixed offers and wireless broadband has contributed further to fixed-mobile migration, while the increase in voice net additions of cable competitors, on the back of aggressively priced and promoted triple-play offers, continued to impact line loss.

IPTV _ In terms of triple-play services, PT launched its IPTV-based offer at the end of June 2007. At the end of 2007, PT had added a total of 21 thousand IPTV customers. The triple-play offer includes 42 pay-TV channels (of which 10 are a la carte), a broadband access of up to 8Mbps and unlimited fixed-to-fixed calls. Additionally, customers can buy premium services, such as SportTV (premium sports), premium movie channels and VOD services. This triple-play service is provided using ADSL 2+. PT was the first operator in Portugal to introduce HDTV and has the most extensive VOD offer in the market.

Wireline operating data

| | 2007 | 2006 | y.o.y |
|---------------------------------|--------|--------|---------|
| Main accesses (000) | 4,176 | 4,404 | (5.2)% |
| Retail accesses | 3,682 | 4,001 | (8.0)% |
| PSTN/ISDN | 3,010 | 3,317 | (9.2)% |
| Traffic-generating lines | 2,772 | 2,909 | (4.7)% |
| Carrier pre-selection | 238 | 408 | (41.7)% |
| ADSL retail (1) | 652 | 685 | (4.9)% |
| TV subscribers | 21 | 0 | n.m. |
| Wholesale accesses | 494 | 403 | 22.6% |
| Unbundled local loops | 291 | 196 | 48.7% |
| Wholesale line rental | 140 | 142 | (1.4)% |
| ADSL wholesale | 62 | 65 | (3.5)% |
| Net additions (000) | (227) | (74) | n.m. |
| Retail accesses | (319) | (353) | (9.8)% |
| PSTN/ISDN | (306) | (453) | (32.3)% |
| Traffic-generating lines | (136) | (285) | (52.2)% |
| Carrier pre-selection | (170) | (168) | 1.4% |
| ADSL retail | (33) | 100 | n.m. |
| TV subscribers | 21 | 0 | n.m. |
| Wholesale accesses | 91 | 279 | (67.4)% |
| Unbundled local loops | 95 | 124 | (22.9)% |
| Wholesale line rental | (2) | 142 | n.m. |
| ADSL wholesale | (2) | 13 | n.m. |
| ARPU (Euro) | 30.4 | 30.1 | 1.1% |
| Voice | 24.5 | 25.0 | (2.2)% |
| Data and other | 5.9 | 5.0 | 17.5% |
| Total traffic (million minutes) | 12,502 | 13,442 | (7.0)% |
| Retail traffic | 5,217 | 5,575 | (6.4)% |
| Wholesale traffic | 7,285 | 7,867 | (7.4)% |
| Retail MOU (minutes / month) | 159 | 158 | 0.6% |
| Employees | 6,354 | 7,181 | (11.5)% |

(1) Includes a database cleanup (related to inactive prepaid broadband customers) of 103 thousand.

Fixed-mobile convergent products _ In addition, PT has begun to rollout fixed-mobile convergent products to its SME/SoHo and residential segments as a means to increase revenues and improve customer loyalty. After having developed a mobile OfficeBox offer in the first half of 2007, PT has now integrated fixed voice and broadband, as well as a PC, into an upgraded version of the OfficeBox product (see description in domestic mobile section - TMN for further detail). With regards to the residential segment, PT launched a wireless broadband offer also using the brand Sapo Mobile (Sapo is the fixed ADSL brand). Customers can opt between a monthly flat rate or alternatively a daily usage rate in case they also subscribe to a fixed ADSL

monthly package, thus benefiting from a fixed and mobile bundle and increasing the perceived value attributed to the fixed broadband offer.

ARPU _ Blended ARPU, which was not impacted by the database cleanup undertaken at the end of the year, increased by 1.1% y.o.y in 2007 to Euro 30.4 driven by the growth in data ARPU, which increased by 17.5% y.o.y. The increased penetration of data services, including corporate VoIP and IPTV, more than offset the reduction in voice and broadband ARPU.

Traffic _ Although retail traffic fell by 6.4% y.o.y. in 2007, as a result of line loss, retail MOU increased by 0.6% y.o.y in the period to 159 minutes, reflecting the positive impact of the rollout of flat-rate pricing plans. The 7.4% y.o.y reduction in wholesale traffic in 2007 is explained primarily by the 58.8% y.o.y decrease in dial-up Internet traffic, as a result of the continued migration to broadband.

Domestic mobile - TMN

Operating revenues _ Operating revenues increased by 2.7% y.o.y in 2007 to Euro 1,543 million, supported by the growth of service revenues (+2.2% y.o.y) and equipment sales (+9.3% y.o.y), as a result of the successful TMN s campaigns, namely the Summer and Christmas campaigns. Customer revenues increased by 2.6% y.o.y to Euro 1,146 million on the back of strong customer growth, particularly in postpaid and wireless broadband.

Interconnection revenues grew 0.3% y.o.y. in 2007 to Euro 247 million, notwithstanding the negative impact from the reduction of mobile termination rates (MTR). Excluding this impact (Euro 14 million), service revenues would have increased by 3.2% y.o.y in 2007.

Domestic mobile income statement (1)

Euro million

| | 2007 | 2006 | y.o.y |
|--------------------------------|---------|---------|---------|
| Operating revenues | 1,542.9 | 1,502.4 | 2.7% |
| Services rendered | 1,393.1 | 1,363.2 | 2.2% |
| Customer | 1,146.2 | 1,117.0 | 2.6% |
| Interconnection | 246.9 | 246.2 | 0.3% |
| Sales | 141.8 | 129.7 | 9.3% |
| Other operating revenues | 8.1 | 9.4 | (14.3)% |
| Operating costs, excluding D&A | 864.0 | 843.7 | 2.4% |
| Wages and salaries | 52.7 | 56.0 | (5.8)% |
| Direct costs | 282.6 | 292.9 | (3.5)% |
| Commercial costs | 318.3 | 306.6 | 3.8% |
| Other operating costs | 210.4 | 188.2 | 11.8% |
| EBITDA (2) | 679.0 | 658.7 | 3.1% |
| Depreciation and amortisation | 223.6 | 220.1 | 1.6% |
| Income from operations (3) | 455.4 | 438.6 | 3.8% |
| EBITDA margin | 44.0% | 43.8% | 0.2pp |
| Capex (4) | 198.0 | 188.6 | 5.0% |
| Capex as % of revenues | 12.8% | 12.6% | 0.3pp |
| EBITDA minus Capex | 481.0 | 470.1 | 2.3% |

(1) Includes intragroup transactions.

(2) EBITDA = income from operations + depreciation and amortisation.

(3) Income from operations = income before financials and income taxes + curtailment costs + losses (gains) on disposal of fixed assets + net other costs.

(4) Includes Euro 15 million related to the capitalisation of a long-term telecom contract with PT Comunicações and excludes the commitments under the terms of the UMTS licence (Euro 242 million in 2007).

Mobile termination rates _ Mobile termination rates currently stand at Euro 11 cents per minute, following the reduction on 1 October 2006. A final decision concerning the draft proposal issued by the telecom regulator for the MTR schedule for 2008 is still pending. The draft decision proposed a reduction to Euro 8 cents per minute on 1 January 2008, followed by quarterly cuts of Euro 0.5 cents until reaching Euro 6.5 cents per minute on 1 October 2008. This proposal, reintroduces asymmetry in fixed-to-mobile rates, after having eliminated it in 2005, and introduces asymmetry in mobile-to-mobile rates, a flat 20% premium for the third operator on the prices referred above, subject to a review at the end of 2008.

EBITDA _ EBITDA increased by 3.1% y.o.y to Euro 679 million in 2007, notwithstanding significantly higher commercial activity. In spite of the increase in commercial activity, mainly focused on prepaid to postpaid migration and wireless broadband sales, the decrease in unitary SARC (-14.9% y.o.y) and the focus on the reduction of addressable costs, namely staff, resulted in an EBITDA margin improvement of 0.2pp y.o.y to 44.0% in 2007. The negative impact of MTR cuts amounted to Euro 7 million in 2007. Excluding this impact, EBITDA would have increased by 4.2% y.o.y in 2007.

Capex _ Capex increased from Euro 189 million in 2006 to Euro 198 million in 2007, equivalent to 12.8% of operating revenues. Capex was directed primarily towards network capacity, as a result of increased voice and data usage, and 3G/3.5G coverage (approximately 82% of network capex). EBITDA minus Capex amounted to Euro 481 million in 2007, representing an increase of 2.3% from 2006.

Domestic mobile operating data (1)

| | 2007 | 2006 | y.o.y |
|-----------------------------------|-------|-------|---------|
| Customers (000) | 6,261 | 5,704 | 9.8% |
| Net additions (000) | 558 | 391 | 42.5% |
| MOU (minutes) | 121 | 120 | 0.3% |
| ARPU (Euro) | 19.8 | 21.0 | (5.7)% |
| Customer | 15.8 | 16.6 | (4.5)% |
| Interconnection | 3.5 | 3.8 | (7.5)% |
| Roamers | 0.5 | 0.6 | (24.9)% |
| ARPM (Euro cents) | 16.4 | 17.5 | (6.0)% |
| Data as % of service revenues (%) | 16.0 | 13.3 | 2.8pp |
| SARC (Euro) | 46.9 | 55.1 | (14.9)% |
| Employees | 1,144 | 1,140 | 0.4% |

(1) Includes MVNO subscribers.

Customers _ Total customers increased by 9.8% y.o.y to 6,261 thousand, which includes MVNO subscribers, with net additions in 2007 reaching 558 thousand (+42.5% y.o.y), as a result of the

successful TMN's campaign both for voice and data offers and including the strong take-up of wireless broadband supported by the information society initiatives. In early October, TMN celebrated the 6 million customer mark, thus consolidating its leadership position in the market. TMN continued to focus on postpaid, particularly on the corporate segment, and on prepaid to postpaid migration. As a result, approximately 70% of net additions in the period were postpaid, which accounted for 23.8% of total customers at the end of 2007.

Handset portfolio _ TMN launched several initiatives during the Christmas campaign, using the TMN and the UZO brands, aimed at stimulating usage. In terms of handsets, TMN continued to focus on having a balanced and broad portfolio, with an important component of exclusive handsets, which allows for greater pricing flexibility and thus better control of SARC. Additionally, TMN reinforced its offering of the Blackberry email to corporate, SME and SoHo segments. For the Summer campaign, TMN launched 25 new handsets, of which 8 were exclusive, and for the Christmas campaign, TMN offered 16 new handsets, of which 6 were exclusive.

Broadband _ The rollout of broadband data remained a key priority during the quarter. Demand for the service *internetnotelemovel*, which was the first flat-rate offer for Internet and email access on mobile handsets launched in Portugal, has been picking up, whilst wireless broadband take-up remains strong. The wireless broadband take-up has been underpinned by the *e-escolas* programme, a part of the Government's *Plano Tecnológico* initiative, which aims to provide laptop computers with wireless broadband connectivity, at certain discounts, to schools, teachers, students and info-excluded individuals. This project is being developed as

part of TMN's commitment to the development of the information society, as per the UMTS licence terms. At the end of 2007, TMN had already delivered approximately 70 thousand laptops bundled with broadband subscriptions.

Fixed-mobile convergent offers _ TMN has also been developing fixed-mobile convergent offers with the objective of providing more comprehensive and integrated solutions for its customers. OfficeBox , which targets the SME and SoHo segments, is an off-the-shelf product aimed at covering the full telecommunication needs of small businesses. It includes fixed-line and mobile voice, fixed and mobile Internet access, mobile handset and a PC. Its minimum price is a flat rate of Euro 70 per month per workstation.

ARPU _ ARPU decreased by 5.7% y.o.y in 2007 to Euro 19.8, mainly as a result of the increasing penetration in lower segments of the market and the growing number of users with multiple SIM cards, as well as lower roaming prices. Nevertheless, the growth in the average customer base more than offset the dilution in ARPU, allowing service revenues to grow by 2.2% y.o.y in 2007. Roamers ARPU decreased by 24.9% y.o.y as a result of the adjustments TMN has been making to its roaming pricing plans, following EU-imposed changes to wholesale roaming prices, which came into effect as of 1 September 2007. Blended MOU increased by 0.3% y.o.y in 2007 to 121 minutes, as a result of the growth in outgoing voice MOU.

Data services _ Data services continued to contribute strongly to top line growth, with data revenues having increased by 23.5% y.o.y in 2007 and already accounting for 16.0% of service revenues at the end of the period, which compares favourably with 13.3% in 2006.

The increase in data service revenues is primarily based on non-SMS data revenues, which grew by 84.6% y.o.y and already accounted for 34.4% of total data revenues in 2007. This growth in non-SMS data was driven by a strong performance in terms of mobile Internet and wireless broadband. Data usage, measured in kilobytes, increased by more than five times in 2007 when compared to 2006. The number of SMS in 2007 reached approximately 180 messages per month per active SMS user. The number of active SMS users reached 50% of total customers at the end of the 2007.

International market

Brazilian mobile - Vivo

Operating revenues _ Vivo's operating revenues, as stated in Brazilian Reais and in accordance with IFRS, increased by 14.2% y.o.y in 2007 to R\$ 13,133 million, primarily as a result of the strong growth in service revenues (+17.6% y.o.y), which was underpinned by the growth in customers and in ARPU. This strong performance more than offset the decrease in equipment sales and in other operating revenues.

Brazilian mobile income statement (1)

R\$million

| | 2007 | 2006 | y.o.y |
|--|----------|----------|---------|
| Operating revenues | 13,133.0 | 11,498.0 | 14.2% |
| Services rendered | 11,502.8 | 9,777.5 | 17.6% |
| Sales | 1,376.1 | 1,391.7 | (1.1)% |
| Other operating revenues | 254.1 | 328.9 | (22.7)% |
| Operating costs, excluding D&A | 9,960.2 | 8,787.3 | 13.3% |
| Wages and salaries | 686.8 | 631.0 | 8.8% |
| Direct costs | 2,284.4 | 1,359.6 | 68.0% |
| Commercial costs | 3,535.4 | 3,277.1 | 7.9% |
| Other operating costs | 3,453.5 | 3,519.5 | (1.9)% |
| EBITDA (2) | 3,172.8 | 2,710.8 | 17.0% |
| EBITDA~, excluding exceptional items (3) | 3,107.7 | 2,746.0 | 13.2% |
| Depreciation and amortisation | 2,789.2 | 2,763.4 | 0.9% |
| Income from operations (4) | 383.6 | (52.7) | n.m. |
| EBITDA margin | 24.2% | 23.6% | 0.6pp |
| EBITDA margin, excluding exceptional items | 23.7% | 23.9% | (0.2pp) |
| Capex | 1,919.0 | 2,113.0 | (9.2)% |
| Capex as % of revenues | 14.6% | 18.4% | (3.8pp) |
| EBITDA minus Capex | 1,253.8 | 597.7 | 109.8% |

(1) Information prepared in accordance with IFRS.

(2) EBITDA = income from operations + depreciation and amortisation.

(3) Adjusts for the one-off provision related to bad debt booked in 2Q06 in the amount of R\$ 162 million.

(4) Income from operations = income before financials and income taxes + curtailment costs + losses (gains) on disposal of fixed assets + net other costs.

EBITDA _ EBITDA increased by 17.0% y.o.y to R\$ 3,173 million in 2007. Part of this improvement is explained by an extraordinary provision for bad debts booked in the second quarter of 2006 (R\$ 162 million). Nevertheless, the strong underlying performance in terms of top line resulted in an EBITDA (excluding exceptionals items) increase of 13.2% y.o.y. to R\$ 3,108 million in 2007, notwithstanding the higher commercial activity. As a result of the measures implemented over the past year and a half to control bad debt, Vivo provisions for doubtful receivables in 2007 fell to approximately 4% of gross revenues. Unitary SARC fell by 16.1% y.o.y to R\$ 110 in 2007. As a result, EBITDA margin increased by 0.6pp in 2007 to 24.2%.

Capex _ Capex decreased by 9.2% y.o.y to R\$ 1,919 million in 2007, equivalent to 14.6% of operating revenues. Capex in 2007 was directed towards: (1) the implementation of the GSM/EDGE overlay, and

(2) network coverage and quality. The GSM/EDGE network overlay was implemented in record time and already covers 2,318 municipalities. All of the capex related to the initial GSM/EDGE rollout, as announced in July 2006, has been already invested. EBITDA minus Capex increased from R\$ 598 million in 2006 to R\$ 1,254 million in 2007.

Acquisitions _ On 2 August, Vivo reached an agreement to acquire Telemig Celular and Amazonia Celular. Anatel has already approved the acquisition of Telemig Celular. On 20 December, Vivo reached an agreement with Oi (Telemar Norte Leste) to sell Tele Norte Celular, the controlling company of Amazonia Celular. Additionally, on 25 September, Vivo acquired 1.9 GHz frequencies in all of the regions where it did not operate, in particular in the Northeast states. Vivo has thus achieved full nationwide coverage in Brazil, which has been a long-standing objective of the Company and should consolidate its leadership position in the mobile market. In December, Vivo participated in the bidding process of 3G frequencies and succeeded in achieving a nationwide coverage having offered R\$ 1.1 billion for the band J licenses.

Brazilian mobile operating data (1)

| | 2007 | 2006 | y.o.y |
|-----------------------------------|--------|--------|---------|
| Customers (000) | 33,484 | 29,053 | 15.2% |
| Net additions (000) | 4,430 | (752) | n.m. |
| MOU (minutes) | 77 | 74 | 4.9% |
| ARPU (R\$) | 30.4 | 27.1 | 12.2% |
| Customer | 17.3 | 15.7 | 10.3% |
| Interconnection | 13.1 | 11.5 | 14.7% |
| Data as % of service revenues (%) | 7.9 | 6.8 | 1.1pp |
| SARC (R\$) | 109.7 | 130.7 | (16.1)% |
| Employees | 5,600 | 5,896 | (5.0)% |

(1) Operating data calculated using Brazilian GAAP.

Customers _ Vivo's customer base increased by 15.2% y.o.y to 33,484 thousand, with net additions reaching 4,430 thousand in 2007 on the back of significantly higher commercial activity when compared to 2006. GSM accounted for approximately 65% of total gross additions in 2007, bringing the total number of GSM customers to more than 11.2 million at the end of the year, equivalent to 33.6% of total customers. As part of the continued focus on improving customer satisfaction and usage, Vivo launched a set of postpaid plans, called Vivo Escolha, in the third quarter of 2006. More than one year after introducing the new family of plans, approximately 67% of the postpaid customer base (excluding corporates) has already moved to a Vivo Escolha plan. Vivo's focus on providing the best network quality and the best service offering has been resulting in improved customer satisfaction levels, as evidenced by recent consumer surveys.

MOU _ Vivo's blended MOU increased by 4.9% y.o.y in 2007 to 77 minutes, reflecting the growth in outgoing traffic, as a result of successful campaigns aimed at increasing consumption in the prepaid segment, notwithstanding the strong growth of the subscriber base throughout 2007.

ARPU _ Vivo's blended ARPU reached R\$ 30.4 in 2007, an increase of 12.2% y.o.y, driven by the strong growth in customer and interconnection ARPU, which increased by 10.3% y.o.y and 14.7% y.o.y respectively, on the back of higher penetration of data services.

Data revenues _ Data revenues increased by 35.5% y.o.y in 2007, representing 7.9% (+1.1pp y.o.y) of service revenues. In terms of data services, Vivo has leveraged on being the only

operator using two technologies, positioning CDMA/EVDO as the best solution for mobile data. As a result, Vivo has continued to experience strong growth in its WAP and ZAP (EVDO data cards) offers. Recently it introduced innovative services such as Vivo Play (downloads and video streaming) and Vivo Flash (residential wireless broadband access for desktops).

Other international investments

Highlights of main assets in Africa and Asia (2007) (1) (2)

thousand (customers), million (financials)

| | Stake | Customers | Rev. local | y.o.y | EBITDA local | y.o.y | Margin | Rev. Euro | EBITDA Euro |
|-------------------|--------|-----------|------------|-------|--------------|-------|--------|-----------|-------------|
| Médi Télécom (3) | 32.18% | 6,669 | 4,926 | 5.0% | 2,271 | 9.3% | 46.1% | 438.4 | 202.1 |
| Unitel (3) (5) | 25.00% | 3,307 | 891 | 37.2% | 536 | 23.6% | 60.2% | 648.9 | 390.6 |
| MTC (4) (5) | 34.00% | 800 | 1,140 | 16.4% | 599 | 2.0% | 52.6% | 117.7 | 61.9 |
| CVT (4) (5) | 40.00% | 221 | 7,458 | 6.9% | 4,705 | 6.4% | 63.1% | 67.6 | 42.7 |
| CTM (3) | 28.00% | 533 | 2,289 | 9.0% | 967 | 19.2% | 42.2% | 207.4 | 87.6 |
| CST (4) (5) | 51.00% | 38 | 156,321 | 12.4% | 53,062 | 9.2% | 33.9% | 8.3 | 2.8 |
| Timor Telecom (4) | 41.12% | 81 | 32 | 35.4% | 15 | 58.7% | 46.0% | 23.0 | 10.6 |
| UOL | 29.00% | 1,690 | 525 | 9.2% | 153 | 12.5% | 29.2% | 197.0 | 57.5 |

(1) All information prepared in accordance with local GAAP.

(2) Figures account for 100% of the company. PT has management contracts in Médi Télécom, CVT and Timor Telecom.

(3) Equity consolidation method.

(4) Full consolidation method.

(5) These stakes are held by Africatel, which is controlled 78% by PT.

Morocco - Médi Télécom

Médi Télécom revenues increased by 5.0% y.o.y in 2007 to MAD 4,926 million, while EBITDA increased by 9.3% y.o.y to MAD 2,271 million. The mobile customer base increased by 28.9% y.o.y to 6,665 thousand, with net additions in 2007 totalling 1,496 thousand, driven by the sale of SIM-only packages. At the end of December 2007, Médi Telecom's market share stood at 33.5%, having increased 0.4pp over the end of

September 2007. MOU decreased by 4.6%

y.o.y in 2007 to 49 minutes. ARPU totalled MAD 69.3 in 2007, a decrease of 23.1% over 2006, mainly due to the significant growth of the customer base, the increasing proportion of lower ARPU customers and the increased competition in the market.

Angola - Unitel

Unitel's revenues and EBITDA increased by 37.2% and 23.6% y.o.y respectively in 2007, underpinned by strong customer growth, both in Luanda and in the main districts of the Angola. EBITDA margin reached 60.2% in 2007. Net additions totalled 1,258 thousand in 2007, with the total customer base reaching 3,307 thousand at the end of December 2007, an increase of 61.4% over the same period of last year. Unitel's MOU decreased by 16.1% y.o.y in 2007 to 118 minutes. ARPU totalled USD 27.6 in 2007, a decrease of 19.5% over 2006, as a result of the strong growth in the customer base.

Namibia - MTC

MTC's revenues and EBITDA increased by 16.4% and 2.0% y.o.y respectively in 2007. The EBITDA growth was impacted by the increase in commercial costs, as a result of higher commercial activity particularly in postpaid, higher leased line costs related to network rollout and higher personnel costs. Net additions totalled 191 thousand in 2007, with total customers reaching 800 thousand at the end of December 2007, an increase of 31.3% over the same period of 2006. Postpaid customers increased by 38.5% y.o.y, representing 8.9% of total

customer base. ARPU totalled NAD 134 in 2007, a decrease of 15.2% y.o.y, primarily as a result of the growth in the customer base in 2007.

Cape Verde - CVT

CVT's revenues and EBITDA increased by 6.9% and 6.4% y.o.y respectively in 2007, mainly due to the strong growth in mobile customers, which increased by 35.9% y.o.y to 148 thousand customers. Mobile MOU reached 82 minutes, an increase of 3.4% y.o.y in 2007. Mobile ARPU in 2007 was CVE 2,766, a decrease of 10.0% y.o.y. EBITDA Margin reached 63.1% in 2007.

Macao - CTM

CTM's revenues increased by 9.0% y.o.y to MOP 2,289 million in 2007, as a result of the increase in the number of mobile and broadband customers. EBITDA improved by 19.2% y.o.y to MOP 967 million in 2007. In the mobile division, customers increased by 17.0% y.o.y to 349 thousand at the end of December 2007. CTM's mobile ARPU decreased by 12.4% y.o.y to MOP 219 in 2007, as a result of the growth in the customer base.

São Tomé e Príncipe - CST

CST's revenues increased by 12.4% y.o.y to STD 156,321 million in 2007, with EBITDA growing by 9.2% y.o.y to STD 53,062 million. In the mobile division, CST added 12 thousand customers in 2007, bringing the total number of customers to 30 thousand at the end of

December 2007, an increase of 63.4% y.o.y. Mobile MOU decreased by 23.6% y.o.y in 2007, reaching 62 minutes, as a result of the growth in the customer base. Mobile ARPU was STD 299 thousand in 2007, a decrease of 22.2% over 2006.

East Timor - Timor Telecom

Timor Telecom's revenues and EBITDA increased by 35.4% and 58.7% y.o.y respectively, mainly as a result of the strong increase in the number of mobile customers. Timor Telecom's net additions reached 29 thousand, bringing the total customer base to 78 thousand at the end of December 2007, an increase of 59.3% y.o.y. Mobile MOU decreased by 4.1% y.o.y to 101 minutes. Mobile ARPU was USD 33 in 2007, a decrease of 7.4% over 2006.

Brazil - UOL

UOL's revenues increased by 9.2% y.o.y to R\$ 525 million in 2007, as a result of the growth in the customer base and in advertising revenues. EBITDA increased by 12.5% y.o.y to R\$ 153 million in 2007, corresponding to an EBITDA margin of 29.2%, underpinned by the strong growth in brand advertising and subscription revenues coupled with a strict cost control. UOL's subscriber base totalled 1,690 thousand at the end 2007, including 973 thousand broadband customers, which represented an increase of 23% over 2006. In December 2007, page views and unique visitors increased by 19% and 29% y.o.y respectively.

03 Employees**Number of employees and productivity ratios**

| | 2007 | 2006 | Δ y.o.y | y.o.y |
|-----------------------------|--------|--------|---------|---------|
| Domestic employees | 10,338 | 11,336 | (998) | (8.8)% |
| Wireline | 6,354 | 7,181 | (827) | (11.5)% |
| Domestic mobile • TMN | 1,144 | 1,140 | 4 | 0.4% |
| Other | 2,840 | 3,015 | (175) | (5.8)% |
| International employees | 18,300 | 19,346 | (1,046) | (5.4)% |
| Brazilian mobile • Vivo (1) | 2,800 | 2,948 | (148) | (5.0)% |
| Other | 15,500 | 16,398 | (898) | (5.5)% |
| Total Group employees | 28,638 | 30,682 | (2,044) | (6.7)% |
| Fixed lines per employee | 657 | 613 | 44 | 7.2% |
| Mobile cards per employee | | | | |
| TMN | 5,473 | 5,003 | 470 | 9.4% |
| Vivo | 5,979 | 4,928 | 1,052 | 21.3% |

(1) The number of employees in the Brazilian mobile business corresponds to 50% of the employees of Vivo.

At the end of 2007, the number of staff employed by PT totalled 28,638 employees, of which 36.1% were based in Portugal. In the wireline business, the ratio of fixed lines per employee improved by 7.2% y.o.y in 2007 to 657 lines, reflecting the ongoing workforce rationalisation programme, while in TMN the ratio of mobile cards per employee rose by 9.4% to 5,473 cards. At the end of December 2007, the total number of employees of Vivo decreased by 5.0% y.o.y to 5,600 employees, with the ratio of mobile cards per employee increasing by 21.3% to 5,979 cards.

As part of the cost rationalisation programme, PT continued with its workforce reduction programme, with headcount decreasing by 1,004 employees in 2007, of which 827 were in the wireline business.

04 **Capital markets**

Shareholder remuneration

In terms of shareholder remuneration, PT returned approximately Euro 3.4 billion to shareholders in 2007, through a combination of the following:

- Share buyback of Euro 1,185 million. On 20 December 2007, PT cancelled 103,056,500 of its own shares, equivalent to 9.13% of its share capital, and reduced its share capital from Euro 33,865,695 to Euro 30,774,000. As of 31 December 2007, PT had equity swap contracts on its own shares totalling Euro 135 million.
- The distribution of 180.6 million shares of PT Multimédia to PT shareholders, equivalent to Euro 1.7 billion, assuming the weighted average market price of PT Multimédia on the Euronext Lisbon as at 6 November 2007 (Euro 9.18 per share).
- Remuneration of Euro 517 million corresponding to the payment of the May 2007 dividend equal to 47.5 cents per share for the fiscal year 2006.

Subject to Shareholders' approval at the AGM.

Regarding dividends for the fiscal year 2007 to be paid in 2008, PT's Board of Directors will propose the submission for shareholders' approval at the next AGM, to be held on 28 March 2008, the payment of a cash dividend of 57.5 cents per share, representing an increase of 21.1% over the previous year.

In global terms, considering the shareholder remuneration of 2006, through the payment of dividends in the amount of Euro 526 million, PT had already returned to its shareholders around 66% of the total remuneration package approved for the period 2006-2009, which corresponds to approximately Euro 3.9 billion.

In addition, as at the date of this report, PT had contracted equity swaps to acquire 63,391,786 PT shares, of which 20,640,000 shares were contracted under the previous share buyback programme. As part of the share buyback programme under execution, PT has acquired,

directly or through equity swaps, a total of 145,808,286 own shares, equivalent to 14.21% of PT's share capital (or 12.92% of PT's share capital prior to the share capital reduction executed on 20 December 2007), amounting to Euro 1,434 million.

Shareholder structure

PT has a diversified shareholder base, with approximately 68% of its share capital being held by foreign shareholders, divided mainly among United States and Europe. The Portuguese market has been increasing its weight in PT's share capital, representing now almost a third of the total shareholder base, with Continental Europe and the US market representing approximately 23% and 26%, respectively, of PT's outstanding capital.

At the end of 2007, the holdings of the qualified shareholders represented approximately 57% of PT's share capital, as follows:

Qualified holdings

31 December 2007

| Institutions | No. of shares | % of capital |
|--------------------------------|---------------|--------------|
| Brandes Investments Partners | 98,943,217 | 9.65% |
| Telefónica | 93,915,644 | 9.16% |
| Espirito Santo Group | 91,311,811 | 8.90% |
| Caixa Geral de Depósitos Group | 65,341,768 | 6.37% |
| Ongoing Strategy Investments | 60,404,969 | 5.89% |
| Telmex | 38,460,000 | 3.75% |
| Fidelity | 23,592,185 | 2.30% |
| Barclays Group | 23,216,664 | 2.26% |
| Capital Group Companies | 22,996,339 | 2.24% |
| Credit Suisse | 22,683,484 | 2.21% |
| Visabeira Group | 22,667,473 | 2.21% |
| Controlinveste Comunicações | 22,284,551 | 2.17% |

Share performance

PT shares registered a favourable evolution in 2007, in line with the positive performance of the European telecommunications sector in the period. PT shares closed the year 2007 at Euro 8.93, representing an increase of 8.6% over the previous year (considering a PT share price adjusted by the spin-off of PT Multimédia of Euro 8.22 for the 2006 year-end). The DJ Stoxx Telecom Europe index in 2007 also increased by 14.6% over last year, as well as the PSI-20 index which registered an increase of 16.3% in the same period. Taking into account shareholder remuneration, PT provided a total shareholder return of 11.7% in 2007.

Source: Bloomberg (local currency).

Among the major financial markets, the Bovespa registered the best performance in 2007 (+43.6%), followed by the DAX (+22.3%). The PSI-20 index also saw a positive performance in 2007, registered the second highest increase (+16.3%) among the European financial markets.

Source: Bloomberg (local currency).

Around 1,343 million PT shares were traded in 2007, equivalent to a daily average of 5.3 million shares, with the trading volume accounting for approximately 14% of the total trading volume of Euronext Lisbon. PT's average turnover increased to 119% in 2007, as compared with 107% in last year.

In 2007, PT's ADRs increased by 20.7%, closing the year at US\$ 13.02. An average of approximately 100 thousand PT ADRs were traded daily in 2007 on the New York Stock Exchange. The number of ADRs outstanding at the end of 2007 was 48.7 million, of which 73%

were owned by international qualified shareholders. PT's ADR programme continues to be one of the most active among European telecom operators.

Bond performance

The key credit strength of PT in 2007 was again its ability to generate a strong operating free cash flow, as a result of leading market positions in both fixed and mobile businesses in Portugal and in mobile business in Brazil, as well as the implementation of continued cost cutting programmes. In 2007, PT maintained a strong liquidity position, given its high level of cash, its debt profile and the additional flexibility provided by its stand-by lines.

Rating

After the failure of the tender offer for Portugal Telecom, Standard & Poor's and Moody's confirmed PT's rating as BBB- and Baa2 respectively, both with stable outlook. These ratings reflect the factors mentioned above, as well as the expected increase in indebtedness resulting from the implementation of PT's shareholder remuneration package.

Bonds

In the beginning of 2007, PT's bond performance was mainly determined by the probability of success assigned to the tender offer over PT launched in 2006, as that event would result in the weakening of the Company's credit quality. Thus, after the failure of the tender offer, spreads of PT bonds tightened gradually until the end of May.

In July, the decline in the housing market in the United States, mainly linked to defaults on subprime loans, resulted in credit spreads widening across the market. This, together with its impacts on financial markets, has been the main driver for the performance of PT bonds until the end of 2007.

Source: Bloomberg

On 3 July 2007, PT launched and priced exchangeable bonds in the amount of Euro 750,000,000, due 2014, exchangeable into fully paid ordinary shares of PT. These bonds were issued by Portugal Telecom International Finance BV on 28 August 2007, carrying a coupon of 4.125% , with an exchange price of Euro 13.9859. Effective 30 October 2007, the exchange price was adjusted to Euro 11.60 as a result of the spin-off of PT Multimédia, according to the terms and conditions of the bonds.

Until the end of 2007, the price of the exchangeable bonds followed the change in the price of PT shares, reaching 105.5 at the end of the year.

Investor relations activities

PT has a policy of providing its shareholders and other members of the international financial community with clear, transparent, regular, two-way communications.

During 2007, the Company participated in several investor events, including investor roadshows, analyst and investor presentations, one-on-one meetings and conference calls, as well as investor conferences in Europe and in the US.

In 2007, PT held a total of over 200 meetings with analysts and investors. Additionally, PT held meetings in its offices, as well as conference-calls with investors and analysts on a regular basis.

During 2007, PT held three roadshows in Europe and the US. The two most significant were held in February (after the announcement of the full-year results), as well as the roadshow held between the end of November and the beginning of December.

The domestic and international financial community continued to recognise PT's efforts in terms of investor relations. This was recognised internationally by the two awards PT received at the 2007 IR Magazine Continental Europe Awards:

- Best Investor Relations Officer (Small and Medium Cap)
- Best Investor Relations in Portugal

Domestically, PT received three prizes at the 2007 Investor Relations Awards, promoted by Deloitte, Diário Económico and Semanário Económico, as follows:

- Best CEO in the Investor Relations area
- Annual Report (non-financial sector) - Honourable Mention
- Best Investor Relations Officer - Honourable Mention

05 **Main events**

Events of the year

Shareholder remuneration

27.APR.07 PT's shareholders approved at the Annual General Meeting (AGM) the following proposals related to the shareholder remuneration package:

- The payment of a cash dividend of Euro 0.475 per share for the fiscal year 2006. The dividend was paid on 18 May 2007.
- The free attribution (spin-off) of all the ordinary shares of PT Multimédia held by PT to its shareholders.
- The acquisition of PT's own shares, in connection with the share buyback programme announced.

28.SEP.07 Following the approval of the proposal above mentioned, PT acquired 103,056,500 own shares, corresponding to 9.13% of its share capital, by a total amount of Euro 1.05 billion, through the exercise of the physical settlement of equity swap contracts.

Share capital

27.APR.07 PT's shareholders approved at the AGM a share capital increase to Euro 474,119,730, to be carried out by means of incorporation of legal reserve in the amount of Euro 79,019,955. At the same meeting, the shareholders approved a share capital reduction in the amount of Euro 440,254,035 to Euro 33,865,695, to be carried out through a reduction in the par value of PT shares to 3 cents.

22.MAY.07 PT executed the public deed for the referred share capital increase and reduction operations, with the resulting share capital amounting to Euro 33,865,695, comprised by 1,128,856,500 shares with a par value of 3 cents each.

20.DEC.07 As part of the execution of the share buyback programme, PT registered the reduction of its share capital in the amount of Euro 3,091,695 through the cancellation of 103,056,500 treasury shares. As a result, PT's share capital is now equivalent to Euro 30,774,000, comprised by 1,025,800,000 shares with a par value of 3 cents each.

Spin-off of PT Multimédia

21.SEP.07 PT announced that its Board of Directors approved the execution of the PT Multimédia spin-off by the end of October 2007, which was within the expected timeframe and in accordance with the terms approved by the Annual General Shareholders Meeting of 27 April 2007.

12.OCT.07 PT announced that the execution of the spin-off of its 58.43% holding in PT Multimédia would be completed on 7 November 2007, under the following terms:

- Timetable - ex-right date: 30 October; record date: 1 November and credit date of PT Multimédia shares to PT's shareholders accounts: 7 de November.
- The allotment to each shareholder of the number of PT Multimédia shares resulting from the application of the ratio 0.176067 to the number of PT shares held on 1 November (record date), rounded down, with a cash payment for the corresponding difference.
- For tax and accounting purposes, the spin-off was considered a dividend in kind and therefore each PT shareholder was subject to withholding tax in accordance with applicable legislation.

06.NOV.07 PT announced that the reference price, to determine the cash amounts in connection with the withholding tax and the compensation for fractional shares resulting from the application of the spin-off ratio, corresponding to the weighted average market price of PT Multimédia shares on the Euronext Lisbon on 6 November 2007 was Euro 9.18 per share.

07.NOV.07 PT announced the completion of the spin-off of PT Multimédia, with a total of 154.9 million shares being transferred to the shareholders accounts, representing 50.1% of the

share capital and voting rights in PT Multimédia. As a result of the application of the withholding tax and the fractional shares mechanisms, PT retained an interest of 8.3% of PT Multimédia's share capital, corresponding to 25.7 million shares. Following the sale of these PT Multimédia shares, on 13 November 2007, PT no longer holds PT Multimédia shares in its balance sheet. The buyers of such PT Multimédia shares have agreed to a 6-month lock-up period, as per US legal requirements.

Acquisition of Telemig Participações and Tele Norte Participações

02.AUG.07 Vivo announced the signature of a stock purchase agreement with Telpart Participações to acquire control of Telemig Celular Participações and Tele Norte Celular Participações, corresponding to 22.72% and 19.34% of total share capital respectively, for an aggregate amount of R\$ 1.2 billion. Assuming full acceptance of all mandatory and voluntary offers, Vivo will have acquired a beneficial interest of 58.2% in Telemig Celular and 54.6% in Amazônia Celular, for an aggregate consideration of approximately R\$ 2.9 billion (including the value of the subscription rights of R\$ 87 million to be acquired from Telpart). Anatel has already approved the acquisition of Telemig Celular. With this transaction Vivo reaffirms its leadership in the wireless market.

20.DEC.07 Vivo reached an agreement with Oi (Telemar Norte Leste) to sell Tele Norte Celular, the controlling company of Amazonia Celular.

Debt

05.MAR.07 Moody's confirmed its rating for PT at Baa2, with stable outlook, following the failure of the tender offer. Fitch Ratings also confirmed its rating for PT at BBB, with negative outlook.

16.MAR.07 Standard & Poor's confirmed its rating for PT at BBB-, with stable outlook, following the failure of the tender offer.

03.JUL.07 PT successfully issued a Euro 750 million exchangeable bond with a maturity of 7 years. The coupon was fixed at 4.125% and the exchange price at Euro 13.9859, which was adjusted, on 30 October 2007, to Euro 11.60 following the spin-off of PT's interest in PT Multimédia.

Corporate bodies

02.MAR.07 Approval at the Shareholders' Meeting of the election of the Vice-Chairman of the General Meeting of Shareholders, Daniel Proença de Carvalho, and of the Secretary of the General Meeting of Shareholders, Francisco Leal Barona, following the termination of the term of office of the former holders of these positions, as well as the ratification of the appointment of the Director, Nuno Rocha dos Santos de Almeida, to complete the 2006/2008 term of office in both cases.

22.JUN.07 Approval at the Shareholders' Meeting of the following proposals:

- Amendment to the articles of association of PT in light of the amendments to the Portuguese Companies Code, which, notably, aims at the implementation of the Anglo-Saxon governance model in PT, with the Company's supervision to be carried out by an

Audit Committee composed of members of the Board of Directors and by a statutory auditor.

- Change in the composition of the Board of Directors from 21 to 23 members and election of Rafael Mora Funes and José Xavier de Basto as members of the Board of Directors to complete the 2006-2008 term of office.
- Election of the directors João Mello Franco (Chairman), Thomaz Paes de Vasconcellos and José Xavier de Basto as members of the Audit Committee for the 2006-2008 term of office.
- Election of the company P. Matos Silva, Garcia Jr., P. Caiado & Associados, SROC, represented by Pedro Matos Silva as Statutory Auditor, and of the company Ascensão, Gomes, Cruz & Associado SROC, represented by Mário Gomes as alternate Statutory Auditor, for the 2006-2008 term of office.
- Election of Eduardo Vera-Cruz Pinto as the new Vice-Chairman of the General Meeting of Shareholders, following the resignation of the former Vice-Chairman, to complete the 2006-2008 term of office.
- Election of Álvaro Pinto Correia, João Mello Franco and Francisco Esteves de Carvalho as members of the Compensation Committee in substitution of the resigning members.

21.SET.07 PT's Board of Directors announced the appointment of Zeinal Bava, Deputy CEO of PT, as CEO of PT Portugal and of PT Comunicações, in addition to his role as CEO of TMN, following the resignation of Rodrigo Costa as Vice-President of PT and CEO of the Wireline division. The Chairman and CEO of PT, Henrique Granadeiro, announced that he will propose

to the Board of Directors, following the Annual General Meeting to approve accounts, the appointment of Zeinal Bava as CEO of PT, while remaining as Chairman of the Board.

Competition Authority fine

02.AUG.07 The Portuguese Competition Authority sanctioned PT for alleged abuse of dominant position by refusing to provide access to its ducts and applied a fine of Euro 38 million. Supported by legal opinions, PT has decided not to accrue for this contingency, as it considers that the outcome will be ultimately favourable for PT.

Public tender offer

12.JAN.07 PT published an update to the report of the Board of Directors regarding the public tender offer announced by Sonaecom. On the same date, PT was notified by the Portuguese Securities Commission (CMVM) of its decision to register the offer.

20.FEB.07 PT published an update to the report of the Board of Directors, following the revision of the offer price announced by Sonaecom on 15 February 2007.

27.FEB.07 PT issued a clarification on the shareholder remuneration package included in the update to the Board of Directors report on the revision of the offer price published on 20 February 2007.

01.MAR.07 Following the amendment to the prospectus on the tender offer launched by Sonaecom SGPS and Sonaecom BV, the Board of Directors of PT considered that the offerors' amendments to the prospectus did not change the consideration and terms of the revised offer

that has been announced, only clarified the conditions of the financing of the offer, namely the sale of assets and the allocation of PT's results through dividends to service the debt assumed by the offerors. Therefore, the Board of Directors reiterated the position and the commitments expressed in its report of 20 February 2007.

02.MAR.07 PT's shareholders rejected, by the majority of the votes cast at the general meeting, the proposal related to the removal of the voting limitation in the bylaws of the Company, whose approval was a condition of the tender offer launched by Sonaecom. Thus, and in accordance with the understanding of the CMVM, the tender offer launched by Sonaecom for PT and PT Multimédia shares, and their effects, lapsed.

Subsequent events

Corporate bodies

18.JAN.08 PT announced that Armando António Martins Vara resigned from his office as non-executive member of the company's Board of Directors.

31.JAN.08 PT announced that António Viana-Baptista and Fernando Abril-Martorell resigned from their office as non-executive members of the company's Board of Directors.

12.FEB.08 PT announced the appointment of Francisco Manuel Marques Bandeira, José María Álvarez-Pallete López and Santiago Fernández Valbuena as non-executive members of the Company's Board of Directors, to complete the 2006-2008 term of Office, thus replacing Armando António Martins Vara, António Viana-Baptista and Fernando Abril-Martorell respectively.

Shareholder remuneration

13.FEB.08 PT announced that, as part of the share buyback programme, it has the right to acquire 63,391,786 shares through equity swap agreements, which includes 20,640,000 shares contracted under the previous share buyback programme. As a result, as part of the share buyback programme under execution, PT has acquired a total of 145,808,286 own shares, equivalent to 12.92% of PT's share capital prior to the share capital reduction executed on 20 December 2007, by a total amount of Euro 1,434 million.

06 Outlook

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Portugal Telecom will continue to explore the growth potential of its asset portfolio, both domestically and internationally. In the domestic market, PT aims to explore full telecommunications and multimedia opportunities through fixed-mobile convergent offers and through multimedia integrated propositions. Internationally, PT intends to continue developing its mobile asset in Brazil, taking advantage of the potential growth of the Brazilian market, and to exploit opportunities in growth markets where PT has clear competitive advantages.

PT will continue to operate in a highly competitive and regulated environment that will pose continued risks and threats to its existing businesses, placing the profitability of its assets under pressure.

In order to anticipate these challenges, PT's strategy in the domestic market will be based upon the development of fixed-mobile convergent services for all segments of the market aimed at improving customer loyalty and decreasing retention costs, while using the various brands in an integrated manner. PT's strategy will also be based on the deployment of new services aimed at providing a pay-TV offering with distinctive and customised content tailored to meet the customer needs. A multi-platform strategy will be designed to provide nationwide coverage of these services. PT will continue to contribute to the development of the information society in Portugal and to promoting the info-inclusion of all Portuguese citizens not only in the urban

areas, but also in the more remote and rural regions of Portugal. PT will continue streamlining its businesses by rationalising its cost structure through productivity increases and business process reengineering.

Internationally, PT aims to continue exploring the growth potential of Vivo, its Brazilian mobile asset, leveraging on Brazil's attractive economic growth prospects, favourable demographics and the opportunity for the fixed-mobile migration. PT will also take advantage of the nationwide coverage of Brazil recently achieved, an opportunity that was never available to date, in order to regain market share in key market segments, namely corporate and high-end. The upcoming launch of 3G services and the existing know-how of Vivo in the data segment should contribute to further exploit the mobile broadband and data opportunity. PT also aims to continue increasing its exposure to high-growth markets in Africa by selectively considering value-creating opportunities and taking full advantage of its existing portfolio and partnerships.

In line with its remuneration commitment, PT should continue to provide an attractive shareholder remuneration profile combined with above-average growth prospects, provided by its international portfolio.

07 Statement by the persons responsible

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For the purposes of subparagraph 1, c) of article 245 of the Portuguese Securities Code, the members of the Board of Directors of Portugal Telecom, SGPS, S.A. identified hereunder declare, in the capacity and within their functions as described therein, that, to the best of their knowledge and grounded on the information to which they had access within such Board of Directors and/or Executive Committee, as applicable, while in office:

- The management report, the financial statements, the auditor's opinion and the other financial statements and documents required by law or regulation concerning the financial year ended on 31 December 2007 were prepared in accordance with the applicable set of accounting standards and give a true and fair view of the assets, liabilities, financial position and profit or loss of Portugal Telecom, SGPS, S.A. and the undertakings included in the consolidation taken as a whole;
- The management report concerning such financial year includes a fair review of the development of the business and the performance and position of Portugal Telecom, SGPS, S.A. and the undertakings included in the consolidation taken as a whole, including an accurate description of the principal risks and uncertainties that they face.

Lisbon, 27 February 2008

Henrique Granadeiro, Chairman of the Board of Directors and Chief Executive Officer

Zeinal Bava, Deputy Chief Executive Officer

Luís Pacheco de Melo, Executive Director, Chief Financial Officer

João Pedro Baptista, Executive Director

António Caria, Executive Director

Rui Pedro Soares, Executive Director

Santiago Fernández Valbuena, Non-Executive Director

José María Álvarez-Pallete López, Non-Executive Director

Joaquim Goes, Non-Executive Director

Amílcar de Moraes Pires, Non-Executive Director

Francisco Marques Bandeira, Non-Executive Director

Jorge Tomé, Non-Executive Director

Nuno de Almeida e Vasconcellos, Non-Executive Director

Rafael Mora Funes, Non-Executive Director

João de Mello Franco, Non-Executive Director

Thomaz Paes de Vasconcellos, Non-Executive Director

José Xavier de Basto, Non-Executive Director

Franquelim Alves, Non-Executive Director

Gerald McGowan, Non-Executive Director

Francisco Pereira Soares, Non-Executive Director

Fernando Soares Carneiro, Non-Executive Director

Luís de Azevedo Coutinho, Non-Executive Director

Consolidated financial statements

PORTUGAL TELECOM, SGPS, SA

CONSOLIDATED INCOME STATEMENT

FOR THE YEARS ENDED 31 DECEMBER 2007 AND 2006

(Amounts stated in Euro)

| | Notes | 2007 | 2006 |
|---|-----------|----------------------|----------------------|
| <u>CONTINUING OPERATIONS</u> | | | |
| REVENUES | | | |
| Services rendered | 6 | 5,625,495,438 | 5,245,888,869 |
| Sales | 6 | 442,466,483 | 426,230,971 |
| Other revenues | 6 | 80,447,271 | 93,167,779 |
| | | 6,148,409,192 | 5,765,287,619 |
| COSTS, EXPENSES, LOSSES AND (INCOME) | | | |
| Wages and salaries | 8 | 638,072,873 | 633,477,183 |
| Post retirement benefits | 9.5 | (65,076,144) | (72,114,978) |
| Direct costs | 10 | 907,297,176 | 724,870,453 |
| Costs of products sold | 11 | 656,149,583 | 580,619,498 |
| Support services | | 233,571,798 | 202,072,507 |
| Marketing and publicity | | 147,246,817 | 138,301,415 |
| Supplies and external services | 12 | 945,616,627 | 928,511,310 |
| Indirect taxes | 14 | 201,825,104 | 175,910,937 |
| Provisions and adjustments | 39 | 127,033,719 | 216,636,355 |
| Depreciation and amortisation | 33 and 34 | 1,123,064,739 | 1,130,713,808 |
| Curtailement costs, net | 9.5 | 275,619,171 | 18,962,004 |
| Gains on disposals of fixed assets, net | | (2,795,990) | (5,149,008) |
| Other costs, net | 15 | 45,071,936 | 115,399,995 |
| | | 5,232,697,409 | 4,788,211,479 |
| Income before financial results and taxes | | 915,711,783 | 977,076,140 |
| Net interest expense | 16 | 197,368,292 | 220,073,341 |
| Net foreign currency exchange losses (gains) | | 12,427,018 | (4,467,691) |
| Net gains on financial assets and other investments | 17 | (248,783,007) | (18,333,763) |
| Equity in earnings of associated companies, net | 31 | (126,127,657) | (130,605,856) |
| Net other financial expenses | 18 | 48,316,434 | 51,778,746 |
| | | (116,798,920) | 118,444,777 |
| Income before taxes | | 1,032,510,703 | 858,631,363 |
| Income taxes | 19 | 243,277,665 | (21,364,371) |
| Net income from continuing operations | | 789,233,038 | 879,995,734 |
| <u>DISCONTINUED OPERATIONS</u> | | | |

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| | | | |
|---|-----------|--------------------|--------------------|
| Net income from discontinued operations | 20 | 45,474,124 | 74,132,079 |
| NET INCOME | | 834,707,162 | 954,127,813 |
| Attributable to minority interests | 21 | 92,847,426 | 87,368,156 |
| Attributable to equity holders of the parent | 23 | 741,859,736 | 866,759,657 |
| Earnings per share from total operations | | | |
| Basic | 23 | 0.71 | 0.78 |
| Diluted | 23 | 0.67 | 0.73 |
| Earnings per share from continued operations | | | |
| Basic | 23 | 0.69 | 0.74 |
| Diluted | 23 | 0.66 | 0.69 |

The accompanying notes form an integral part of these financial statements.

PORTUGAL TELECOM, SGPS, SA

CONSOLIDATED BALANCE SHEET

31 DECEMBER 2007 AND 2006

(Amounts stated in Euro)

| | Notes | 2007 | 2006 |
|----------------------------------|-------|-----------------------|-----------------------|
| ASSETS | | | |
| Current Assets | | | |
| Cash and cash equivalents | | 664,642,854 | 548,464,617 |
| Short-term investments | 24 | 1,170,293,202 | 1,535,233,729 |
| Accounts receivable - trade | 25 | 1,307,429,771 | 1,181,912,412 |
| Accounts receivable - other | 26 | 128,745,389 | 218,912,177 |
| Inventories | 27 | 160,592,407 | 130,280,564 |
| Taxes receivable | 28 | 239,111,584 | 211,747,572 |
| Prepaid expenses | 29 | 106,526,815 | 121,714,749 |
| Other current assets | 30 | 38,979,994 | 50,405,004 |
| Total current assets | | 3,816,322,016 | 3,998,670,824 |
| Non-Current Assets | | | |
| Accounts receivable - trade | | 1,289,741 | 916,813 |
| Accounts receivable - other | 26 | 4,352,233 | 15,237,939 |
| Taxes receivable | 28 | 148,340,234 | 124,531,128 |
| Prepaid expenses | | 6,822,888 | 2,628,424 |
| Investments in group companies | 31 | 538,080,641 | 499,098,279 |
| Other investments | 32 | 27,235,420 | 132,391,079 |
| Intangible assets | 33 | 3,383,123,427 | 3,490,881,263 |
| Tangible assets | 34 | 3,585,397,171 | 3,942,033,190 |
| Post retirement benefits | 9.3 | 134,060,599 | 134,060,519 |
| Deferred taxes | 19 | 992,880,357 | 1,167,007,154 |
| Other non-current assets | 30 | 484,266,159 | 663,792,688 |
| Total non-current assets | | 9,305,848,870 | 10,172,578,476 |
| Total assets | | 13,122,170,886 | 14,171,249,300 |
| LIABILITIES | | | |
| Current Liabilities | | | |
| Short-term debt | 35 | 1,256,085,485 | 1,372,724,030 |
| Accounts payable | 36 | 1,108,882,163 | 1,115,089,223 |
| Accrued expenses | 37 | 641,050,928 | 680,217,532 |
| Deferred income | 38 | 286,056,467 | 215,738,311 |
| Taxes payable | 28 | 381,956,714 | 316,962,828 |
| Provisions | 39 | 123,340,200 | 105,151,491 |
| Other current liabilities | 40 | 67,308,947 | 82,495,889 |
| Total current liabilities | | 3,864,680,904 | 3,888,379,304 |
| Non-Current Liabilities | | | |
| Medium and long-term debt | 35 | 4,960,675,814 | 4,467,537,132 |
| Taxes payable | 28 | 31,172,618 | 25,787,484 |
| Deferred income | | 1,413,069 | 380,097 |
| Provisions | 39 | 111,833,374 | 102,633,567 |
| Post retirement benefits | 9.3 | 1,463,932,239 | 1,807,570,587 |

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| | | | |
|--|----|-----------------------|-----------------------|
| Deferred taxes | 19 | 84,880,140 | 90,377,817 |
| Other non-current liabilities | 40 | 521,772,540 | 682,545,374 |
| Total non-current liabilities | | 7,175,679,794 | 7,176,832,058 |
| Total liabilities | | 11,040,360,698 | 11,065,211,362 |
| SHAREHOLDERS EQUITY | | | |
| Share capital | 41 | 30,774,000 | 395,099,775 |
| Capital issued premium | 41 | | |
| Treasury shares | 41 | (323,178,913) | (187,612,393) |
| Legal reserve | 41 | 6,773,139 | 82,706,881 |
| Reserve for treasury shares | 41 | 3,091,695 | |
| Accumulated earnings | 41 | 1,620,761,976 | 1,965,055,467 |
| Equity excluding minority interests | | 1,338,221,897 | 2,255,249,730 |
| Minority interests | 21 | 743,588,291 | 850,788,208 |
| Total equity | | 2,081,810,188 | 3,106,037,938 |
| Total liabilities and shareholders equity | | 13,122,170,886 | 14,171,249,300 |

The accompanying notes form an integral part of these financial statements.

PORTUGAL TELECOM, SGPS, SA

CONSOLIDATED STATEMENT OF RECOGNISED INCOME AND EXPENSES

FOR THE YEARS ENDED 31 DECEMBER 2007 AND 2006

(Amounts stated in Euro)

| | Notes | 2007 | 2006 |
|--|-------|----------------------|----------------------|
| Income and expenses recognised directly in shareholders' equity | | | |
| Post retirement benefits | | | |
| Net actuarial gains | 9.6 | 285,237,065 | 319,415,213 |
| Tax effect | 19 | (75,588,720) | (100,691,917) |
| Financial instruments and investments | | | |
| Hedge accounting | | | |
| Change in fair value | | 3,685,028 | 32,537,381 |
| Transferred to profit and loss | 42 | (8,287,000) | (6,938,643) |
| Investments available for sale: | | | |
| Changes in fair value | 32 | 15,682,412 | 19,831,643 |
| Transferred to profit and loss on sale | 17 | (38,650,508) | |
| Tax effect | 19 | 7,306,068 | (12,223,825) |
| Foreign currency translation adjustments (i) | | 204,087,132 | (76,506,877) |
| Other expenses recognised directly in shareholders' equity, net (ii) | | (1,830,620) | (3,353,908) |
| | | 391,640,857 | 172,069,067 |
| Income recognised in the consolidated income statement | | 834,707,162 | 954,127,813 |
| Total income recognised | | 1,226,348,019 | 1,126,196,880 |
| Attributable to minority interests | | | |
| | | 92,847,426 | 87,368,156 |
| Attributable to equity holders of the parent | | 1,133,500,593 | 1,038,828,724 |

(i) Gains recorded in 2007 are mainly related to the appreciation of the Real against the Euro from 2.8118 as at 31 December 2006 to 2.5963 as at 31 December 2007, while losses recorded in 2006 are primarily related to the devaluation of the Real against the Euro from 2.744 as at 31 December 2005 to 2.8118 as at 31 December 2006.

(ii) In 2007 and 2006, current income taxes recognised directly in shareholders' equity amounted to Euro 4,437,430 and Euro 2,667,726, respectively (Note 28), and are related to the tax effect on the gains obtained on the equity swaps over Portugal Telecom's own shares.

The accompanying notes form an integral part of these financial statements.

PORTUGAL TELECOM, SGPS, SA

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE YEARS ENDED 31 DECEMBER 2007 AND 2006

(Amounts stated in Euro)

| | Notes | 2007 | 2006 |
|--|-------|------------------|------------------|
| OPERATING ACTIVITIES | | | |
| Collections from clients | | 7,070,397,265 | 6,763,769,410 |
| Payments to suppliers | | (3,653,519,418) | (3,277,388,237) |
| Payments to employees | | (654,757,374) | (653,682,324) |
| Payments relating to income taxes | 44.a | (206,528,920) | (51,626,295) |
| Payments relating to post retirement benefits | 9.4 | (284,159,570) | (580,789,898) |
| Payments relating to indirect taxes and other | 44.b | (610,407,039) | (572,755,719) |
| Cash flow from operating activities from continued operations | | 1,661,024,944 | 1,627,526,937 |
| Cash flow from operating activities from discontinued operations | 20 | 198,182,708 | 194,134,513 |
| Cash flow from operating activities (1) | | 1,859,207,652 | 1,821,661,450 |
| INVESTING ACTIVITIES | | | |
| Cash receipts resulting from | | | |
| Short-term financial applications | 44.c | 25,017,800,206 | 20,265,198,328 |
| Financial investments | 44.d | 239,646,906 | 2,435,335 |
| Tangible and intangible assets | | 15,424,276 | 12,456,930 |
| Interest and related income | | 246,999,708 | 237,362,095 |
| Dividends | 44.e | 94,799,920 | 34,267,817 |
| Other investing activities | 44.f | 130,710,004 | 54,285,892 |
| | | 25,745,381,020 | 20,606,006,397 |
| Payments resulting from | | | |
| Short-term financial applications | 44.c | (24,652,859,679) | (18,501,169,649) |
| Financial investments | 44.g | (3,342,537) | (93,174,205) |
| Tangible fixed assets | | (756,401,882) | (723,195,587) |
| Other investing activities | | (17,214,795) | (29,382,265) |
| | | (25,429,818,893) | (19,346,921,706) |
| Cash flow from investing activities related to continued operations | | 315,562,127 | 1,259,084,691 |
| Cash flow from investing activities related to discontinued operations | 20 | (79,620,931) | (122,394,941) |
| Cash flow from investing activities (2) | | 235,941,196 | 1,136,689,750 |
| FINANCING ACTIVITIES | | | |
| Cash receipts resulting from | | | |
| Loans obtained | 44.h | 9,032,800,130 | 16,282,847,588 |
| Subsidies | | 1,781,572 | 1,823,692 |
| Other financing activities | | 220,786 | 39,292 |
| | | 9,034,802,488 | 16,284,710,572 |
| Payments resulting from | | | |
| Loans repaid | 44.h | (8,809,340,609) | (18,016,333,731) |
| Lease rentals (principal) | | (17,089,599) | (12,790,988) |
| Interest and related expenses | | (491,753,664) | (552,211,935) |
| Dividends | 44.i | (552,726,968) | (552,208,352) |
| Acquisition of treasury shares | 41.3 | (1,050,271,924) | |
| Other financing activities | 44.j | (46,962,926) | (81,046,857) |

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| | | | |
|---|----|------------------|------------------|
| | | (10,968,145,690) | (19,214,591,863) |
| Cash flow from financing activities related to continued operations | | (1,933,343,202) | (2,929,881,291) |
| Cash flow from financing activities related to discontinued operations | 20 | (20,267,540) | (85,489,101) |
| Cash flow from financing activities (3) | | (1,953,610,742) | (3,015,370,392) |
| Cash and cash equivalents at the beginning of the period | | 548,464,617 | 612,158,485 |
| Change in cash and cash equivalents (4)=(1)+(2)+(3) | | 141,538,106 | (57,019,192) |
| Effect of exchange differences | | 23,442,726 | (6,674,676) |
| Cash and cash equivalents of PT Multimédia as of the date of the spin-off | | (48,802,595) | |
| Cash and cash equivalents at the end of the period | | 664,642,854 | 548,464,617 |

The accompanying notes form an integral part of these financial statements.

Portugal Telecom, SGPS, SA

Notes to the Consolidated Financial Statements

As at 31 December 2007

(Amounts stated in Euros, except where otherwise stated)

1. Introduction

a) Parent company

Portugal Telecom, SGPS, SA (formerly Portugal Telecom, SA, Portugal Telecom) and subsidiaries (Group , Portugal Telecom Group , or the Company), are engaged in rendering a comprehensive range of telecommunications and multimedia services in Portugal and other countries, including Brazil.

Portugal Telecom was incorporated on 23 June 1994, under Decree-Law 122/94, as a result of the merger, effective 1 January 1994, of Telecom Portugal, SA (Telecom Portugal), Telefones de Lisboa e Porto (TLP), SA (TLP) and Teledifusora de Portugal, SA (TDP). On 12 December 2000, Portugal Telecom, SA changed its name to Portugal Telecom, SGPS, SA, and became the holding company of the Group.

As a result of the privatization process, between 1 June 1995 and 4 December 2000, Portugal Telecom's share capital is mainly owned by private shareholders. As at 31 December 2007, the Portuguese State owned, directly or indirectly, 8.44% of the total ordinary shares and all of the A Shares of Portugal Telecom (Note 41.1).

The shares of Portugal Telecom are traded on the Euronext Lisbon Stock Exchange and on the New York Stock Exchange.

b) Corporate purpose

Continued operations

Portugal Telecom Group is engaged in rendering a comprehensive range of telecommunications services in Portugal and abroad, including Brazil.

In Portugal, fixed line services are rendered by PT Comunicações, SA (PT Comunicações), under the provisions of the Concession Agreement entered into with the Portuguese State on 20 March 1995 in accordance with Decree-Law 40/95, for an initial period of thirty years, subject to renewal for subsequent periods of fifteen years. On 11 December 2002, according to the terms of the Modifying Agreement to the Concession Contract, PT Comunicações acquired the property of the Basic Network of Telecommunications and Telex (Basic Network).

Data transmission services are rendered through PT Prime - Soluções Empresariais de Telecomunicações e Sistemas, SA (PT Prime), which is also an Internet Service Provider (ISP) for large clients.

ISP services for residential clients and small and medium companies are rendered through PT.com Comunicações Interactivas, SA (PT.com), which also provides services relating to the conception, design and exhibit of publicity and information space on Internet portals.

Mobile services in Portugal are rendered by TMN - Telecomunicações Móveis Nacionais, SA (TMN), under a GSM license granted by the Portuguese State in 1992 (period of 15 years), renewed in 2007 until 16 March 2022, and a UMTS license obtained in 19 December 2000 (period of 15 years).

In Brazil, the Group renders mobile telecommunications services through Brasilcel NV (Brasilcel or Vivo), a joint venture incorporated in 2002 by Portugal Telecom (through PT Móveis, SGPS, SA PT Móveis) and Telefónica (through Telefónica Móviles, SA) to join the mobile operations of each group. Currently, Brasilcel, through its company Vivo, SA, provides mobile services in the Brazilian states of São Paulo, Paraná, Santa Catarina, Rio de Janeiro, Espírito Santo, Bahia, Sergipe, Rio Grande do Sul, and eleven states in the Midwestern and Northern regions of Brazil. On 3 August 2007, Vivo Participações, SA (a holding company listed on São Paulo stock exchange that is held by Brasilcel and controls Vivo, SA) signed a stock purchase agreement with Telpart Participações S.A. (Telpart) to acquire control of Telemig Celular Participações S.A. (Telemig Celular) and Tele Norte Celular Participações S.A. (Tele Norte Celular), providers of mobile telecommunication services in the Brazilian State of

Minas Gerais and in the Amazon region Under this purchase agreement, Vivo Participações, S.A. will acquire 22.72% and 19.34% of total capital of Telemig Celular and Tele Norte Celular, respectively, for an aggregate amount of R\$ 1.2 billion, subject to certain price adjustments. In addition, Vivo Participações, SA will acquire from Telpart certain subscription rights for an aggregate amount of R\$ 87 million. The conclusion of the transaction is subject to ANATEL (the Brazilian telecom regulator) approval and relating to Telpart's share capital to ratification by general shareholders' meetings of Vivo and Telpart, among other customary closing conditions, which were not in place as at 31 December 2007.

Discontinued operations (Note 20)

PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, SA (PT Multimedia - recently renamed ZON Multimédia, Serviços de Telecomunicações e Multimédia, SGPS, SA) was the Group's subsidiary for multimedia operations. Through its subsidiary TV Cabo Portugal, SA, PT Multimedia renders cable and satellite television services and voice and internet access services in mainland Portugal, Madeira and Azores. PT Multimedia also renders other multimedia services in Portugal, namely the editing and selling of DVD and movies through Lusomundo Audiovisuais, SA and the distribution and exhibition of movies through Lusomundo Cinemas, SA. At the last Annual General Meeting of Portugal Telecom held on 27 April 2007, it was approved the free allotment (spin-off) of all ordinary shares of PT Multimedia held by Portugal Telecom to its shareholders.

On 7 November 2007 Portugal Telecom concluded the distribution to its shareholders of its interest in PT Multimédia.

The net income of this business in 2006 and in 2007 until the conclusion of the spin-off was presented in the consolidated income statement under the caption Net income from discontinued operations (Note 20).

The consolidated financial statements for the year ended 31 December 2007 were approved by the Board of Directors and authorized for issue on 27 February 2008.

2. Basis of presentation

Consolidated financial statements are presented in Euros, which is the currency of the majority of the Portugal Telecom's operations. Financial statements of foreign subsidiaries are translated to Euros according to the accounting principles described in Note 3.q).

The consolidated financial statements of Portugal Telecom have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU), and include all interpretations of the International Financial Reporting Interpretation Committee (IFRIC) as at 31 December 2007. For Portugal Telecom, no differences have been identified between IFRS as adopted by the EU and applied by Portugal Telecom, and IFRS as published by the International Accounting Standards Board.

Consolidated financial statements have been prepared assuming the continuity of operations, based on the accounting records of all subsidiaries (Exhibit I).

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses during the reported periods (Note 3).

a) Consolidation principles

Controlled entities

Portugal Telecom has fully consolidated the financial statements of all controlled entities. Control is achieved where the Group has the majority of the voting rights or has the power to govern the financial and operating policies of an entity. In any case, where the Group does not have the majority of the voting rights but in substance controls the entity, the financial statements of the entity are fully consolidated (See Exhibit I).

The interest of any third party in the equity and net income of fully consolidated companies is presented separately in the consolidated balance sheet and consolidated income statement, under the caption "Minority interests" (Note 21).

Losses applicable to the minorities in excess of the minority's interest in the subsidiary's equity are allocated against the interest of the Group, except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses. Any future gains reported by the subsidiary are allocated against the interest of the Group, until the excess losses recognised by the Group are covered.

Assets, liabilities and contingent liabilities of an acquired subsidiary are measured at fair value at acquisition date. Any excess amount to the identifiable net assets is recognised as goodwill. If the acquisition cost is lower than the fair value of identifiable net assets acquired, the difference is recognised as a gain in the net income for the period the acquisition occurs. Minority interests are presented proportionally to the fair value of identifiable net assets.

The results of subsidiaries acquired or disposed during the period are included in the consolidated income statement from the effective date of the acquisition or up to the effective date of disposal, as appropriate.

All intra-group transactions, balances, income and expenses are eliminated in the consolidation process. Gains obtained in intra-group transactions are also eliminated in the consolidation process.

Where necessary, adjustments are made to the financial statements of subsidiaries to adjust their accounting policies in line with those adopted by the Group.

Interests in joint ventures

Portugal Telecom has proportionally consolidated the financial statements of jointly controlled entities beginning on the date the joint control is effective. Under this method, assets, liabilities, income and expenses of the entity are added, on a proportional basis, to the corresponding consolidated caption. Financial investments are classified as jointly controlled entities if the joint control agreement clearly demonstrates the existence of joint control.

All transactions and balances with jointly controlled entities are eliminated to the extent of the Group's interest in the joint venture.

Jointly controlled entities are presented in Exhibit III.

Investments in associates

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policies of the entity but not to control or jointly control those policies.

Financial investments in associated companies are accounted for under the equity method (Exhibit II). Under this method, investments in associated companies are carried in the consolidated balance sheet at cost, adjusted periodically for the Group's share in the results of the associated company, recorded as part of financial results under the caption "Equity in earnings of associated companies, net" (Note 31). In addition, these financial investments are adjusted for any impairment losses that may occur.

Losses in associated companies in excess of the cost of acquisition are not recognised, except where the Group has assumed any commitment to cover those losses.

Any excess of the cost of acquisition over the Group's share of the fair value of net assets acquired and contingent liabilities of the associate recognised at the date of acquisition is recorded as goodwill. The goodwill is included within the carrying amount of the investment and is assessed annually for impairment as part of the investment. If the acquisition cost is lower than the fair value of identifiable net assets, the difference is recorded as a gain in the net income for the period the acquisition occurs.

Dividends received from associated companies are recorded as a reduction in the value of financial investments.

Profits and losses occurring in transactions with associated companies are eliminated to the extent of the Group's interest in the associate, and recorded against the corresponding financial investment.

Non-current assets held for sale and disposal groups

Non-current assets and disposal groups are classified as held for sale or as discontinued operation when the asset or the group of assets will be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets will be transferred in the transaction. This condition is regarded as met, only when: (i) the subject transaction is highly probable, and the asset or group of assets is available for immediate sale or to be transferred in its present condition; (ii) the Group has assumed a commitment to the subject of transaction; and (iii) the transaction is expected to be completed within one year. Non-current assets classified as held for sale are measured at the lower of the assets' previous carrying amount or the fair value less costs to sell.

Goodwill

Goodwill represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary, jointly controlled or associated entity recognised at the date of acquisition, in accordance with IFRS 3. Considering the exception of IFRS 1, the Group used the provisions of IFRS 3 only for acquisitions that occurred after 1 January 2004. Goodwill related to acquisitions made up to 1 January 2004 was recorded at the carrying amount of those acquisitions as of that date, and is subject to annual impairment tests thereafter.

Goodwill related to foreign investments is carried at the reporting currency of the investment, being translated to Euros at the exchange rate prevailing at the balance sheet date. Exchange gains or losses are recognised in the Statement of Recognised Income and Expenses under the caption Cumulative foreign currency translation adjustments .

Goodwill related to associated companies is recognised under the caption Investments in group companies (Note 31), and goodwill related to subsidiaries and jointly controlled entities is recognized under the caption Intangible assets (Note 33). Goodwill is not amortised, but tested, on an annual basis, for impairment losses, which are recognised in net income in the period they occur, and cannot be reversed in a subsequent period.

On disposal of a subsidiary, jointly controlled entity or associate, the goodwill allocated to that investment is included in the determination of the gain or loss on disposal.

b) Changes in the consolidated Group

During 2007, there were no significant changes in the consolidated Group except for the spin-off of PT Multimedia mentioned above.

During 2006 the main change in the consolidated Group was the inclusion of Mobile Telecommunications Limited (MTC), following the acquisition of a 34% stake in the share capital of this company in September 2006. In connection with this transaction, Portugal Telecom entered into an agreement with the remaining shareholders of

MTC, under which Portugal Telecom has the power to set and control financial and operating policies of this company. Accordingly, Portugal Telecom consolidated MTC's assets, liabilities and results as from the date the control has been transferred (September 2006). Portugal Telecom's consolidated financial statements include MTC's assets and liabilities as at 31 December 2007 and 2006 and its results for the year ended 31 December 2007 and for the four months period from 1 September 2006 to 31 December 2006. The assets and liabilities from MTC as at 1 September 2006, when it was included for the first time in the consolidation, are as follows:

| | Fair value of net assets acquired | Fair value of intangible assets identified (i) | Total |
|--|-----------------------------------|--|--------------------|
| ASSETS | | | |
| Current assets | 66,062,847 | | 66,062,847 |
| Intangible assets | 7,037,337 | 7,085,832 | 14,123,169 |
| Tangible assets | 47,680,742 | | 47,680,742 |
| Other non-current assets | 605,639 | | 605,639 |
| Total assets | 121,386,565 | 7,085,832 | 128,472,397 |
| LIABILITIES | | | |
| Current liabilities | 11,240,416 | | 11,240,416 |
| Other non-current liabilities | 14,795,400 | 2,480,041 | 17,275,441 |
| Total liabilities | 26,035,816 | 2,480,041 | 28,515,857 |
| Total net assets acquired | | | 99,956,540 |
| PT's share of net assets acquired | | | 33,985,224 |

34%

(i) In the purchase price allocation, Portugal Telecom has identified intangible assets not included in MTC's financial statements, related to the license that allows MTC to operate in the Namibian telecommunications market. The related tax effect amounted to Euro 2,480,041.

Portugal Telecom has made the following purchase price allocation related to the acquisition of MTC:

| | |
|-----------------------------------|--------------------|
| Shareholders' agreement (i) | 34,163,176 |
| PT's share of net assets acquired | 33,985,224 |
| Goodwill | 40,499,689 |
| Purchase price | 108,648,089 |

(i) This caption relates to the agreement entered into with the other shareholders of MTC, which allows Portugal Telecom to set and control financial and operating policies of this company. The fair value of this agreement was determined based on the comparison between the purchase price of Portugal Telecom's acquisition of a 34% stake in MTC's share capital and the payable price of a previous transaction with former shareholders of MTC, since the main difference between those transactions is related to the power to control this company.

3. Summary of significant accounting policies, judgments and estimates

a) Current classification

Assets to be realized and liabilities to be settled within one year from the date of the balance sheet are classified as current.

b) Inventories

Inventories are stated at average acquisition cost. An adjustment to the carrying value of inventories is recognised when the net realizable value is lower than the average cost, recorded in net income of the period the loss occurs under the caption "Cost of products sold". Usually these losses are related to technological obsolescence and lower rotation.

c) Tangible assets

Tangible assets are stated at acquisition cost, net of accumulated depreciation, investment subsidies and accumulated impairment losses, if any. Acquisition cost includes: (1) the amount paid to acquire the asset; (2) direct expenses related to the acquisition process; and (3) the estimated cost of dismantling or removal of the assets (Notes 3.g and 39). Under the exception of IFRS 1, revaluation of tangible assets made in accordance with Portuguese legislation applying monetary indices, prior to 1 January 2004, was not adjusted and was included as the deemed cost of the asset for IFRS purposes.

Tangible assets are depreciated on a straight-line basis from the month they are available for use, during its expected useful life. The amount of the asset to be depreciated is reduced by any residual estimated value. The depreciation rates correspond to the following estimated average economic useful lives:

| | Years |
|-------------------------------------|--------------|
| Buildings and other constructions | 3 - 50 |
| Basic equipment: | |
| Network installations and equipment | 4 - 40 |
| Switching equipment | 5 - 10 |
| Telephones, switchboards and other | 5 - 10 |
| Submarine cables | 15 - 20 |
| Satellite stations | 15 |
| Other telecommunications equipment | 3 - 10 |
| Other basic equipment | 4 - 20 |
| Transportation equipment | 4 - 8 |
| Tools and dies | 4 - 10 |
| Administrative equipment | 3 - 10 |
| Other tangible fixed assets | 3 - 10 |

Estimated losses resulting from the replacement of equipments before the end of their economic useful lives are recognised as a deduction to the corresponding asset's carrying value, against results of the period, as well as any impairment of these assets. The cost of recurring maintenance and repairs is charged to net income as incurred. Costs associated with significant renewals and betterments are capitalized if any future economic benefits are expected and those benefits can be reliably measured.

From the moment certain tangible assets meet the criteria for being classified as held for sale, no additional amortization is recognized and those assets are classified as current assets available for sale. The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the assets and is recognised in the income statement under the caption Gains on disposals of fixed assets, net when occurred.

d) Intangible assets

Intangible assets are stated at acquisition cost, net of accumulated amortisation and accumulated impairment losses, if any. Intangible assets are recognised only if any future economic benefits are expected and those benefits as well as the cost of the asset can be reliably measured.

Intangible assets include mainly goodwill (Note 2.a), telecommunications licenses and related rights and software licenses.

Internally-generated intangible assets, namely research and development expenditures, are recognised in net income when incurred. Development expenditures can only be recognised initially as an intangible asset if the Company demonstrates the ability to complete the project and put the asset in use or make it available for sale.

Intangible assets, except goodwill, are amortised on a straight-line basis from the month they are available for use, during the following periods:

| Telecommunications licenses: | |
|---|---------------------------------------|
| • Band A and Band B licenses held by Vivo | Period of the license |
| • Property of the Basic Network held by PT Comunicações | Period of the concession (until 2025) |
| • UMTS license owned by TMN | Period of the license (until 2015) |
| Satellite capacity acquisition rights | Period of the contracts (until 2015) |
| Software licenses | 3 - 6 |
| Other intangible assets | 3 - 8 |

Following the business combination of MTC undertaken at the end of 2006 (Note 2.b), Portugal Telecom has identified an intangible asset related to the agreement entered into with the other shareholders of MTC, which allows Portugal Telecom to control this company. This agreement does not have a definite useful life and therefore this intangible asset is not amortized but is subject to annual impairment tests. The main factors considered to determine that this intangible does not have a definite useful life were as follows:

- (a) The expected use of the asset by the entity is directly related to the shareholders' agreements duration, which is indefinite;

(b) The shareholders' agreement relates only to the life of the operations of MTC, which is also considered indefinite, as provided for in MTC's by-laws. There is no relation between the expected useful life of another group of assets and the useful life of the intangible asset; and

(c) There were no legal, regulatory, or contractual provisions stipulated in the agreement that would limit its useful life.

e) Investment property

Investment property includes primarily buildings and land held to earn rentals and/or capital appreciation, and not for use in the normal course of the business (exploration, service render or sale).

Investment property is stated at its acquisition cost plus transaction costs and reduced by accumulated depreciation and accumulated impairment losses, if any. Expenditures incurred (maintenance, repairs, insurance and real estate taxes) and any income obtained are recognised in income statement of the period.

f) Impairment of tangible and intangible assets, excluding goodwill

The Group performs impairment tests for its tangible and intangible assets if any event or change results in an indication of impairment. In case of any such indication, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss.

Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. The primary cash-generating units identified in the Group correspond to the wireline and mobile businesses in Portugal and mobile in Brazil. The recoverable amount is the higher of fair value less cost to sell and the value in use. In assessing fair value less cost to sell, the amount that could be received from an independent entity is considered, reduced by direct costs related with the sale. In assessing the value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the specific risk to the asset.

If the recoverable amount of an asset is estimated to be less than its carrying amount, an impairment loss is recognised immediately in the profit and loss statement.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior periods. A reversal of an impairment loss is recognised immediately in net income.

g) Provisions and contingent liabilities

Provisions are recognised when the Group has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where any of the above mentioned criteria does not exist, or is not accomplished, the Group discloses the event as a contingent liability, unless the cash outflow is remote.

Provisions for restructuring are only recognised if a detail and formal plan exists and if the plan is communicated to the related parties.

Provisions for dismantling and removal costs are recognised from the day the assets are in use and if a reliable estimate of the obligation is possible (Notes 3.c) and 39). The amount of the provision is discounted, being the corresponding effect of time recognised in net income, under the caption Net interest expense .

Provisions are updated on the balance sheet date, considering the best estimate of the Group's management.

h) Pension benefits

Under several defined benefit plans, PT Comunicações and PT Sistemas de Informação, SA (PT SI) are responsible to pay to a group of employees a pension or a pension supplement. In order to fund these obligations, various pension funds were incorporated by PT Comunicações (Note 9.1).

The amount of the Group's liabilities with respect to pensions and pension supplements is estimated based on actuarial valuations, using the Projected Unit Credit Method. The Group has elected to apply the option in IAS 19 to recognise actuarial gains and losses directly in shareholders' equity.

Plan amendments related to reduction of the benefits granted to employees are recorded as prior years' service gains or losses. Prior years' service gains or losses related to vested rights are recognised under the caption 'Post retirement benefits' when they occur. Those related to unvested rights are recognised on a straight-line basis until they become vested, which usually corresponds to the retirement date. Gains obtained with the settlement of any plan is recognized when incurred under the caption 'Curtailement costs, net'.

Pension and pension supplement liabilities stated in the balance sheet correspond to the difference between the Projected Benefit Obligation (PBO) related to pensions deducted from the fair value of pension fund assets and any prior years' service gains or losses not yet recognised.

Contributions made by the Group to defined contribution pension plans are recognised in net income when incurred.

i) Post retirement health care benefits

Under a defined benefit plan, PT Comunicações and PT SI are responsible to pay, after the retirement date, health care expenses to a group of employees and relatives. This health care plan is managed by Portugal Telecom Associação de Cuidados de Saúde (PT-ACS). In 2004, the Group established PT Prestações Mandatária de Aquisições e Gestão de Bens, SA (PT Prestações) to manage an autonomous fund to finance these obligations (Note 9.2).

The amount of the Group's liabilities with respect to these benefits after retirement date is estimated based on actuarial valuations, using the Projected Unit Credit Method. The Group has elected to apply the option in IAS 19 to recognise actuarial gains and losses directly in shareholders' equity.

Plan amendments related to reduction of the benefits granted to employees are recorded as prior years' service gains or losses. Prior years' service gains or losses related to vested rights are recognised under the caption 'Post retirement benefits' when they occur and those related to unvested rights are recognised on a straight-line basis.

until they become vested, which usually corresponds to the retirement date. Gains obtained with the settlement of any plan is recognized when incurred under the caption Curtailment costs, net .

Accrued post retirement health care liabilities stated in the balance sheet correspond to the present value of obligations from defined benefit plans, deducted from the fair value of fund assets and any prior years service gains or losses not yet recognised.

j) Pre-retirement and suspended employees

In connection with the programs related to employees that are under a suspended contract agreement, or that have pre-retired, the Group recognizes a liability in the balance sheet, which is recorded in the income statement under the caption Curtailment costs, net . This liability reflects the total responsibilities for the payment of salaries up to the retirement date and for pensions, pension supplements and health care expenses after that date, which are determined based on actuarial studies (Note 9).

k) Grants and subsidies

Grants and subsidies from the Portuguese Government and from the European Union are recognised at fair value when the receivable is probable and the Company can comply with all requirements of the subsidy s program.

Grants and subsidies to training and other operating activities are recognised in net income when the related expenses are recognised.

Grants and subsidies to acquire assets are deducted from the carrying amount of the related assets (Note 3.c).

l) Financial assets and liabilities

Financial assets and liabilities are recognised on the Group s balance sheet when the Group becomes a party to the contractual provisions of the instrument.

(i) Loans and receivables (Notes 25 and 26)

Trade receivables, loans granted and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as receivables or loans granted.

Trade receivables do not have any implicit interest and are presented at nominal value, net of allowances for estimated non-recoverable amounts, which are computed basically based on (a) the aging of the receivables and (b) the credit profile of specific customers.

(ii) Available for sale investments (Note 32)

Available for sale investments are those related to listed or quoted shares held by the Group and in connection with which the Company does not have a strategic interest. Available for sale investments are classified as non-current assets (Note 32).

All acquisitions and disposals of these investments are recognised on the date the agreement or contract is signed, independently of the settlement date. Investments are initially recognised by their acquisition cost, including any expenses related to the transaction.

Subsequent to the initial recognition, available for sale investments are measured at fair value through equity, except for available for sale investments not listed in any active market and where an estimate of fair value is not reliable which are recognised at acquisition cost, net of any impairment losses. On disposal of an impaired or an available for sale investment, accumulated changes in the fair value of the investment previously recognised in equity are transferred to net income.

(iii) Financial liabilities and equity instruments

Financial liabilities and equity instruments issued by the Group are classified according to the substance of the contractual arrangements entered into and the definitions of a financial liability and an equity instrument. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Equity instruments issued by the Group are recognised based on the proceeds, net of any costs of issuance.

Exchangeable bonds issued by Portugal Telecom are recognised as compound instruments, comprising the following elements: (i) the present value of the debt, estimated using the prevailing market interest rate for similar non-convertible debt and recorded under debt liabilities; and (ii) the fair value of the embedded option for the holder to convert the bond into equity, recorded directly in shareholders' equity. As of the balance sheet date, the debt component is recognised at amortised cost.

(iv) Bank loans (Note 35)

Bank loans are recognised as a liability based on the related proceeds, net of any transaction cost. Interest cost, which is computed based on the effective interest rate and including premiums paid upfront, is recognised when incurred.

(v) Accounts payable (Note 36)

Trade payables are recognised at nominal value, which is substantially similar to their fair value.

(vi) Derivative financial instruments and hedge accounting (Note 42)

The activities of the Group are primarily exposed to financial risks related with changes in foreign currency exchange rates and changes in interest rates. The Group's policy is to contract derivative financial instruments to hedge those risks, subject to analysis and Executive Board approval.

Derivative financial instruments are initially measured at fair value on the contract date, and are remeasured to fair value at subsequent reporting dates.

Hedge accounting

The provisions and requirements of IAS 39 must be met in order to qualify for hedge accounting. Currently, Portugal Telecom for accounting purposes classify certain derivative financial instruments as fair value and cash flow hedges.

Changes in the fair value of derivative financial instruments classified as fair value hedges are recognised in net income of the period, together with the changes in the value of the covered assets or liabilities related with the hedged risk.

The effective portion of the changes in fair value of derivative financial instruments classified as cash flow hedges is recognised directly in shareholders' equity, and the ineffective portion is recognised as financial results. When changes in the value of the covered asset or liability are recognised in net income, the corresponding amount of the derivative financial instrument previously recognised under Hedge accounting is transferred to net income.

Changes in fair value of derivative financial instruments that, in accordance with internal policies, were contracted to economically hedge an asset or liability but do not comply with the provisions and requirements of IAS 39 to be accounted for as hedges, are classified as derivatives held for trading and recognised in net income.

(vii) Treasury shares (Note 41)

Treasury shares are recognised as a deduction to shareholders' equity, under the caption Treasury shares at acquisition cost, and gains or losses obtained in the disposal of those shares are recorded under Accumulated earnings.

Equity swaps on own shares that include an option exercisable by Portugal Telecom for physical settlement are recognised as a financial liability and a corresponding reduction of equity, and are accounted for as an acquisition of treasury shares on the inception date of the contract.

(viii) Cash and cash equivalents and short term investments (Note 24)

Cash and cash equivalents comprise cash on hand and demand bank deposits, due within three months or less from the date of acquisition that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

In the consolidated cash flow statement, cash and cash deposits also includes overdrafts recognised under the caption Short-term debt .

Short term investments comprise investments for the purpose of generating investment returns, and they are therefore not classified as cash equivalents.

(ix) Qualified Technological Equipment transactions

In previous years, the Company entered into certain Qualified Technological Equipment transactions (QTE), whereby some telecommunications equipment was sold to certain foreign entities. Simultaneously, those foreign entities entered into leasing contracts with respect to the equipment with special purpose entities, which entered into conditional sale agreements to resell the related equipment to the Company. The Company maintains the legal possession of this equipment.

These transactions correspond to a sale and lease-back transaction, and the equipment continued to be recorded on the Company s consolidated balance sheet. The Company obtained the majority of the economic benefits of the special purpose entities, and therefore those entities were fully consolidated in the Company s financial statements. Consolidated non-current assets include an amount equivalent to the proceeds of the sale of the equipment (Note 30), and non-current liabilities include the future payments under the leasing contract (Note 40). As at the balance sheet date, those amounts are measured at fair value.

Up-front fees received from this transaction are recognised in net income on a straight-line basis during the period of the contracts.

m) Own work capitalized

Certain internal costs (materials, work force and transportation) incurred to build or produce tangible assets are capitalized only if:

- the tangible assets are identifiable;
- the tangible assets will generate future economic benefits which can be reliably estimated; and
- development expenses can be reliably measured.

The amounts capitalized are deducted from the corresponding operating costs incurred and no internally generated margin is recognised. When any of the above mentioned criteria is not met, the expense is recognised in net income.

Financial costs are not capitalised and expenses incurred during investigation are recognised in net income when incurred.

n) Leasings (the company as a lessee)

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases (Note 13). The classification of leases depends on the substance of the transaction and not on the form of the contract.

Assets acquired under finance leases and the corresponding liability to the lessor, are accounted for using the finance method, in accordance with the lease payment plan (Note 35). Interest included in the rents and the depreciation of the assets are recognised in net income in the period they occur.

Under operating leases, rents are recognised on a straight-line basis during the period of the lease (Note 13).

o) Taxation

Income tax expense represents the sum of the tax currently payable and deferred tax. Income tax is recognised in accordance with IAS 12.

Portugal Telecom has adopted the tax consolidation regime in Portugal (currently known as the special regime for the taxation of groups of companies). The provision for income taxes is determined on the basis of the estimated taxable income for all the companies in which Portugal Telecom holds at least 90% of the share capital and that are domiciled in Portugal and subject to Corporate Income Tax (IRC). The remaining Group companies not covered by the tax consolidation regime of Portugal Telecom are taxed individually based on their respective taxable income, at the applicable tax rates.

The tax currently payable is based on taxable income for the period, and the deferred tax is based on differences between the carrying amounts of assets and liabilities of the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method.

Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is reasonably likely that taxable income will be available against which deductible temporary differences can be used, or when there are deferred tax liabilities whose reversal is expected in the same period in which the deferred tax assets reverse. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that is no longer probable that sufficient taxable income will be available to allow for all or part of the asset to be recovered.

Deferred tax is charged to net income, except when it relates to items charged or credited directly to shareholders' equity, in which case the deferred tax is also recognised directly in shareholders' equity.

p) Revenue recognition

Revenues from fixed line telecommunications are recognised at their gross amounts when services are rendered. Billings for these services are made on a monthly basis throughout the month. Unbilled revenues or revenues not billed by other operators but accrued or incurred as of the date of the financial statements are recorded based on estimates. Differences between accrued amounts and the actual unbilled revenues, which ordinarily are not significant, are recognised in the following period.

Revenues from international telecommunications services are divided with the operators in the country in which calls are terminated based on traffic records of the country of origin and rates established in agreements with the various telecommunications operators. The operator of the country of origin of the traffic is responsible for crediting the operator of the destination country and, if applicable, the operators of the transit countries.

Revenues from telephone line rentals are recognised as an operating lease in the period to which they apply, under the caption **Other revenues**.

Revenues from ISP services result essentially from monthly subscription fees and telephone traffic when the service is used by customers. These revenues are recognised when the service is rendered.

Advertising revenues from telephone directories and related costs are recognised in the period in which the directories are effective. PT Comunicações has a contract with Páginas Amarelas whereby the latter is responsible for production, publishing and distribution of PT Comunicações' telephone directories, as well as for selling advertising space in the directories. The total cost to be paid by PT Comunicações for such services is set at a fixed 64% of its gross revenues from the sale of advertising space in telephone directories. The prices of advertising space are fixed, not contingent, and based on the expected volume of the distributed directories (approximately one to every telephone number). Revenues from the sale of advertising space are invoiced directly by PT Comunicações to its corporate clients during the one-year advertising period. These revenues are recognized in earnings on a monthly basis during the period for the respective directory.

Revenues from mobile telephony services result essentially from the use of the wireless network, by customers or other operators. The moment in which revenues are recognised and the corresponding caption are as follows:

| Nature of the revenue | Caption | Moment of recognition |
|------------------------------------|-------------------|--------------------------------------|
| Use of the network | Services rendered | In the month the service is rendered |
| Interconnection fees | Services rendered | In the month the service is rendered |
| Roaming | Services rendered | In the month the service is rendered |
| Pre-paid cards | Services rendered | When the service is rendered |
| Terminal equipment and accessories | Sales | When the sale occurs |

Revenues from bundling services or products are allocated to each of its components based on its fair value and are recognised separately in accordance with the methodology adopted to each component.

Revenues from the Pay-TV result essentially from and are recognised as follows: (i) monthly subscription fees for the use of the service are recognised in the period the service is rendered; (ii) rental of equipment is recognised in the period it is rented; and (iii) sale of equipment is recognised at the moment of sale.

q) Foreign currency transactions and balances

Transactions denominated in foreign currencies are translated to Euros at the exchange rates prevailing at the time the transactions are made. At the balance sheet date, assets and liabilities denominated in foreign currencies are adjusted to reflect the exchange rates prevailing at such date. The resulting gains or losses on foreign exchange transactions are recognised in net income. Exchange differences on non-monetary items, including goodwill, and on monetary items representing an extension of the related investment and where settlement is not expected in the foreseeable future, are recognized directly in shareholders' equity under the caption "Foreign currency translation adjustments", and included in the Statement of Recognised Income and Expenses.

The financial statements of subsidiaries operating in other countries are translated to Euros, using the following exchange rates:

- Assets and liabilities at exchange rates prevailing at the balance sheet date;
- Profit and loss items at average exchange rates for the reported period;

- Cash flow items at average exchange rates for the reported period, where these rates approximate the effective exchange rates (and in the remaining cases, at the rate effective on the day the transaction occurred); and
- Share capital, reserves and retained earnings at historical exchange rates.

The effect of translation differences is recognised in shareholders' equity under the caption 'Foreign currency translation adjustments' and included in the Statement of Recognised Income and Expenses.

The Group adopted the exception under IFRS 1 relating to cumulative translation adjustments as of 1 January 2004 and transferred this amount from 'Foreign currency translation adjustments' to 'Accumulated earnings'. As from 1 January 2004, the Group has been recognizing all translation adjustments directly in shareholders' equity and therefore these amounts are transferred to net income only if and when the related investments are disposed of.

r) Borrowing costs

Borrowing costs related to loans are recognised in net income when incurred. The Group does not capitalise any borrowing costs related to loans to finance the acquisition, construction or production of any asset.

s) Cash flow statement

The consolidated statement of cash flows is prepared under IAS 7, using the direct method. The Group classifies all highly liquid investments purchased, with original maturity of three months or less, as cash and cash equivalents. The 'Cash and cash equivalents' item presented in the statement of cash flows also includes overdrafts, classified in the balance sheet under 'Short-term debt'.

Cash flows are classified in the statement of cash flows according to three main categories, depending on their nature: (1) operating activities; (2) investing activities; and (3) financing activities. Cash flows from operating activities include primarily collections from clients, payments to suppliers, payments to employees, payments relating to post retirement benefits and net payments relating to income taxes and indirect taxes. Cash flows from investing activities include primarily the acquisitions and disposals of investments in associated companies, dividends received from associated companies and purchase and sale of property, plant and equipment. Cash flows from financing activities include primarily borrowings and repayments of debt, payments of lease rentals, payments

relating to interest and related expenses, acquisition and sale of treasury shares and payments of dividends to shareholders.

t) Subsequent events (Note 47)

Events that occur after the balance sheet date that could influence the value of any asset or liability as of that date are considered when preparing the financial statements for the period. Those events are disclosed in the notes to the financial statements, if material.

Critical judgments and estimates

The preparation of the consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the application of policies and reported amounts. Estimates and judgements are continually evaluated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances on which the estimate was based, or as a result of new information or more experience. The main accounting judgments and estimates reflected in the consolidated financial statements, are as follows:

- (a) **Post retirement benefits** The present value of the post retirement obligation is computed based on actuarial methodologies, which use certain actuarial assumptions. Any changes in those assumptions will impact the carrying amount of post retirement obligations. The key assumptions for post retirement obligations are disclosed in Note 9.
- (b) **Goodwill impairment analysis** Portugal Telecom tests annually whether goodwill has suffered any impairment. The recoverable amounts of cash-generating units have been determined based on value-in-use calculations. The use of this method requires the estimate of future cash flows expected to arise from the continuing operation of the cash generating unit and the choice of a suitable discount rate in these estimates.
- (c) **Valuation and useful life of intangible assets** Portugal Telecom has made assumptions in relation to the potencial future cash flows resulting from separable intangible assets acquired as part of business combinations, which include expected future revenues, discount rates and useful life of such assets.
- (d) **Recognition of provisions and adjustments** Portugal Telecom is party to various legal claims for which, based on the opinion of its legal advisors, a judgment is made to determine whether a provision should be recorded for these contingencies (Note 46). Adjustments for accounts receivable are computed based primarily on the aging of the receivables, the risk profile of the customer and its financial condition. These estimates related to adjustments for accounts receivables differ from business to business.
- (e) **Assessment of the fair value of financial instruments** Portugal Telecom chooses an appropriate valuation technique for financial instruments not quoted in an active market based on its best knowledge of the market

and of the assets. In this process, Portugal Telecom applies the valuations techniques commonly used by market practitioners and uses assumptions based on market rates.

Estimates used are based on the best information available during the preparation of consolidated financial statements, although future events, neither controlled nor foreseeable by the Company, could occur and have an impact on the estimates. Changes to the estimates used by management, that occur after the date of the consolidated financial statements are recognised in net income, in accordance with IAS 8, using a prospective methodology.

4. Changes in accounting policies and estimates

During the year 2007, no changes occurred in the accounting policies used by the Group, when compared to those ones used in 2006.

The only new standard adopted by Portugal Telecom during the year ended 31 December 2007 was IFRS 7 Financial instruments . The impact of adopting this standard consisted in including additional disclosures related to financial instruments (Note 42).

In addition, when the Board of Directors approved these financial statements, the following standards and interpretations, not yet adopted by Portugal Telecom, had been issued, but their application is only being required in subsequent years:

- IAS 23 (revised) - Borrowing costs (years started on or after 1 January 2009);
- IFRS 8 - Segment reporting (years started on or after 1 January 2009);
- IFRIC 11 - Treasury share transactions (years started on or after 1 March 2007);
- IFRIC 12 - Concession contracts (years started on or after 1 January 2008);
- IFRIC 13 - Loyalty programs (years started on or after 1 July 2008);
- IFRIC 14 - Defined benefits (years started on or after 1 January 2008);
- IAS 1 (revised) - Presentation of financial statements (years started on or after 1 January 2009);
- IAS 27 (revised) - Consolidated and separate financial statements (years started on or after 1 July 2009);
- IAS 28 (revised) - Investments in associates (years started on or after 1 July 2009);

- IAS 31 (revised) - Interests in joint ventures (years started on or after 1 July 2009);
- IAS 32 (revised) - Financial instruments: presentation (years started on or after 1 January 2009);
- IFRS 2 (revised) - Share-based payments (years started on or after 1 January 2009); and
- IFRS 3 (revised) - Business combinations (years started on or after 1 July 2009).

The possible impact of adopting the above standards and interpretations in future years has not been fully assessed by Portugal Telecom.

5. Exchange rates used to translate foreign currency financial statements

As at 31 December 2007 and 2006, assets and liabilities denominated in foreign currencies were translated to Euros using the following exchange rates:

| Currency | 2007 | 2006 |
|-----------------------|----------|----------|
| Argentine peso | 4.6386 | 4.0474 |
| Australian dollar | 1.6757 | 1.6691 |
| Botswana pula | 8.9056 | 7.9313 |
| Brazilian real | 2.5963 | 2.8118 |
| British pound | 0.73335 | 0.6715 |
| Canadian dollar | 1.4449 | 1.5281 |
| Cape Verde Escudo | 110.2650 | 110.2650 |
| CFA franc | 655.9570 | 655.9570 |
| Chinese Yuan Renmimbi | 10.7524 | 10.009 |
| Danish krone | 7.4583 | 7.456 |
| Hong Kong dollar | 11.48 | 10.2409 |
| Hungarian forint | 253.7300 | 251.7700 |
| Japanese yen | 164.9300 | 156.9300 |
| Kenyan shilling | 93.552 | 91.6632 |
| Macao pataca | 11.8244 | 10.5481 |
| Moroccan dirham | 11.4042 | 11.1354 |
| Mozambique metical | 34.8300 | 34.4700 |
| Namibian dollar | 10.0298 | 9.2124 |
| Norwegian krone | 7.9580 | 8.2380 |
| São Tomé Dobra | 20,947.9 | 17,222.3 |
| South African rand | 10.0298 | 9.2124 |
| Swedish krone | 9.4415 | 9.0404 |
| Swiss franc | 1.6547 | 1.6069 |
| Ugandan shilling | 2,499.6 | 2,292.2 |
| US Dollar | 1.4721 | 1.317 |

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During the years 2007 and 2006, income statements of subsidiaries expressed in foreign currencies were translated using the following average exchange rates to the Euro:

| Currency | 2007 | 2006 |
|-----------------------|----------|----------|
| Argentine peso | 4.3073 | 3.8875 |
| Botswana pula | 8.4729 | 7.3955 |
| Brazilian real | 2.6661 | 2.7315 |
| Cape Verde Escudo | 110.2650 | 110.2650 |
| CFA franc | 655.9570 | 655.9570 |
| Chinese Yuan Renmimbi | 10.4294 | 10.3807 |
| Hungarian forint | 251.3667 | 264.1325 |
| Kenyan shilling | 92.6231 | 90.8083 |
| Macao pataca | 11.037 | 10.0475 |
| Moroccan dirham | 11.2352 | 11.0362 |
| Mozambique metical | 35.5658 | 32.1779 |
| Namibian dollar | 9.6837 | 7.7668 |
| São Tomé Dobra | 18,737.3 | 15,735.4 |
| Swiss franc | 1.6438 | 1.5731 |
| Ugandan shilling | 2,369.8 | 2,310.2 |
| US Dollar | 1.3732 | 1.2557 |

6. Revenues

Consolidated revenues by reportable segment in 2007 and 2006, are as follows:

| | 2007 | 2006 |
|------------------------------------|---------------|---------------|
| Wireline (Note 7.a) | 1,843,549,443 | 1,952,996,699 |
| Services rendered (Note 3.p) | 1,784,077,277 | 1,903,558,954 |
| Sales (i) | 40,062,027 | 32,105,763 |
| Other revenues (ii) | 19,410,139 | 17,331,982 |
| Domestic Mobile - TMN (Note 7.b) | 1,464,603,409 | 1,426,182,034 |
| Services rendered (Note 3.p) | 1,321,677,241 | 1,290,765,345 |
| Sales (i) | 135,300,250 | 126,042,387 |
| Other revenues (ii) | 7,625,918 | 9,374,302 |
| Brazilian Mobile - Vivo (Note 7.c) | 2,462,940,843 | 2,104,711,912 |
| Services rendered (Note 3.p) | 2,157,218,441 | 1,789,759,729 |
| Sales (i) | 258,068,670 | 254,752,333 |
| Other revenues (ii) | 47,653,732 | 60,199,850 |
| Other businesses (iii) | 377,315,497 | 281,396,974 |
| Services rendered | 362,522,479 | 261,804,841 |
| Sales | 9,035,536 | 13,330,488 |
| Other revenues | 5,757,482 | 6,261,645 |
| | 6,148,409,192 | 5,765,287,619 |

-
- (i) These captions include mainly the sales of terminal equipment (fixed telephones and modems) of the wireline business and terminal mobile equipments of TMN and Vivo.
 - (ii) Other revenues include mainly the benefits from contractual penalties imposed to customers, rentals of equipment and of other own infra-structures, and revenues resulting from consultancy projects.
 - (iii) This caption is related to services rendered and sales primarily from MTC (mobile operator in Namibia), Mobitel (call center operation in Brazil) and Cabo Verde Telecom (telecommunications operator).

Consolidated revenues in 2007 and 2006 by geographic area, are as follows:

| | 2007 | 2006 |
|-----------------|---------------|---------------|
| Portugal | 3,397,647,288 | 3,460,826,637 |
| Brazil | 2,528,111,431 | 2,165,975,225 |
| Other countries | 222,650,473 | 138,485,757 |
| | 6,148,409,192 | 5,765,287,619 |

7. Segment reporting

Portugal Telecom's primary basis of business segmentation is related to the nature of the services rendered and the type of technology used by its operating companies. This is the manner in which the Board of Directors oversees and controls the business and also the manner in which financial information is internally organized and communicated. Accordingly, the business segments from the continuing operations as at 31 December 2007 and 2006 are as follows:

- a. Wireline (including Retail, Wholesale and Data and Corporate);
- b. Domestic Mobile (TMN); and
- c. Brazilian Mobile (Vivo).

The Wireline segment includes PT Comunicações, PT Prime, PT.com and PT Corporate.

In relation to the mobile businesses, Portugal Telecom has identified two different business segments, the Domestic Mobile and Brazilian Mobile, due to the differences between licenses and technologies of both. In terms of technology, GSM/UMTS is the technology used by TMN, while CDMA is the main technology used by Vivo. Also, the telecommunications markets in Portugal and Brazil are substantially different in terms of economic and regulatory environment, classes of customers, suppliers and marketing strategies, which support Portugal Telecom's decision to establish the two different businesses.

Portugal Telecom's secondary basis of segmentation is geographical, under which it distinguishes three segments:

- a. Portugal;

- b. Brazil; and
- c. Other countries.

Segment information for the years 2007 and 2006 is presented below.

a) Wireline

Income statements of this reportable segment for the years 2007 and 2006 are as follows:

| | 2007 | 2006 |
|---|---------------|---------------|
| REVENUES | | |
| Services rendered - external customers (Note 6) | 1,784,077,277 | 1,903,558,954 |
| Services rendered - inter-segment | 106,630,112 | 108,723,206 |
| Sales - external customers (Note 6) | 40,062,027 | 32,105,763 |
| Sales - inter-segment | 472,987 | 679,411 |
| Other revenues - external customers (Note 6) | 19,410,139 | 17,331,982 |
| Other revenues - inter-segment | 11,764,082 | 9,382,218 |
| | 1,962,416,624 | 2,071,781,534 |
| COSTS, EXPENSES, LOSSES AND (INCOME) | | |
| Wages and salaries | 252,859,780 | 271,970,593 |
| Post retirement benefits (i) | (65,301,000) | (71,553,000) |
| Direct costs | 354,011,295 | 356,128,163 |
| Costs of products sold | 37,632,031 | 32,678,000 |
| Marketing and publicity | 36,247,639 | 39,630,306 |
| Support services | 114,137,429 | 116,995,350 |
| Supplies and external services | 213,355,242 | 210,004,952 |
| Indirect taxes | 5,480,850 | 5,891,200 |
| Provisions and adjustments | 5,203,944 | 37,183,186 |
| Depreciation and amortisation | 323,606,387 | 355,521,631 |
| Work force reduction program costs (ii) | 274,849,277 | 6,091,803 |
| Net gains on disposals of fixed assets | (9,290,728) | (2,617,722) |
| Other costs, net | 16,814,997 | 14,015,578 |
| | 1,559,607,143 | 1,371,940,040 |
| Income before financial results and taxes | 402,809,481 | 699,841,494 |
| Net interest expenses (income) | 2,081,218 | (93,455) |
| Net foreign currency exchange losses | 1,106,563 | 1,740,579 |
| Net gains on financial assets and other investments | (1,415,656) | (1,445,020) |
| Net other financial expenses | 1,390,107 | 967,217 |
| | 3,162,232 | 1,169,321 |
| Income before taxes | 399,647,249 | 698,672,173 |
| Minus: Income taxes | 115,696,441 | 209,608,152 |
| Net income | 283,950,808 | 489,064,021 |

(i) Post retirement benefits were negative in 2007 and 2006 due to the the recognition of prior years service gains of Euro 110,336,000 and Euro 150,556,684, respectively, related to plan ammendmnts occurred during these years (Note 9).

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- (ii) The increase in this caption is mainly due to the recognition of a gain amounting to Euro 220,417,000 in 2006 related to the impact of the termination of the Protocol with the national healthcare system under the Health Care Plan (Note 9.2) and higher costs with the work force reduction program in 2007.

Total assets and liabilities of this segment as at 31 December 2007 and 2006 are as follows:

| | 2007 | 2006 |
|-------------|---------------|---------------|
| Assets | 3,937,770,341 | 4,203,333,498 |
| Liabilities | 3,012,740,702 | 3,152,213,639 |

Capital expenditures in tangible and intangible assets for this reportable segment for the years 2007 and 2006 were Euro 292 million and Euro 239 million, respectively. The increase in capital expenditures is primarily explained by a contract entered into by PT Comunicações for the acquisition of satellite capacity until 2015 for an aggregate amount of Euro 42.6 million (Note 33).

As at 31 December 2007 and 2006, the total staff in the wireline business was 6,354 and 7,181 employees, respectively.

b) Domestic Mobile TMN

Income statements of this reportable segment for the years 2007 and 2006 are as follows:

| | 2007 | 2006 |
|--|---------------|---------------|
| REVENUES | | |
| Services rendered - external customers (Note 6) | 1,321,677,241 | 1,290,765,345 |
| Services rendered - inter-segment | 71,379,851 | 72,468,785 |
| Sales - external customers (Note 6) | 135,300,250 | 126,042,387 |
| Sales - inter-segment | 6,485,902 | 3,636,530 |
| Other revenues - external customers (Note 6) | 7,625,918 | 9,374,302 |
| Other revenues - inter-segment | 469,979 | 68,881 |
| | 1,542,939,141 | 1,502,356,230 |
| COSTS, EXPENSES, LOSSES AND (INCOME) | | |
| Wages and salaries | 52,728,072 | 56,002,890 |
| Direct costs | 282,600,676 | 292,852,093 |
| Costs of products sold | 179,705,328 | 170,555,611 |
| Marketing and publicity | 34,387,480 | 30,350,283 |
| Support services | 46,523,659 | 35,393,808 |
| Supplies and external services | 225,351,681 | 224,154,024 |
| Indirect taxes | 29,746,098 | 22,670,064 |
| Provisions and adjustments | 12,920,301 | 11,679,529 |
| Depreciation and amortisation | 223,605,934 | 220,113,746 |
| Work force reduction costs | 627,947 | 669,084 |
| Net losses on disposals of fixed assets | 1,212,349 | 25,558 |
| Other costs | 1,876,062 | 2,179,235 |
| | 1,091,285,587 | 1,066,645,925 |
| Income before financial results and taxes | 451,653,554 | 435,710,305 |
| Net interest income | (10,489,597) | (5,283,072) |
| Net foreign currency exchange losses | 73,674 | 516,813 |
| Equity in losses (earnings) of affiliated companies, net | 2,614 | (3,385) |
| Net other financial expenses | 1,038,056 | 941,236 |
| | (9,375,253) | (3,828,408) |
| Income before taxes | 461,028,807 | 439,538,713 |
| Minus: Income taxes | 123,025,875 | 121,484,647 |
| Net income | 338,002,932 | 318,054,066 |

Total assets and liabilities of this segment as at 31 December 2007 and 2006 are as follows:

| | 2007 | 2006 |
|-------------|---------------|---------------|
| Assets | 2,433,369,333 | 2,496,628,387 |
| Liabilities | 1,425,678,744 | 1,205,928,371 |

Capital expenditures in tangible and intangible assets for this reportable segment for the years 2007 and 2006 were Euro 440 million and Euro 189 million, respectively. The increase in capital expenditures for this reportable segment is primarily explained by an amount of Euro 242 million (Note 33) capitalized in 2007, and is related to the

commitments assumed by TMN under the UMTS license based on the agreement signed by TMN with the Portuguese Government in 2007 which determined the initiatives that will be undertaken (Note 33).

As at 31 December 2007 and 2006, the total staff in this segment was 1,144 and 1,140 employees, respectively.

c) Brazilian Mobile

Income statements of this reportable segment for the years 2007 and 2006 are as follows:

| | 2007 | 2006 |
|--|---------------|---------------|
| REVENUES | | |
| Services rendered - external customers (Note 6) (i) | 2,157,218,441 | 1,789,759,729 |
| Sales - external customers (Note 6) | 258,068,670 | 254,752,333 |
| Other revenues - external customers (Note 6) | 47,653,732 | 60,199,850 |
| Other operating revenues - inter-segment | 15,351 | |
| | 2,462,956,194 | 2,104,711,912 |
| COSTS, EXPENSES, LOSSES AND (INCOME) | | |
| Wages and salaries | 128,804,738 | 115,504,566 |
| Direct costs (i) | 428,423,619 | 248,871,761 |
| Costs of products sold | 449,411,844 | 385,151,405 |
| Marketing and publicity | 65,964,388 | 63,767,476 |
| Support services | 186,507,248 | 158,990,603 |
| Supplies and external services | 352,103,602 | 345,117,155 |
| Indirect taxes | 151,446,132 | 126,913,606 |
| Provisions and adjustments | 105,270,191 | 164,187,221 |
| Depreciation and amortisation | 523,077,105 | 505,846,599 |
| Net losses (gains) on disposals of fixed assets | 5,736,801 | (2,431,564) |
| Other costs (ii) | 2,354,339 | 56,528,474 |
| | 2,399,100,007 | 2,168,447,302 |
| Income before financial results and taxes | 63,856,187 | (63,735,390) |
| Net interest expense (iii) | 64,187,559 | 92,429,146 |
| Net foreign currency exchange gains | (2,249,366) | (8,530,559) |
| Net losses (gains) on financial assets and other investments | (1,738,911) | 4,103,236 |
| Net other financial expenses | 25,784,002 | 31,602,515 |
| | 85,983,284 | 119,604,338 |
| Income before taxes | (22,127,097) | (183,339,728) |
| Minus: Income taxes | (631,639) | (156,886,220) |
| Net income | (21,495,458) | (26,453,508) |

(i) The increase in services rendered and in direct costs is primarily explained by the changes in the interconnection regulatory regime in Brazil (termination of the Bill & Keep regime), which led to

the gross recognition of interconnection revenues and costs (Note 10).

- (ii) In 2006, this caption includes approximately Euro 51 million (Note 15) related to the adjustment of the realizable amount of CDMA equipments due to technological obsolescence.

- (iii) The change in this caption is mainly related to a gain recorded in 2006 amounting to Euro 134 million (Note 19), related to the recognition of deferred tax assets related to tax losses from previous periods, which recoverability was only achieved in 2006.

Capital expenditures in tangible and intangible assets for this reportable segment for the years 2007 and 2006 were Euro 360 million and Euro 387 million, respectively.

A summarized balance sheet of 50% of the assets and liabilities of Vivo as at 31 December 2007 and 2006 is presented below:

| | 2007 | 2006 |
|-------------------------------|---------------|---------------|
| Current assets | 1,193,252,087 | 902,752,315 |
| Intangible assets | 2,303,677,393 | 2,245,254,964 |
| Tangible assets | 1,200,360,228 | 1,131,810,840 |
| Deferred taxes | 384,944,524 | 351,507,323 |
| Other non-current assets | 167,866,145 | 142,454,925 |
| Total assets | 5,250,100,377 | 4,773,780,367 |
| Current liabilities | 1,331,838,063 | 1,059,188,211 |
| Medium and long-term debt | 462,660,429 | 517,255,183 |
| Other non-current liabilities | 104,569,993 | 87,071,963 |
| Total liabilities | 1,899,068,485 | 1,663,515,357 |

As at 31 December 2007 and 2006, the total staff in this segment (50% of Vivo) was 2,800 and 2,948 employees, respectively.

d) Reconciliation of revenues, net income, assets and liabilities

In 2007 and 2006, the reconciliation between revenues of reportable segments and consolidated revenues is as follows:

| | 2007 | 2006 |
|--|---------------|---------------|
| Total relating to reportable segments | 5,968,311,959 | 5,678,849,676 |
| Total relating to other businesses (i) | 668,097,060 | 549,720,637 |
| Elimination of intragroup revenues | (487,999,827) | (463,282,694) |
| Total consolidated revenues | 6,148,409,192 | 5,765,287,619 |

(i) The increase in this caption is mainly related to the consolidation of MTC from September 2006, which contributed with Euro 120 million and Euro 41 million to Portugal Telecom's consolidated operating revenues in 2007 and 2006, respectively.

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In 2007 and 2006, the reconciliation between net income of reportable segments and consolidated net income, is as follows:

| | 2007 | 2006 |
|---|---------------|---------------|
| Total relating to reportable segments | 600,458,282 | 780,664,579 |
| Total relating to other businesses (i) | 22,762,416 | (38,875,968) |
| Other items not included in reportable segments: | | |
| Net interest expense related with loans obtained at group level | (141,589,112) | (133,020,722) |
| Net foreign currency exchange gains | (13,496,147) | (1,805,476) |
| Net gains on financial assets and other investments (ii) | 245,628,440 | 20,991,979 |
| Equity in earnings of affiliated companies | 126,130,271 | 130,602,471 |
| Income tax not included in reportable segments (iii) | (5,186,988) | 195,570,950 |
| Consolidated net income | 834,707,162 | 954,127,813 |

-
- (i) The improvement in this caption is mainly related to: (1) the increase of MTC's contribution to Portugal Telecom's consolidated income before financial results and taxes, from Euro 19 million in 2006 to Euro 50 million in 2007, since this company was only acquired on September 2006; and (2) the reduction in expenses incurred by Portugal Telecom with the tender offer launched by Sonae, from Euro 35 million in 2006 to Euro 7 million in 2007 (Note 15).
- (ii) In 2007, this caption includes primarily (a) the gain of Euro 110,955,318 (Note 17) related to the disposal of a 22% stake in Africatel, the holding company that aggregates all of Portugal Telecom's interests in sub-Saharan Africa, (b) gains of Euro 38,650,508 (Note 17) related to the disposal of available for sale investments, (c) the gain of Euro 77,428,725 (Note 42) related to the change in the fair value of the equity swaps over PT Multimedia shares up to its settlement date, and (d) the gain of Euro 32,188,194 (Note 17) related to the financial settlement of equity swaps over own shares.
- (iii) In 2006, this caption includes mainly (a) the recognition of a tax credit amounting to Euro 53 million (Note 19) related to the liquidation of a subsidiary, and (b) a gain of Euro 142 million (Note 19) resulting from the reduction of deferred tax liabilities following the adoption by the Company of the voluntary taxation regime for certain gains on the disposals of investments made in previous years, whose taxation was deferred at that time in accordance with the tax legislation.

As at 31 December 2007 and 2006, the reconciliation between assets of reportable segments and consolidated assets is as follows:

| | 2007 | 2006 |
|--|----------------|----------------|
| Total assets relating to reportable segments (i) | 11,621,240,051 | 12,625,567,751 |
| Total assets relating to other businesses and eliminations | 906,038,480 | 894,074,388 |
| Other items not included in reportable segments: | | |
| Investments in group companies and other investments (ii) | 541,578,046 | 585,838,311 |
| Goodwill (Note 33) | 53,314,309 | 65,768,850 |
| Total consolidated assets | 13,122,170,886 | 14,171,249,300 |

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- (i) As at 31 December 2006, this caption includes Euro 1,151,825,499 (Note 20) related to PT Multimédia segment, which following the conclusion of its spin-off on November 2007 (Note 1) is no longer part of the Portugal Telecom Group as at 31 December 2007.

(ii) The reduction in this caption is primarily explained by the disposal of the investment in Banco Espírito Santo, which as at 31 December 2006 amounted to Euro 95,340,000 (Note 32).

As at 31 December 2007 and 2006, the reconciliation between liabilities of reportable segments and consolidated liabilities is as follows:

| | 2007 | 2006 |
|---|----------------|----------------|
| Total liabilities relating to reportable segments (i) | 6,337,487,931 | 6,572,770,085 |
| Total liabilities relating to other businesses and eliminations | (311,183,699) | (252,389,174) |
| Other items not included in reportable segments: | | |
| Loans obtained at a group level | 5,014,056,466 | 4,744,830,451 |
| Total consolidated liabilities | 11,040,360,698 | 11,065,211,362 |

(i) As at 31 December 2006, this caption includes Euro 551,112,718 (Note 20) related to PT Multimédia segment, which following the conclusion of its spin-off on November 2007 (Note 1) is no longer part of the Portugal Telecom Group as at 31 December 2007.

Total assets, liabilities, tangible assets and intangible assets by geographic area as at 31 December 2007 and 2006 and capital expenditures for tangible and intangible assets in 2007 and 2006 are as follows:

| | Total assets | Total liabilities | 2007 Tangible assets (Note 34) | Intangible assets (Note 34) | Capital expenditures for tangible and intangible assets (iv) |
|--------------|----------------|-------------------|--------------------------------------|--------------------------------|--|
| Portugal (i) | 6,801,516,786 | 5,178,641,633 | 2,251,017,698 | 926,355,217 | 732,917,156 |
| Brazil (ii) | 5,465,930,992 | 1,947,534,215 | 1,215,150,692 | 2,309,185,592 | 366,870,020 |
| Other (iii) | 854,723,108 | 3,914,184,850 | 119,228,781 | 147,582,618 | 41,246,244 |
| | 13,122,170,886 | 11,040,360,698 | 3,585,397,171 | 3,383,123,427 | 1,141,033,420 |

| | Total assets | Total liabilities | 2006 Tangible assets (Note 34) | Intangible assets (Note 34) | Capital expenditures for tangible and intangible assets (iv) |
|--------------|----------------|-------------------|--------------------------------------|--------------------------------|--|
| Portugal (i) | 8,502,616,584 | 6,131,463,187 | 2,685,753,152 | 1,148,693,900 | 447,662,366 |
| Brazil | 4,866,913,022 | 1,690,551,545 | 1,145,651,310 | 2,249,235,370 | 392,932,179 |
| Other (iii) | 801,719,694 | 3,243,196,630 | 110,628,728 | 92,951,993 | 27,132,211 |
| | 14,171,249,300 | 11,065,211,362 | 3,942,033,190 | 3,490,881,263 | 867,726,756 |

(i) The reduction in assets, liabilities, tangible and intangible assets from domestic businesses is primarily related to the contribution of the PT Multimedia segment to these captions as at 31 December 2006, which amounted to Euro 1,151,825,499, Euro 551,112,718, Euro 297,282,364 (Note 34) and Euro 413,567,344 (Note 33), respectively. As at 31 December 2007,

PT Multimédia is no longer part of the Portugal Telecom Group, following the conclusion of its spin-off on November 2007 (Note 1).

- (ii) The increase in assets and liabilities is mainly related to the appreciation of the Brazilian Real.
- (iii) As at 31 December 2007, assets and liabilities of other geographic areas include Euro 194,140,064 and Euro 3,834,321,109 respectively, related to PT Finance, the group finance subsidiary incorporated in the Netherlands. The assets of PT Finance correspond mainly to short-term investments and the liabilities correspond mainly to loans obtained in financial markets, which are then used to finance the Company's businesses primarily in Portugal. As at 31 December 2006, assets and liabilities of other geographic areas include Euro 195,242,342 and Euro 3,158,205,855 respectively, related to PT Finance.
- (iv) In 2007, capital expenditures from domestic businesses include an amount of Euro 241,746,603 (Note 33) related to the commitments assumed by under the UMTS license.

8. Wages and salaries

During the years 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|-------------------|-------------|-------------|
| Salaries | 504,988,145 | 501,631,356 |
| Employee Benefits | 101,273,912 | 94,461,544 |
| Health care | 10,833,038 | 14,453,749 |
| Training | 6,909,253 | 7,464,074 |
| Social care | 5,981,553 | 7,923,609 |
| Insurance | 4,844,672 | 4,309,507 |
| Other | 3,242,300 | 3,233,344 |
| | 638,072,873 | 633,477,183 |

9. Post retirement benefits

9.1. Pension benefits

As referred to in Note 3.h, PT Comunicações is responsible for the payment of pensions and pension supplements to retired, suspended and active employees. These liabilities, which are estimated based on actuarial valuations, are as follows:

- a) Retirees and employees of Telecom Portugal (Plan CGA) hired prior to 14 May 1992, or who were retired on that date, are entitled to receive a pension benefit from PT Comunicações. Employees hired after that

date are covered by the general Portuguese Government social security system. Suspended employees are also entitled to receive a benefit payment normally equal to approximately 90% of salary prior to leaving service (with an annual increase in some cases).

b) Retirees and employees of TLP hired prior to 23 June 1994 are entitled to receive a pension supplement from PT Comunicações, which complements the pension paid by the Portuguese social security system. Pre-retired employees are also entitled to receive benefit payments (equal to 25% to 80% of their base salaries at the time of pre-retirement) until they reach the Portuguese social security retirement age. After that date, these former employees become entitled to the pension supplement. Suspended employees are also entitled to receive a benefit payment normally equal to 90% of salary prior to leaving service (with an annual increase in some cases).

c) Retirees and employees of TDP hired prior to 23 June 1994 are entitled to receive a pension supplement from PT Comunicações, which complements the pension paid by the Portuguese social security system. Pre-retired employees are also entitled to receive benefit payments (equal to 25% to 80% of their base salaries at the time of pre-retirement) until they reach the Portuguese social security retirement age. After that date, these employees have the right to this pension supplement. Suspended employees are also entitled to receive a benefit payment normally equal to approximately 90% of salary prior to leaving service (with an annual increase in some cases).

d) Retirees and employees of Companhia Portuguesa Rádio Marconi, SA (Marconi , a company merged into PT Comunicações in 2002) hired prior to 1 February 1998 are entitled to a pension benefit from Caixa Marconi and to a supplemental pension benefit (Marconi Complementary Fund). In addition, PT Comunicações contributes to Fundo de Melhoria Marconi with 1.55% of salaries paid to these employees, which is responsible to pay the additional pension supplement.

e) On retirement, PT Comunicações pays a lump sum gratuity of a fixed amount which depends on the length of service completed by the employee. Employees hired by PT Comunicações or any of its predecessor companies after the dates indicated above are not entitled to these benefits, as they are covered by the general Portuguese Government social security system.

PT SI employees who were transferred from PT Comunicações and Marconi and were covered by any of the pension plans described above maintain the right to such benefits.

The actuarial valuations for these plans, as at 31 December 2007 and 2006, were computed based on the projected unit credit method and considered the following actuarial assumptions and rates:

| | 2007 | 2006 |
|---|---------------|-------|
| Rate of return on long-term fund assets | 6.00% | 6.00% |
| Pensions liabilities discount rate | 5.25% | 4.75% |
| Salaries liabilities discount rate | 4.75% | 4.25% |
| Salary growth rate | 2.00% | 2.25% |
| Pension growth rate | Linked to GDP | |
| | Growth | 1.75% |
| Inflation rate | 2.00% | 1.75% |

The discount rate for pension liabilities was computed based on long-term yield rates of high-rating bonds as of the balance sheet date for maturities comparable to those liabilities.

The rate of return on long-term fund assets was estimated based on historical information on the return of portfolio assets, the expected portfolio in future years (defined in accordance with the expected maturity of the liabilities) and certain financial market performance indicators usually considered in market analysis.

Salary growth rate was established in accordance with PT Comunicações policy for wages and salaries.

The demographic assumptions considered as at 31 December 2007 and 2006 were as follows:

Mortality table:

| | |
|--------------------------------------|-------------------|
| Employees (while in active service): | |
| Males | AM (92) |
| Females | AF (92) |
| Pensioners: | |
| Males | PA (90)m adjusted |
| Females | PA (90)f adjusted |

Disability table: Swiss Reinsurance Company

Turnover of employees: Nil

Demographic assumptions considered by Portugal Telecom are based on mortality tables generally accepted for actuarial valuation purposes, with these tables being periodically adjusted to reflect the mortality experience occurred in the closed universe of the plan participants.

During 2007, benefits granted under pension plans were amended or settled as follows:

- a) Dec-Law 187/2007 and Law 52/2007 introduced certain changes to pension formulas in order to guarantee the long-term financial sustainability of the Portuguese social security system. These changes are also applied to some of PT Comunicações plans, which led to a reduction in the total pension liability.
- b) PT Comunicações, based on advice of legal counsel, introduced additional changes to pension supplement plans, namely the reduction of the supplement annual growth rate.
- c) PT Comunicações, based on advice of legal counsel, cancelled contributions to Fundo Melhoria Marconi that were being made above the 1.55% mandatory contribution. Following this decision, this plan was no longer treated for accounting purposes as a defined benefits plan and the related accrued liability as at 31 December 2007, amounting to Euro 12,841,000 (Note 9.5), was derecognized.
- d) The pension plan of DCSI was settled, following the liquidation of this company on December 2007, and Euro 362,721 was paid to the beneficiaries and the excess accrued liability as at the settlement date of Euro 329,178 was recognized as a gain under the caption Curtailment costs, net (Note 9.5).

The impact of the above mentioned changes to benefits, reduced Portugal Telecom's pension liability by Euro 134,863,178 from which (a) Euro 110,336,000 recognized as a prior year service gain, since it was related to vested rights, (b) Euro 11,357,000 related to unvested rights and therefore were deferred up to the retirement date (Note 3.h) and (c) Euro 12,841,000 and Euro 329,178 related to the settlement of the Fundo de Melhoria and DCSI Plans, respectively, which were recognized as curtailment gains.

Based on the actuarial studies, the benefit obligation and the fair value of the pension funds as at 31 December 2007 and 2006 were as follows:

| | 2007 | 2006 |
|---|----------------------|----------------------|
| Projected benefit obligation: | | |
| Pension, pension supplements and gratuities | 2,762,077,000 | 3,073,825,333 |
| Salaries to pre-retired and suspended employees | 985,739,338 | 997,670,254 |
| | 3,747,816,338 | 4,071,495,587 |
| Pension funds assets at fair value | (2,316,814,232) | (2,263,925,000) |
| Unfunded pension obligations | 1,431,002,106 | 1,807,570,587 |
| Prior years' service gains (i) | 9,660,000 | |
| Present value of unfunded pension obligations (Note 9.3) | 1,440,662,106 | 1,807,570,587 |

(i) This caption refers to the component of the prior years' service gain resulting from the changes in the benefits granted under pension plans introduced during 2007, related to unvested rights. This amount will be recognized in earnings during the estimated period in which those benefits will be earned by employees (15 years).

As at 31 December 2007 and 2006, the portfolio of pension funds was as follows:

| | 2007 | | 2006 | |
|--|----------------------|---------------|----------------------|---------------|
| | Amount | % | Amount | % |
| Equities (i) | 1,132,131,173 | 48.9% | 1,024,536,020 | 45.3% |
| Bonds | 744,044,644 | 32.1% | 726,262,119 | 32.1% |
| Property (ii) | 176,727,406 | 7.6% | 264,172,280 | 11.7% |
| Cash, treasury bills, short-term stocks and other current assets | 263,911,009 | 11.4% | 248,954,581 | 11.0% |
| | 2,316,814,232 | 100.0% | 2,263,925,000 | 100.0% |

(i) As at 31 December 2007 and 2006, this caption included investments in Portugal Telecom's shares and in shares of related parties, as follows:

| | 2007 | | 2006 | |
|----------------------|------------------|--------------------|------------------|--------------------|
| | Number of shares | Amount | Number of shares | Amount |
| Banco Espírito Santo | 3,107,904 | 196,618,560 | 13,107,904 | 178,529,652 |
| Telefónica | 8,928,305 | 198,386,937 | 8,928,305 | 143,924,277 |
| Portugal Telecom | 3,887,262 | 34,713,250 | 3,887,262 | 38,250,658 |
| | | 429,718,747 | | 360,704,587 |

(ii) As at 31 December 2007, this caption included certain properties that have been rented to PT Group companies, which represented approximately 95% of the value of property investments held by the funds. In addition, during 2007, a building was disposed of at market value to a property investment fund held by a related party.

Portugal Telecom is exposed to risks related to the changes in the fair value of the plan assets associated with Portugal Telecom's post retirement defined benefit plans. The main purpose of the established investment policy is capital preservation through five main principles:

(1) diversification; (2) stable strategic asset allocation and

disciplined rebalancing; (3) lower exposure to currency fluctuations; (4) specialized instruments for each class of assets; and (5) cost control.

During the years 2007 and 2006, the movement in the plan assets was as follows:

| | 2007 | 2006 |
|--|----------------------|----------------------|
| Opening balance of the plan assets | 2,263,925,000 | 2,200,172,000 |
| Actual return on assets | 79,991,229 | 158,277,996 |
| Payments of benefits | (165,557,000) | (163,959,000) |
| Contributions made by the Company (Note 9.4) | 155,231,003 | 59,844,004 |
| Participants contributions | 9,665,000 | 9,590,000 |
| Asset settlement (i) | (26,441,000) | |
| Closing balance of the plan assets | 2,316,814,232 | 2,263,925,000 |

(i) This amount corresponds to the market value of the Fundo Melhoria Marconi, which was settled following the decision of PT Comunicações of not make contributions above the mandatory 1.55% contribution.

A summary of the components of the net periodic pension cost recorded in 2007 and 2006 is presented below:

| | 2007 | 2006 |
|---|---------------------|--------------------|
| Service cost | 15,147,000 | 21,793,000 |
| Interest cost | 185,913,899 | 176,964,706 |
| Expected return on plan assets | (141,491,000) | (130,803,000) |
| Prior years service gains | (111,285,000) | (23,301,000) |
| Sub total (Note 9.5) | (51,715,101) | 44,653,706 |
| Work force reduction program (Note 9.3) (i) | 280,163,727 | 197,304,200 |
| Settlement of Fundo Melhoria Marconi (Note 9.5) | (12,841,000) | |
| Settlement of DCSI Plan (Note 9.3) | (329,178) | |
| Pension cost | 215,278,448 | 241,957,906 |

(i) This amount includes Euro 7,863,478 (Note 20) related to the pre-retirement of employees under the spin-off process which was recorded under the caption Discontinued operations, while the remaining amount of Euro 272,300,249 (Note 9.5) was recorded under the caption Curtailment costs, net.

Actuarial gains and losses resulting essentially from changes in actuarial assumptions or differences between those actuarial assumptions and actual data, are recognised directly in shareholders equity. During the years 2007 and 2006, the movement in accumulated net actuarial losses was as follows:

| | 2007 | 2006 |
|--|----------------------|----------------------|
| Opening balance (Note 41.6) | 1,404,159,583 | 1,653,137,579 |
| Change in actuarial assumptions (Note 9.6) | (132,842,395) | (208,250,000) |

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| | | |
|---|----------------------|----------------------|
| Differences between actual data and actuarial assumptions (Note 9.6): | | |
| Pension benefit obligation related | (180,390,281) | (13,253,000) |
| Asset related | 61,499,771 | (27,474,996) |
| Closing balance (Note 41.6) | 1,152,426,678 | 1,404,159,583 |

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During the year 2007, the change in actuarial assumptions corresponds to the net effect of: (i) the increase in the discount rate from 4.75% to 5.25% for pension liabilities and from 4.25% to 4.75% for salary liabilities, reflecting the evolution of market yields; (ii) the reduction in the salary growth rate from 2.25% to 2.00%; and (iii) the increase in the inflation rate from 1.75% to 2.00%. During 2006, the change in actuarial assumptions corresponds to the net effect of: (i) the increase in the discount rate from 4.5% to 4.75% for pension liabilities and from 3.5% to 4.25% for salary liabilities; (ii) the reduction in the salary growth rate from 3.0% to 2.25%; (iii) the reduction in the pension growth rate and inflation rate from 2.0% to 1.75%; and (iv) the adjustment in mortality tables (PA (90), from less three years to less four years).

Differences between actual data and actuarial assumptions related to the PBO, results mainly from the early retirement age for pre-retired employees being earlier than expected and from salaries and pension increases being lower than the assumptions used.

9.2. Health care benefits

As referred to in Note 3.i, PT Comunicações is responsible for the payment of post retirement health care benefits to certain active employees, suspended employees, pre-retired employees, retired employees and their eligible relatives. Health care services are rendered by PT-ACS, which was incorporated with the only purpose of managing the Company's Health Care Plan.

This plan sponsored by PT Comunicações includes all employees hired by PT Comunicações until 31 December 2003 and by Marconi until 1 February 1998. Certain employees of PT SI who were transferred from PT Comunicações are also covered by this health care plan.

The financing of the Health Care Plan is assured by defined contributions made by participants to PT-ACS and the remainder by PT Comunicações, which incorporated an autonomous fund in 2004 for this purpose.

The health care plan of DCSI was settled during the year 2007 following the liquidation of this company, and an amount of Euro 434,172 was paid to the beneficiaries. The remaining accrued liability amounting to Euro 677,785 was recognized as a gain under the caption Curtailment costs, net (Note 9.5).

In the second half of 2006, PT Comunicações made some changes to the Health Care Plan in order to maintain its long-term sustainability and financing. These changes included mainly a reduction in the amount that PT Comunicações pays for each medical act and an increase in participants' contributions (from 1.7% of salary in 2007 until 2.1% of salary in 2009), with these effects leading to a reduction in health care benefit obligations at the end of 2006 and to a reduction in future service costs.

In addition, in December 2006 PT Comunicações and SNS agreed to terminate the Protocol entered into in 2004 related to the Health Care Plan. In connection with this Protocol, SNS paid to PT Comunicações an annual amount per participant, and PT Comunicações paid the health care expenses incurred by its participants in SNS's hospitals network. Historically, this Protocol presented a deficit situation for PT Comunicações, with this trend being included in the unfunded health care benefit obligations.

The actuarial valuations for these plans, as at 31 December 2007 and 2006, were computed based on the projected unit credit method and considered the following actuarial assumptions and rates:

| | 2007 | 2006 |
|---|-------|-------|
| Rate of return on long-term fund assets | 6.00% | 6.00% |
| Health care liabilities' discount rate | 5.25% | 4.75% |
| Health care cost trend rate: | | |
| Next two years | 3.50% | 3.50% |
| Years thereafter | 3.00% | 2.75% |
| Salary growth rate | 2.00% | 2.25% |
| Inflation rate | 2.00% | 1.75% |

The discount rate for health care liabilities was computed based on long-term yield rates of high-rating bonds as of the balance sheet date for maturities comparable to those liabilities.

The rate of return on long-term fund assets was estimated based on historical information on the return of portfolio assets, the expected portfolio in future years (defined in accordance with the expected maturity of the liabilities) and certain financial market performance indicators usually considered in market analysis.

Health care cost trend rate was estimated based on specific indicators for this sector and historical information, with the long-term rate being computed also based on the inflation rate.

The demographic assumptions considered as at 31 December 2007 and 2006 were as follows:

Mortality table:

| | |
|--------------------------------------|-------------------|
| Employees (while in active service): | |
| Males | AM (92) |
| Females | AF (92) |
| Pensioners: | |
| Males | PA (90)m adjusted |
| Females | PA (90)f adjusted |

Disability table: Swiss Reinsurance Company

Turnover of employees: Nil

Demographic assumptions considered by Portugal Telecom are based on mortality tables generally accepted for actuarial valuation purposes, with these tables being periodically adjusted to reflect the mortality experience occurred in the closed universe of the plan participants.

Based on the actuarial studies, the benefit obligation and the fair value of health care funds and prior years' service gains not yet recognized as at 31 December 2007 and 2006 are as follows:

| | 2007 | 2006 |
|---|----------------------|----------------------|
| Accumulated health care benefit obligation | 455,308,816 | 491,102,185 |
| Plan assets at fair value | (582,330,282) | (644,224,704) |
| Excessive funding of pension obligations | (127,021,466) | (153,122,519) |
| Prior years' service gains (i) | 16,231,000 | 19,062,000 |
| Present value of excessive funding of pension obligations (Note 9.3) | (110,790,466) | (134,060,519) |

(i) This caption refers to the component of the prior years' service gain resulting from the changes in the health care plan occurred in 2006 related to those benefits that are not yet vested. This amount will be recognized in earnings during the estimated period in which those benefits will be earned by employees (18 years).

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As at 31 December 2007 and 2006, the portfolio of the Company's autonomous fund to cover post retirement health care benefit obligations was as follows:

| | 2007 | | 2006 | |
|--|--------------------|---------------|--------------------|---------------|
| | Amount | % | Amount | % |
| Equities | 246,927,446 | 42.4% | 289,205,401 | 44.9% |
| Bonds | 246,542,590 | 42.3% | 260,860,332 | 40.5% |
| Cash, treasury bills, short-term stocks and other current assets | 88,860,246 | 15.3% | 94,158,971 | 14.6% |
| | 582,330,282 | 100.0% | 644,224,704 | 100.0% |

During the years 2007 and 2006, the movement in the plan assets was as follows:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Opening balance of the plan assets | 644,224,704 | 315,576,000 |
| Actual return on assets | 24,783,000 | 26,320,417 |
| Refund of expenses paid on account by PT Comunicações (Note 9.4) | (86,677,422) | |
| Contributions made by PT Comunicações | | 302,328,287 |
| Closing balance of the plan assets | 582,330,282 | 644,224,704 |

A summary of the components of the net periodic post retirement health care cost in 2007 and 2006 is presented below:

| | 2007 | 2006 |
|--|---------------------|----------------------|
| Service cost | 2,608,000 | 6,868,000 |
| Interest cost | 22,998,957 | 40,554,000 |
| Expected return on plan assets | (37,940,000) | (36,935,000) |
| Prior years' service gains | (1,028,000) | (127,255,684) |
| Sub total (Note 9.5) | (13,361,043) | (116,768,684) |
| Work force reduction program costs (Note 9.5) | 9,653,813 | 11,609,762 |
| Settlement of DCSI Plan (Note 9.3) | (677,785) | |
| Termination of SNS Protocol (Notes 7.a) and 9.5) | | (220,417,000) |
| | (4,385,015) | (325,575,922) |

Actuarial gains and losses, resulting essentially from changes in actuarial assumptions or differences between those actuarial assumptions and actual data, are computed periodically by the actuary and are recognised directly in shareholders' equity. During the years 2007 and 2006, the movements in accumulated net actuarial losses were as follows:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Opening balance (Note 41.6) | 246,438,253 | 316,875,470 |
| Change in actuarial assumptions (Note 9.6) | (18,105,160) | (14,078,000) |
| Differences between actual data and actuarial assumptions (Note 9.6): | | |
| Health care benefit obligation related | (28,556,000) | (66,973,800) |
| Assets related | 13,157,000 | 10,614,583 |
| Closing balance (Note 41.6) | 212,934,093 | 246,438,253 |

During the year 2007, the change in actuarial assumptions corresponds to the effect of: (i) the increase in the discount rate from 4.75% to 5.25%; (ii) the increase in the long-term health care cost trend rate from 2.75% to 3.00%; (iii) the reduction in the salary growth rate from 2.25% to 2.00%; and (iv) the increase in the inflation rate from 1.75% to 2.00%. During the year 2006, the change in actuarial assumptions corresponds to the net effect of: (i) the increase in the discount rate from 4.5% to 4.75%; (ii) the reduction in the long-term health care cost trend rate from 3% to 2.75%; (iii) the reduction in the salary growth rate from 3.0% to 2.25%; and (iv) the adjustments in mortality tables (PA (90), from less three years to less four years).

Differences between actual data and actuarial assumptions related to the PBO results mainly from lower health care expenses than expected.

9.3. Responsibilities for post retirement benefits

The movements occurred in the responsibilities for post retirement benefits during the years ended 31 December 2007 and 2006 were as follows:

| | Pension benefits (Nota 9.1) | Health care benefits (Nota 9.2) | Total |
|--|-----------------------------------|---------------------------------------|----------------------|
| Balance as at 31 December 2005 | 2,038,652,313 | 597,231,431 | 2,635,883,744 |
| Changes in consolidation perimeter (i) | 1,270,982 | 1,241,684 | 2,512,666 |
| Net periodic pension cost/(gain) | 44,653,706 | (116,768,684) | (72,114,978) |
| Work force reduction program costs (Note 9.1) | 197,304,200 | 11,609,762 | 208,913,962 |
| Termination of Protocol with SNS (Note 9.5) | | (220,417,000) | (220,417,000) |
| Payments and contributions | (225,332,618) | (336,520,495) | (561,853,113) |
| Net actuarial gains | (248,977,996) | (70,437,217) | (319,415,213) |
| Balance as at 31 December 2006 | 1,807,570,587 | (134,060,519) | 1,673,510,068 |
| Net periodic pension cost/(gain) (Note 9.5) | (51,715,101) | (13,361,043) | (65,076,144) |
| Work force reduction program costs (Note 9.1) | 280,163,727 | 9,653,813 | 289,817,540 |
| Settlement of the Plan Melhoria Marconi (Note 9.5) | (12,841,000) | | (12,841,000) |
| Settlement of the DCSI Plan (Notes 9.1, 9.2 and 9.5) | (329,178) | (677,785) | (1,006,963) |
| Payments, contributions and refunds (Note 9.4) | (330,454,024) | 61,159,228 | (269,294,796) |
| Net actuarial losses (Note 9.6) | (251,732,905) | (33,504,160) | (285,237,065) |
| Balance as at 31 December 2007 | 1,440,662,106 | (110,790,466) | 1,329,871,640 |

(i) In 2006, this caption relates to the accrued post retirement liability of DCSI, a company acquired during 2006.

Certain post retirement benefit plans have a surplus position, therefore according to IAS 19 they should be presented in the balance sheet separately from those plans with a deficit position. As at 31 December 2007 and 2006, net post retirement obligations were recognized in the balance sheet as follows:

| | 2007 | 2006 |
|---------------------------------------|----------------------|----------------------|
| Plans with a deficit position: | | |
| Pensions | 1,463,019,423 | 1,807,570,587 |
| Healthcare | 912,816 | |
| | 1,463,932,239 | 1,807,570,587 |
| Plans with a surplus position: | | |
| Pensions | (22,357,317) | |
| Healthcare | (111,703,282) | (134,060,519) |
| | (134,060,599) | (134,060,519) |
| | 1,329,871,640 | 1,673,510,068 |

The impact of an increase or decrease by 25 bp on the discount rate actuarial assumption would be a decrease or increase of the responsibilities for post retirement benefits by approximately Euro 110 million.

9.4. Cash flow relating to post retirement benefit plans

During the years 2007 and 2006, the payments and contributions regarding post retirement benefits were as follows:

| | 2007 | 2006 |
|--|---------------------|--------------------|
| Pension benefits | | |
| Contributions to the funds (Note 9.1) | 155,231,003 | 59,844,004 |
| Payments of salaries to pre-retired and suspended employees | 174,860,300 | 165,488,614 |
| Settlement of DCSI plan (Note 9.1) | 362,721 | |
| Sub total (Note 9.3) | 330,454,024 | 225,332,618 |
| Health care benefits | | |
| Refund of expenses paid on account by PT Comunicações (Note 9.2) | (86,677,422) | |
| Payments to PT ACS | 25,084,022 | 34,192,208 |
| Settlement of DCSI plan (Note 9.2) | 434,172 | |
| Contributions to the fund | | 302,328,287 |
| Sub total (Note 9.3) | (61,159,228) | 336,520,495 |
| Termination payments | | |
| Related to continued operations (Note 9.5) | 7,513,072 | 18,936,785 |
| Related to discontinued operations (Note 20) | 7,351,702 | |
| Sub total | 14,864,774 | 18,936,785 |
| | 284,159,570 | 580,789,898 |

9.5. Post retirement benefit costs

In 2007 and 2006, post retirement benefit costs and net work force reduction program costs were as follows:

| | 2007 | 2006 |
|--|---------------------|---------------------|
| Post retirement benefits: | | |
| Pension benefits (Notes 9.1 and 9.3) | (51,715,101) | 44,653,706 |
| Health care benefits (Notes 9.2 and 9.3) | (13,361,043) | (116,768,684) |
| | (65,076,144) | (72,114,978) |
| Curtailment costs, net | | |
| Work force reduction program | | |
| Pensions (Note 9.1) | 272,300,249 | 197,304,200 |
| Health care (Notes 9.2 and 9.3) | 9,653,813 | 11,609,762 |
| Termination payments (Note 9.4) | 7,513,072 | 18,936,785 |
| Settlement of the Plan Melhoria Marconi (Note 9.1) | (12,841,000) | |
| Settlement of the DCSI Plan (Notes 9.1 and 9.2) | (1,006,963) | |
| Termination of Protocol with SNS (Notes 9.2 and 9.3) | | (220,417,000) |
| Provisions for SNS receivables (Notes 26 and 39) | | 11,528,257 |
| | 275,619,171 | 18,962,004 |

The impact of an increase (decrease) by 1% in the rate of return on long-term fund assets would have led to a decrease (increase) of post retirement benefit costs in the year 2007 by approximately Euro 29 million, related to the increase (decrease) in expected return on assets.

9.6. Net actuarial gains

In 2007 and 2006, the net actuarial gains recorded in the Statement of Recognised Income and Expenses were as follows:

| | 2007 | 2006 |
|--|----------------------|----------------------|
| Changes in actuarial assumptions | | |
| Pension benefits (Notes 9.1 and 9.3) | (132,842,395) | (208,250,000) |
| Health care benefits (Notes 9.2 and 9.3) | (18,105,160) | (14,078,000) |
| | (150,947,555) | (222,328,000) |
| Differences between actual data and actuarial assumptions | | |
| Pension benefits (Notes 9.1 and 9.3) | (118,890,510) | (40,727,996) |
| Health care benefits (Notes 9.2 and 9.3) | (15,399,000) | (56,359,217) |
| | (134,289,510) | (97,087,213) |
| | (285,237,065) | (319,415,213) |

10. Direct costs

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|-----------------------------------|--------------------|--------------------|
| Telecommunications costs (i) (ii) | 739,631,643 | 567,776,200 |
| Directories (Note 3.p) | 67,996,560 | 74,391,838 |
| Leasings of sites (ii) | 57,242,913 | 53,728,489 |
| Other | 42,426,060 | 28,973,926 |
| | 907,297,176 | 724,870,453 |

-
- (i) The increase in telecommunications costs is mainly related to the termination of the partial Bill & Keep interconnection regime in Brazil (Note 7.c).
- (ii) During 2007 and 2006, these captions include costs related to operating leases totaling Euro 118,205,439 and Euro 104,281,651, respectively (Note 13).

11. Costs of products sold

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Costs of products sold | 657,908,899 | 582,739,442 |
| Increases in adjustments for inventories (Note 39) | 197,841 | 1,159,694 |
| Reductions in adjustments for inventories (Note 39) | (1,957,157) | (3,279,638) |
| | 656,149,583 | 580,619,498 |

12. Supplies and external services

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Commissions | 264,249,979 | 264,528,146 |
| Specialized work | 185,584,524 | 167,679,709 |
| Maintenance and repairs | 155,687,210 | 155,587,635 |
| Electricity | 77,514,893 | 68,183,305 |
| Operating leases (Note 13) | 59,859,136 | 63,897,233 |
| Communications | 20,908,106 | 22,766,726 |
| Installation and removal of terminal equipment | 17,337,399 | 16,048,406 |
| Surveillance and security | 14,463,577 | 13,812,361 |
| Travelling | 12,211,052 | 13,596,095 |
| Fuel, water and other fluids | 11,537,585 | 11,662,325 |
| Office material | 11,098,444 | 11,098,878 |
| Transportation | 10,012,616 | 9,669,906 |
| Insurance | 9,493,951 | 10,275,439 |
| Cleaning expenses | 8,858,243 | 8,537,635 |
| Other | 86,799,912 | 91,167,511 |
| | 945,616,627 | 928,511,310 |

13. Operating leases

During 2007 and 2006, operating lease costs were recognised under the following captions:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Direct costs - capacity (Note 10) | 118,205,439 | 104,281,651 |
| Supplies and external services (Note 12) (i) | 59,859,136 | 63,897,233 |
| | 178,064,575 | 168,178,884 |

(i) This caption is mainly related to rentals of property and leases of transportation equipment.

As at 31 December 2007, the Company's obligations under operating lease contracts mature as follows:

| | |
|------|-------------|
| 2008 | 115,872,158 |
| 2009 | 64,231,075 |
| 2010 | 56,210,593 |
| 2011 | 46,504,832 |

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| | |
|---------------------------|--------------------|
| 2012 | 44,032,381 |
| 2013 and foillowing years | 127,457,190 |
| | 454,308,229 |

14. Indirect taxes

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|----------------------------|--------------------|--------------------|
| Spectrum fees (i) | 133,771,522 | 108,599,557 |
| Value added tax (ii) | 22,233,365 | 23,939,712 |
| Other indirect taxes (iii) | 45,820,217 | 43,371,668 |
| | 201,825,104 | 175,910,937 |

-
- (i) This caption includes primarily spectrum fees from Vivo and TMN, which in 2007 amounted to Euro 103 million and Euro 28 million, respectively, while in 2006 amounted to Euro 80 million and Euro 26 million, respectively.
- (ii) In 2006, this caption includes an amount of Euro 4,214,639 related to a reduction in provisions for accounts receivable, since the Company believes in the recoverability of the value added tax included in those balances (Note 39).
- (iii) This caption includes mainly indirect taxes from Vivo related to Fust (fund to improve the general access to telecommunications services) and Funtel (National Telecommunications Fund), as well as other municipal, federal and state taxes in Brazil.

15. Other costs, net

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|-----------|-------------------|--------------------|
| Donations | 4,346,148 | 3,855,978 |
| Tax fines | 1,715,807 | 1,303,811 |
| Other (i) | 39,009,981 | 110,240,206 |
| | 45,071,936 | 115,399,995 |

-
- (i) The decrease in this caption is primarily explained by the reduction in the expenses incurred by Portugal Telecom related to the tender offer launched by Sonae in 2006 from Euro 35 million in 2006 to Euro 7 million in 2007 (Note 7.d) and by the recognition in 2006 of an adjustment amounting to Euro 51 million (Notes 7.c and 34) to the value of certain CDMA equipments at Vivo.

16. Net interest expense

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Interest expense: | | |
| Related to loans obtained and financial instruments | 304,130,734 | 343,426,728 |
| Other | 7,142,405 | 7,416,137 |
| Interest income: | | |
| Related to cash and short-term investments and financial instruments | (96,019,309) | (102,905,642) |
| Other | (17,885,538) | (27,863,882) |
| | 197,368,292 | 220,073,341 |

17. Net gains on financial assets and other investments

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|----------------------|---------------------|
| Disposal of the 22% investment in Africatel (Note 7.d) (i) | (110,955,318) | |
| Derivatives financial instruments (ii) | (100,003,385) | (17,498,511) |
| Disposals of available for sale investments (Note 7.d) (iii) | (38,650,508) | |
| Real estate investments (iv) | (637,670) | (784,175) |
| Other, net | 1,463,874 | (51,077) |
| | (248,783,007) | (18,333,763) |

-
- (i) This caption is related to the disposal of a 22% stake in Africatel for an amount of Euro 116,999,817 (Note 44.d). This company includes all Portugal Telecom's investments in Sub-Saharan Africa except for Médi Télécom.
- (ii) In 2007, this caption includes net gains of Euro 67,815,191 related to changes in the fair value of derivative financial instruments classified as held for trading (Note 42.2) and a gain of Euro 32,188,194 (Notes 7.d, 41.3 and 44.f) related to the financial settlement of equity swaps. In 2006, this caption includes net losses of Euro 14,422,914 related to changes in the fair value of derivative financial instruments classified as held for trading (Note 42.2), a gain of Euro 23,513,275 related to the financial settlement of equity swaps (Note 44.f) and a gain of Euro 8,408,150 related to dividends obtained by PT on the equity swap over PT Multimedia's shares.
- (iii) In 2007, this caption includes the gains obtained with the disposals of the investments in Banco Espírito Santo and Telefónica amounting to Euro 35,698,600 (Notes 19 and 32) and Euro 2,951,908 (Note 32), respectively.
- (iv) This caption includes gains related to rents received from real estate rented to third parties, net of the amortization of these assets (Note 32).

18. Net other financial expenses

During 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|-------------------------------|-------------------|-------------------|
| Bank commissions and expenses | 34,009,849 | 29,099,186 |
| Other | 14,306,585 | 22,679,560 |
| | 48,316,434 | 51,778,746 |

19. Income taxes

From 1 January 2007, Portugal Telecom and its subsidiaries located in Portugal are subject to Corporate Income Tax (IRC) at a rate of 25%, which is increased up to a maximum of 1.5% of collectible profit through a municipal tax, leading to an aggregate tax rate of approximately 26.5%. In 2006, the Corporate Income Tax was increased up to 10%, leading to an aggregate tax rate of approximately 27.5%. In calculating taxable income, to which the above tax rate is applied, non-tax-deductible amounts are added to or subtracted from book entries. These differences between book and taxable entries can be temporary or permanent.

Portugal Telecom adopted the tax consolidation regime for groups of companies, which apply to all companies in which they hold at least 90% of the capital stock and that comply with Article 63 of the Portuguese Corporate Income Tax Law.

In accordance with Portuguese tax legislation, income tax returns are subject to review and adjustment by the tax authorities during the period of four calendar years (five years for social security, and ten years for the contributions made with respect to the years before 2001), except when there are tax losses, tax benefits were granted, or when tax inspections, claims or appeals are in progress, in which case the time periods are extended or suspended. The Board of Directors of Portugal Telecom, based on information from its tax advisors, believes that any adjustment which may result from such reviews or adjustments, as well as other tax contingencies, would not have a material impact on the consolidated financial statements as at 31 December 2007, except for the situations where provisions have been recognised (Note 39).

a) Deferred taxes

During 2007 and 2006, the movements in deferred tax assets and liabilities were as follows:

| | Balance | Changes in the consolidation | Net income | Accumulated | Foreign currency translation | Balance |
|---|----------------------|------------------------------------|---------------------|---------------------|------------------------------------|------------------|
| | 31 Dec 2006 | perimeter (i) | (ii) | earnings | adjustments | Other |
| Deferred tax assets | | | | | | |
| Accrued post-retirement liability | 443,480,168 | | (15,476,360) | (75,588,720) | | 897 |
| Tax losses carryforward (iii) | 272,545,978 | (73,229,713) | (866,883) | | 16,520,489 | |
| Provisions and adjustments | 112,663,562 | (14,931,534) | (23,874,175) | | 4,063,172 | (80,178) |
| Additional contribution to pension funds | 203,542,091 | | (8,927,983) | | | |
| Financial instruments | 13,224,000 | | 1,065,143 | | (92,486) | (43,671) |
| Other | 121,551,355 | (956,783) | 7,896,775 | | 9,161,811 | 1,233,402 |
| | 1,167,007,154 | (89,118,030) | (40,183,483) | (75,588,720) | 29,652,986 | 1,110,450 |
| Deferred tax liabilities | | | | | | |
| Gains on disposals of investments | 3,176,409 | (29,169) | 659,747 | | | 29,170 |
| Revaluation of fixed assets | 14,342,405 | (29,170) | (1,360,805) | | | (508) |
| Financial instruments and investments available for sale | 11,660,352 | | (4,310,612) | (7,306,068) | | (43,672) |
| Other | 61,198,651 | | 8,485,140 | | (1,591,730) | |
| | 90,377,817 | (58,339) | 3,473,470 | (7,306,068) | (1,591,730) | (15,010) |
| | | (89,059,691) | (43,656,953) | (68,282,652) | 31,244,716 | 1,125,460 |

- (i) Changes in the consolidation perimeter are primarily related to deferred tax assets and liabilities from PT Multimedia (Note 1).
- (ii) The movements in deferred tax assets and liabilities recorded through net income include the recognition of a deferred tax asset of Euro 910,608 (Note 20) related to the tax effect of costs of Euro 3,436,257 related to the spin-off of PT Multimedia that have not yet been considered for corporate tax purposes.
- (iii) As at 31 December 2007, this caption includes the deferred tax assets related to tax losses carryforward recognised by Vivo. Such tax losses from Vivo, amounting to Euro 632 million, have no maturity but can only be used up to a limit of 30% of tax gains for each period.

| | Balance 31 Dec 2005 | Changes in the | | Accumulated earnings | Foreign currency translation adjustments | Taxes payable (Note 28) | Change in tax rate (i) | | | Balance 31 Dec 2006 |
|--|------------------------|----------------------------|----------------------|-------------------------|---|-------------------------------|------------------------|-------------------------|------------------|------------------------|
| | | consolidation perimeter | Net income (i) | | | | Net income | Accumulated earnings | Other | |
| Deferred tax assets | | | | | | | | | | |
| Accrued post-retirement liability | 720,255,233 | 690,983 | (176,539,877) | (84,191,070) | | | (234,254) | (16,500,847) | | 443,480,168 |
| Tax losses carryforward (ii) | 286,876,872 | | 135,657,268 | | (5,537,361) | (137,127,830) | (7,322,971) | | | 272,545,978 |
| Provisions and adjustments | 133,288,748 | | (17,089,026) | | (1,203,761) | | (2,408,020) | | 75,621 | 112,663,562 |
| Additional contribution to pension funds | 139,990,269 | | 71,232,656 | | | | (7,680,834) | | | 203,542,091 |
| Financial instruments | 18,477,273 | | 1,188,042 | (6,999,804) | 39,344 | | (536,861) | | 1,056,006 | 13,224,000 |
| Other | 88,922,614 | | 36,064,997 | | (2,807,165) | | (513,536) | | (115,555) | 121,551,355 |
| | 1,387,811,009 | 690,983 | 50,514,060 | (91,190,874) | (9,508,943) | (137,127,830) | (18,696,476) | (16,500,847) | 1,016,072 | 1,167,007,154 |
| Deferred tax liabilities | | | | | | | | | | |
| Gains on disposals of investments (iii) | 271,627,295 | | (268,331,022) | | | | (119,864) | | | 3,176,409 |
| Revaluation of fixed assets | 16,530,675 | | (1,658,776) | | | | (541,223) | | 11,729 | 14,342,405 |
| Financial instruments | 12,418,218 | | (6,867,410) | 5,493,551 | | | (170,483) | (269,530) | 1,056,006 | 11,660,352 |
| Other | 34,290,889 | 17,275,441 | 9,993,600 | | 1,153,834 | | (1,613,939) | | 98,826 | 61,198,651 |
| | 334,867,077 | 17,275,441 | (266,863,608) | 5,493,551 | 1,153,834 | | (2,445,509) | (269,530) | 1,166,561 | 90,377,817 |
| | | (16,584,458) | 317,377,668 | (96,684,425) | (10,662,777) | (137,127,830) | (16,250,967) | (16,231,317) | (150,489) | |

- (i) In 2006, deferred taxes recorded through net income include a cost of Euro 12,686,904 (Note 20) which was reclassified under the caption "Discontinued operations", as it is related to PT Multimedia.
- (ii) During the year 2006, Vivo recorded deferred tax assets related to tax losses from previous periods amounting to Euro 134 million (Note 7.c).
- (iii) The reduction in this caption is related to the adoption by the Company of the voluntary taxation regime for certain gains obtained in the disposition of investments in prior periods. As a result, the amount excluded from taxation by this regime, of Euro 141,972,529, was recorded as a gain in the income statement in 2006, as mentioned below in the reconciliation of the provision for income taxes.

As at 31 December 2007 and 2006, total deferred tax assets include Euro 394 million and Euro 355 million from foreign countries, respectively, and total deferred liabilities include Euro 19 million and Euro 18 million from foreign countries. These deferred tax assets and liabilities from foreign countries are mainly related to Vivo.

b) Reconciliation of income tax provision

During 2007 and 2006, the reconciliation between the nominal and effective income tax for the period is as follows:

| | 2007 | 2006 |
|---|--------------------|---------------------|
| Income before taxes | 1,032,510,703 | 858,631,363 |
| Statutory tax rate | 26.5% | 27.5% |
| | 273,615,336 | 236,123,625 |
| Permanent differences (i) | (43,509,350) | 11,803,881 |
| Adjustments to the provision for income taxes of the previous year (Note 28) | (9,993,868) | (6,380,082) |
| Difference in tax rates | 5,380,340 | (8,419,634) |
| Increases and reductions in provisions for income tax contingencies (Notes 28 and 39) | 8,808,391 | 8,545,381 |
| Reversal of deferred tax liabilities related to the taxation of 50% of the gains obtained in the disposal of certain financial investments (Note 7.d) | | (141,972,529) |
| Tax losses from previous periods (Note 7.c) | | (134,470,029) |
| Valuation allowance for certain tax losses carryforward (ii) | | 54,723,658 |
| Liquidation of a subsidiary (Note 7.d) | | (53,342,681) |
| Change in statutory tax rate in Portugal (iii) | | 8,329,536 |
| Other | 8,976,816 | 3,694,503 |
| | 243,277,665 | (21,364,371) |
| Income tax | | |
| Income tax-current (Note 28) | 198,710,104 | 292,449,234 |
| Deferred taxes (iv) | 44,567,561 | (313,813,605) |
| | 243,277,665 | (21,364,371) |

- (i) In 2007, this caption includes primarily Euro 29,403,159 and Euro 9,460,129 resulting from the non-taxable gains amounting to Euro 110,955,318 and Euro 35,698,600 (Note 17) related to the disposals of the investments in Africatel and Banco Espírito Santo, respectively.
- (ii) In 2006, this caption relates mainly to tax losses from certain holding companies of Brasilcel, which did not expect to obtain taxable profits in the future that would allow for the recovery of these tax losses. Following the corporate restructuring completed at the end of 2006, Vivo is able to fully recover its tax losses generated in the period.
- (iii) This caption relates to the impact on deferred taxes of the change in the municipal tax to a maximum of 1.5% of collectable profit, as mentioned above.
- (iv) The change in this caption is mainly related to: (a) the reduction of deferred tax liabilities in 2006 by Euro 268 million, following the adoption of the voluntary capital gains taxation regime, as mentioned above; and (b) a gain of Euro 134 million (Note 7.c) recorded in 2006 related to the recognition of tax losses from previous periods at Vivo.

20. Discontinued operations

During the years 2007 and 2006 PT Multimédia was classified as a discontinued operation, following the approval at the Annual General Meeting of Portugal Telecom, held on 27 April 2007, of the spin-off of all ordinary shares of PT Multimedia held by Portugal Telecom to its shareholders.

Portugal Telecom concluded the spin-off on 7 November 2007 and the impact of this transaction on the Company's financial statements was to reduce shareholders' equity excluding minority interests by an amount of Euro 405,328,608 (Note 41), corresponding to the carrying value, as of the date of the spin-off, of the assets and liabilities attributable to the PT Multimédia business, net of minority interests.

Net income from discontinued operations includes the results of PT Multimédia in 2006 and in 2007 up to the conclusion of the spin-off and expenses incurred with the spin-off process, as follows:

| | 2007 | 2006 |
|--|-------------------|-------------------|
| Results of PT Multimédia | 63,150,775 | 74,132,079 |
| Expenses incurred with the spin-off (net of tax) (i) | (17,676,651) | |
| Net income from discontinued operations | 45,474,124 | 74,132,079 |

(i) Expenses incurred in 2007 with the spin-off amounted to Euro 24,049,866, and include primarily work force reduction costs of Euro 7,863,478 (Note 9.1), termination payments of Euro 7,351,702 (Note 9.4) and costs related to changes in the information systems. These costs were presented net of the related tax effect amounting to Euro 6,373,215, including Euro 5,462,607 (Note 28) and Euro 910,608 (Note 19) of current and deferred income tax, respectively.

The results of PT Multimedia in the ten-month period ended 31 October 2007 prior to the conclusion of the spin-off and in 2006 is presented below. Financial information relating to the PT Multimédia segment in 2006 was restated to be presented as a discontinued operation.

| | 2007 | 2006 |
|---|---------------------|---------------------|
| Revenues | 586,736,842 | 666,482,870 |
| Costs: | | |
| Wages and salaries | 34,837,316 | 39,975,868 |
| Direct costs | 182,533,032 | 203,037,771 |
| Commercial costs | 45,023,522 | 56,865,044 |
| Depreciation and amortization (i) | 91,154,879 | 102,502,152 |
| Other costs (ii) | 144,042,093 | 153,162,816 |
| Total costs | 497,590,842 | 555,543,651 |
| Income before financial results and taxes | 89,146,000 | 110,939,219 |
| Interest and other financial expenses, net | 3,324,038 | 7,755,451 |
| Income before income taxes | 85,821,962 | 103,183,768 |
| Provision for income taxes (iii) | (22,671,187) | (29,051,689) |
| Results from discontinued operations | 63,150,775 | 74,132,079 |

-
- (i) This caption includes the amortization related to contracts entered into with PT Comunicações for the acquisition of capacity on its fixed network, which in 2006 amounted to Euro 23,438,318 and were eliminated in Portugal Telecom's consolidation process.
- (ii) In 2006, this caption includes primarily increases and decreases in provisions amounting to Euro 16,456,669 and Euro 14,078,590 (Note 39), respectively. The increases are primarily related to doubtful receivables and the reductions are mainly related to the reduction of the provision for estimated costs from the disposal of Lusomundo Media amounting to Euro 8,017,195.
- (iii) In 2006, this caption includes deferred taxes amounting to Euro 12,686,904 (Note 19) and current income taxes amounting to Euro 16,364,785 (Note 28).

The assets and liabilities related to discontinued operations as at 31 October 2007 and 31 December 2006 are as follows:

| | 31 Oct 2007 | 31 Dec 2006 |
|---|----------------------|----------------------|
| Assets of PT Multimedia: | | |
| Current assets | 186,411,081 | 260,045,709 |
| Intangible assets | 250,184,460 | 283,615,597 |
| Tangible assets | 314,358,492 | 297,282,365 |
| Deferred taxes | 70,665,379 | 89,118,029 |
| Other non-current assets | 33,498,346 | 45,115,850 |
| | 855,117,758 | 975,177,550 |
| Goodwill on the acquisition of PT Multimedia shares | 176,647,949 | 176,647,949 |
| Total assets (Note 7.d) | 1,031,765,707 | 1,151,825,499 |
| Liabilities of PT Multimedia: | | |
| Current liabilities | 299,152,572 | 355,354,019 |
| Medium and long-term debt | 134,349,770 | 173,964,086 |
| Other non-current liabilities | 20,817,520 | 21,794,613 |
| Total liabilities (Note 7.d) | 454,319,862 | 551,112,718 |

The carrying value of net assets related to PT Multimédia amounting to Euro 577 million, as detailed above, net of the related minority interests amounting to Euro 172 million, was recorded as a reduction of accumulated earnings following completion of the spin-off on 7 November 2007.

The statement of cash flows of PT Multimedia in the ten-month period ended 31 October 2007 prior to the conclusion of the spin-off and in 2006 were as follows:

| | 2007 | 2006 |
|---|---------------------|----------------------|
| OPERATING ACTIVITIES | | |
| Collections from clients | 727,457,467 | 755,138,649 |
| Payments to suppliers | (462,184,646) | (486,697,923) |
| Payments to employees | (33,939,670) | (38,734,380) |
| Payments relating to income taxes | (2,656,318) | (2,689,546) |
| Payments relating to indirect taxes and other | (30,494,125) | (32,882,287) |
| Cash flow from operating activities | 198,182,708 | 194,134,513 |
| INVESTING ACTIVITIES | | |
| Cash receipts resulting from | | |
| Financial investments | 3,340,528 | 4,460,469 |
| Tangible fixed assets | 2,038,056 | 641,268 |
| Interest and related income | 605,125 | 1,990,730 |
| Dividends | 1,476,409 | 1,843,062 |
| Other investing activities | 2,163,792 | 358,909 |
| | 9,623,910 | 9,294,438 |
| Payments resulting from | | |
| Financial investments | (3,462) | (1,862,172) |
| Tangible and intangible assets | (89,240,828) | (115,925,107) |
| Other investing activities | (551) | (13,902,100) |
| | (89,244,841) | (131,689,379) |
| Cash flow from investing activities | (79,620,931) | (122,394,941) |
| FINANCING ACTIVITIES | | |
| Cash receipts resulting from | | |
| Loans obtained | 125,220,982 | 1,074,976 |
| Other financing activities | 333,367 | 2,714,960 |
| | 125,554,349 | 3,789,936 |
| Payments resulting from | | |
| Loans repaid | (59,595,173) | (8,459,559) |
| Lease rentals (principal) | (32,994,076) | (41,392,959) |
| Interest and related expenses | (12,058,846) | (10,146,171) |
| Dividends | (41,173,794) | (29,280,348) |
| | (145,821,889) | (89,279,037) |
| Cash flow from financing activities | (20,267,540) | (85,489,101) |

21. Minority interests

During 2007 and 2006, the movements in minority interests were as follows:

| | Balance 31 Dec 2006 | Changes in the consolidation perimeter | Acquisitions, disposals and share capital increases | Net income | Dividends | Currency translation adjustments | Other | Balance 31 Dec 2007 |
|--------------------------|------------------------|--|--|-------------------|---------------------|--|------------------|------------------------|
| Brasilcel (i) | 558,432,965 | | | 14,701,694 | | 46,746,710 | 340,075 | 620,221,444 |
| MTC (ii) | 62,619,712 | | | 22,908,611 | (12,165,875) | (4,902,355) | | 68,460,093 |
| Cabo Verde Telecom | 37,683,845 | | | 12,542,174 | (7,643,967) | | (48,190) | 42,533,862 |
| Timor Telecom | 4,137,046 | | | 2,502,878 | (907,885) | (507,805) | | 5,224,234 |
| LTM | 1,475,269 | | | 746,428 | (673,030) | 7,350 | 34,574 | 1,590,591 |
| CST | 1,564,571 | | | 367,266 | (62,603) | (293,574) | (62,604) | 1,513,056 |
| Kenya Postel Directories | 1,050,462 | | | 509,358 | (290,865) | (20,747) | 16,828 | 1,265,036 |
| Previsão | 1,094,263 | | (184,030) | 47,344 | (40,128) | | (134,782) | 782,667 |
| Africatel (iii) | | | 782,026 | 9,956,220 | (11,553,741) | (2,819,078) | 1,938,726 | (1,695,847) |
| PT Multimedia (iv) | 180,460,811 | (172,119,142) | | 29,143,593 | (41,219,625) | | 3,734,363 | |
| Other | 2,269,264 | 1,915,782 | | (578,140) | (73,867) | (453,982) | 614,098 | 3,693,155 |
| | 850,788,208 | (170,203,360) | 597,996 | 92,847,426 | (74,631,586) | 37,756,519 | 6,433,088 | 743,588,291 |

| | Balance 31 Dec 2005 | Changes in the consolidation perimeter | Acquisitions, disposals and share capital increases | Net income | Dividends | Currency translation adjustments | Other | Balance 31 Dec 2006 |
|--------------------------|------------------------|--|--|-------------------|---------------------|--|------------------|------------------------|
| Brasilcel (i) | 523,268,570 | | 15,716,672 | 33,531,568 | (1,561,159) | (14,431,325) | 1,908,639 | 558,432,965 |
| PT Multimedia (iv) | 178,075,607 | | | 28,669,799 | (35,335,177) | | (375,983) | 171,034,246 |
| MTC (ii) | | 65,971,316 | | 8,948,952 | (11,821,024) | (479,532) | | 62,619,712 |
| Cabo Verde Telecom | 33,668,323 | | | 10,156,904 | (6,137,449) | | (3,933) | 37,683,845 |
| Cabo TV Madeirense | 6,531,728 | | (594,619) | 2,094,571 | (1,766,999) | | | 6,264,681 |
| Timor Telecom | 3,327,479 | | | 1,212,737 | | (403,170) | | 4,137,046 |
| Cabo TV Açoreana | 2,251,967 | | | 731,849 | (705,868) | | | 2,277,948 |
| CST | 1,675,209 | | | 343,821 | (67,133) | (331,669) | (55,657) | 1,564,571 |
| LTM | 1,493,621 | | | 770,788 | (472,574) | (332,101) | 15,535 | 1,475,269 |
| Previsão | 1,109,089 | | | 59,498 | (27,584) | | (46,740) | 1,094,263 |
| Kenya Postel Directories | 1,015,137 | | | 339,976 | (230,945) | (73,706) | | 1,050,462 |
| Other | 1,269,346 | 1,649,981 | | 507,693 | (121,540) | (145,240) | (7,040) | 3,153,200 |
| | 753,686,076 | 67,621,297 | 15,122,053 | 87,368,156 | (58,247,452) | (16,196,743) | 1,434,821 | 850,788,208 |

- (i) The minority interests in Brasilcel correspond to 50% of the interests of minority shareholders of Brasilcel's subsidiaries in their corresponding amounts of equity and net income. The increases in minority interests in 2006, which are included in the column Acquisitions, disposals and share capital increases, are related to Vivo's corporate restructuring completed in February 2006. The reduction in the income applicable to minority interests in 2007, as compared to 2006, is primarily explained by the minority's share in the tax gain recognized by Vivo in 2006 amounting to Euro 134 million (Note 19) related to tax losses from previous periods.
- (ii) The investment in MTC was acquired in September 2006 (Note 2.b), and accordingly its results have been included in Portugal Telecom's consolidated results starting on that date, which primarily explains the increase in net income applicable to minority interests in 2007.
- (iii) In July 2007, Portugal Telecom sold a 22% stake in this investment, which aggregates all of Portugal Telecom's interests in Africa, except for Médi Télécom (Note 17).
- (iv) The minority interests in PT Multimedia correspond to the interests of minority shareholders in PT Multimedia's equity and net income, considering the application of the equity method of accounting. Following the completion of the spin-off of this business on 7 November 2007 (Note 1), PT Multimédia is no longer part of the Group.

22. Dividends

On 27 April 2007, the Annual General Meeting of Portugal Telecom approved the proposal of the Board of Directors to distribute a dividend of Euro 47.5 cents per share relating to year 2006. Accordingly, dividends amounting to Euro 516,506,816 (Notes 41 and 44.i) were paid in 2007.

On 21 April 2006, the Annual General Meeting of Portugal Telecom approved the proposal of the Board of Directors to distribute a dividend of Euro 47.5 cents per share relating to year 2005. Accordingly, dividends amounting to Euro 526,402,838 (Notes 41 and 44.i) were paid in 2006.

23. Earnings per share

Earnings per share for the years 2007 and 2006 were computed as follows:

| | | 2007 | 2006 |
|---|---------------|----------------------|----------------------|
| Income from continued operations, net of minority interests | (1) | 725,529,205 | 824,280,479 |
| Income from discontinued operations, net of minority interests | (2) | 16,330,531 | 42,479,178 |
| Net income attributable to equity holders of the parent | (3) | 741,859,736 | 866,759,657 |
| Financial costs related with exchangeable bonds (net of tax) | (4) | 9,239,015 | 5,272,196 |
| Net income considered in the computation of the diluted earnings per share | (5) | 751,098,751 | 872,031,853 |
| Weighted average common shares outstanding in the period | (6) | 1,050,740,503 | 1,108,740,884 |
| Effect of the exchangeable bonds | | 64,655,173 | 93,895,026 |
| | (7) | 1,115,395,676 | 1,202,635,910 |
| Earnings per share from continued operations, net of minority interests | | | |
| Basic | (1)/(6) | 0.69 | 0.74 |
| Diluted | [(1)+(4)]/(7) | 0.66 | 0.69 |
| Earnings per share from discontinued operations, net of minority interests | | | |
| Basic | (2)/(6) | 0.02 | 0.04 |
| Diluted | (2)/(7) | 0.01 | 0.04 |
| Earnings per share from total operations, net of minority interests | | | |
| Basic | (3)/(6) | 0.71 | 0.78 |
| Diluted | (5)/(7) | 0.67 | 0.73 |

In 2007, dilutive effects include the impact of the exchangeable bonds issued on August 2007, while in 2006 dilutive effects included the impact of these exchangeable bonds and those issued in 2001, which were repaid in December 2006.

24. Short-term investments

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|------------------------------|----------------------|----------------------|
| Bonds | 243,127,974 | 492,607,644 |
| Other short-term investments | 927,165,228 | 1,042,626,085 |
| | 1,170,293,202 | 1,535,233,729 |

The reduction in this caption is primarily related to the reduction during the year 2007 of the short-term commercial paper programs entered into by Portugal Telecom (Note 35).

Bonds are held by Portugal Telecom for short term periods. Acquisition and sale of these securities are executed under terms and conditions agreed in advance with financial intermediaries.

Short term investments have terms and conditions previously agreed with financial institutions.

25. Accounts receivable - trade

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|----------------------|----------------------|
| Current accounts receivable - trade: | | |
| Accounts receivable from customers | 1,428,941,709 | 1,410,621,902 |
| Unbilled revenues | 210,384,282 | 161,947,862 |
| | 1,639,325,991 | 1,572,569,764 |
| Adjustments for doubtful accounts receivable - trade (Note 39) | (331,896,220) | (390,657,352) |
| | 1,307,429,771 | 1,181,912,412 |

26. Accounts receivable - other

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Current accounts receivable - other | | |
| Receivables from related parties (i) | 19,360,241 | 52,582,086 |
| Contributions from SNS (ii) | 30,341,962 | 35,425,856 |
| Discounts given to retired Portuguese citizens (iii) | 21,719,037 | 17,985,959 |
| Trial deposits | 21,022,986 | 16,810,729 |
| Advances to suppliers (iv) | 19,089,604 | 67,351,747 |
| Unbilled interest | 4,414,697 | 7,314,030 |
| Other | 46,390,366 | 53,219,004 |
| | 162,338,893 | 250,689,411 |
| Adjustments for other current accounts receivable (Note 39) | (33,593,504) | (31,777,234) |
| | 128,745,389 | 218,912,177 |
| Other non-current accounts receivable | 6,641,582 | 17,415,215 |
| Adjustments for other non-current accounts receivable (Note 39) | (2,289,349) | (2,177,276) |
| | 4,352,233 | 15,237,939 |

(i) The reduction in this caption is primarily explained by the dividends received from Unitel in January 2007 related to its earnings of 2005 amounting to Euro 27 million (Note 44.e). Dividends from Unitel related to its earnings of 2006 amounting to Euro 46 million (Note 44.e) were paid in October 2007.

(ii) These contributions are related to the agreement with the SNS regarding the Health Care Plan, under which this entity was obliged to make a comparticipation per beneficiary of the plan. This agreement was terminated during 2006 under a restructuring of the Health Care Plan (Note 9.2). As a result of the termination of the Protocol with SNS (Note 9.2), PT Comunicações recorded an adjustment amounting to Euro 19,953,801 to cover certain recoverability risks of these

receivables. This amount includes Euro 11,528,257 (Note 9.5) related to receivables from contributions to retired participants, which was recorded as a deduction to the gain from the termination of the Protocol with SNS; the remaining amount of Euro 8,425,544 is related to receivables from contributions to active participants and was recorded as an expense under the caption Provisions and adjustments .

- (iii) This caption corresponds to discounts given to certain eligible retired Portuguese citizens, which were supposed to be reimbursed by the Portuguese State, under Decree Law 20 C/86, in accordance with the terms of the acquisition of the Basic Network at the end of 2002 and the related Modifying Agreement to the Concession Contract, which stated that this receivable balance should be paid directly by the Portuguese State, which committed to include the corresponding expense in the Annual State Budget. In 2007, the Portuguese State excluded this expense from the Annual State Budget, and no longer will reimburse PT Comunicações. As at 31 December 2007, the account receivable from the Portuguese State is related to the discounts granted during the year 2006, and since 1 January 2007 these discounts are fully paid by PT Comunicações with no right for reimbursement.
- (iv) As at 31 December 2006, this caption included Euro 43 million related to advances to content providers in the PT Multimedia business (audiovisuals business).

27. Inventories

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Merchandise (i) | 149,942,019 | 131,028,707 |
| Raw materials and consumables | 17,707,009 | 16,747,586 |
| Work in progress | 9,319,751 | 7,137,219 |
| | 176,968,779 | 154,913,512 |
| Adjustments for obsolete and slow-moving inventories (Note 39) | (16,376,372) | (24,632,948) |
| | 160,592,407 | 130,280,564 |

- (i) As at 31 December 2007, this caption includes mainly (1) mobile terminal equipments from Vivo and TMN, and (2) telephone and modems (internet access through ADSL) from the wireline business.

28. Taxes receivable and payable

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | | 2006 | |
|-----------------------------------|--------------------|--------------------|--------------------|--------------------|
| | Receivable | Payable | Receivable | Payable |
| Current taxes | | | | |
| Operations in Portugal | | | | |
| Value-added tax | 12,510,592 | 45,559,972 | 42,025,536 | 63,617,392 |
| Income taxes | 93,139,728 | 165,413,419 | 20,997,678 | 117,289,642 |
| Personnel income tax withholdings | | 7,917,086 | | 8,690,404 |
| Social Security Contributions | | 6,303,572 | | 8,291,722 |
| Other | 425,892 | 970,934 | 1,550,871 | 1,692,400 |
| | 106,076,212 | 226,164,983 | 64,574,085 | 199,581,560 |
| Taxes in foreign countries | 133,035,372 | 155,791,731 | 147,173,487 | 117,381,268 |
| | 239,111,584 | 381,956,714 | 211,747,572 | 316,962,828 |
| Non-current taxes | | | | |
| Taxes in foreign countries | 148,340,234 | 31,172,618 | 124,531,128 | 25,787,484 |

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As at 31 December 2007 and 2006, the caption Taxes in foreign countries relates basically to 50% of taxes receivable and payable by Brasilcel's subsidiaries, as follows:

| | 2007 | | 2006 | |
|---------------------------|--------------------|--------------------|--------------------|--------------------|
| | Receivable | Payable | Receivable | Payable |
| Current taxes: | | | | |
| Income taxes | 19,702,942 | 22,861,277 | 36,415,422 | 14,826,855 |
| Indirect taxes | 105,244,634 | 113,231,752 | 101,965,330 | 87,792,618 |
| Other | 8,087,796 | 19,698,702 | 8,792,735 | 14,761,795 |
| | 133,035,372 | 155,791,731 | 147,173,487 | 117,381,268 |
| Non-current taxes: | | | | |
| Income taxes (i) | 100,562,243 | 286,977 | 82,813,411 | |
| Indirect taxes (ii) | 47,777,991 | 30,885,641 | 41,717,717 | 25,787,484 |
| | 148,340,234 | 31,172,618 | 124,531,128 | 25,787,484 |

- (i) This caption is primarily related to withholding income taxes in connection with dividends received by the holding companies of Vivo, which are only recoverable after more than one year and only when these companies achieve taxable profits which allow them to recover those taxes.
- (ii) Taxes receivable included in this caption relate mainly to indirect taxes paid in the acquisition of real state property, which under Brazilian law are only recoverable over a period of 48 months. Taxes payable included in this caption mainly relate to ICMS assessed by the Brazilian State of Paraná payable in a period of 48 months in accordance with a special agreement with the local State Government.

As at 31 December 2007 and 2006, the net balance of the caption Income taxes from operations in Portugal is made up as follows:

| | 2007 | 2006 |
|--|---------------------|---------------------|
| Current income taxes of the operations in Portugal recorded in the balance sheet | (165,413,419) | (117,289,642) |
| Payments on account | 87,354,017 | 7,201,228 |
| Withholding income taxes, net | 4,301,431 | 3,951,609 |
| Income taxes receivable (i) | 1,484,280 | 9,844,841 |
| Net income tax payable from operations in Portugal | (72,273,691) | (96,291,964) |

- (i) As at 31 December 2006, this caption is primarily related to withholding income taxes from previous periods at Portugal Telecom that could only be recoverable when the Company started to pay income taxes after full utilization of its tax losses carriedforward, which occurred during the 2007, and therefore those withholding income taxes were recovered.

The reconciliation between current income taxes recorded in the Company's balance sheet as at 31 December 2007 and 2006 and current income tax expense for the periods then ended, is as follows:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Current income taxes of the operations in Portugal recorded in the balance sheet | 165,413,419 | 117,289,642 |
| Foreign current income taxes of international subsidiaries (i) | 42,927,250 | 45,631,371 |
| Excess provision for income taxes for the previous year (Note 19) | (9,993,868) | |
| Increases and decreases in provisions for income tax contingencies (Notes 19 and 39) | 8,808,391 | 8,545,381 |
| Tax losses carriedforward used in the year (Note 19) (ii) | | 137,127,830 |
| Other | 1,454,949 | 2,887,521 |
| | 208,610,141 | 311,481,745 |

-
- (i) The reduction in this caption is mainly related to Vivo, following Vivo's corporate restructuring at the end of 2006, which allows Vivo to offset losses from certain companies, with taxable profits from other companies.
- (ii) As at 31 December 2006, this caption is related to the utilization of tax losses carryforward by Portugal Telecom and PT Multimedia. As at 31 December 2007, PT Multimedia is no longer part of the Portugal Telecom Group, following the completion of its spin-off, while Portugal Telecom had already fully used its tax losses carriedforward by the end of 2006.

The current income tax expense was recorded in the following captions:

| | 2007 | 2006 |
|-------------------------------------|--------------------|--------------------|
| Profit and loss statement (Note 19) | 198,710,104 | 292,449,234 |
| Discontinued operations (Note 20) | 5,462,607 | 16,364,785 |
| Accumulated earnings | 4,437,430 | 2,667,726 |
| | 208,610,141 | 311,481,745 |

29. Prepaid expenses

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--------------------------|--------------------|--------------------|
| Marketing and publicity | 31,445,870 | 25,674,326 |
| Telephone directories | 30,341,615 | 35,231,362 |
| Sales of equipment (i) | 17,595,322 | 13,561,835 |
| Rentals | 7,257,690 | 7,752,817 |
| Maintenance and repairs | 2,442,023 | 1,898,802 |
| Interest paid in advance | 895,479 | 831,413 |
| Programming content (ii) | | 2,825,949 |
| Other | 16,548,816 | 33,938,245 |
| | 106,526,815 | 121,714,749 |

-
- (i) Sales of mobile phones at Vivo are recognized when the final client activates the equipment. Therefore the negative margin, as well as indirect taxes, are deferred and recognized up to the activation of the customer.
- (ii) These prepaid expenses were related to PT Multimedia, which as at 31 December 2007 is no longer part of the Portugal Telecom Group, following the conclusion of its spin-off in November 2007.

30. Other current and non-current assets

As at 31 December 2007 and 2006, these captions are made up as follows:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Other current assets | | |
| Accounts receivable from QTE transactions (Notes 3.1.ix) and 40) (i) | 35,324,314 | 46,332,009 |
| Other | 3,655,680 | 4,072,995 |
| | 38,979,994 | 50,405,004 |
| Other non-current assets | | |
| Accounts receivable from QTE transactions (Notes 3.1.ix) and 40) (i) | 470,140,303 | 627,430,804 |
| Fair value of equity swaps over PT Multimedia shares and of interest rate derivatives classified as cash flow hedges (Note 42.2) | | 21,033,234 |
| Other | 14,125,856 | 15,328,650 |
| | 484,266,159 | 663,792,688 |

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- (i) In December 2007, certain contracts related to QTE transactions were early terminated without any cost to Portugal Telecom, therefore Portugal Telecom has derecognized the assets and liabilities related to those contracts (Notes 3.1.ix) and 40).

31. Investments in group companies

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Investments in associated companies | 273,637,325 | 229,455,418 |
| Goodwill, net of impairment losses | 167,552,271 | 164,612,372 |
| Loans granted to associated companies and other companies | 95,194,241 | 102,018,169 |
| Investments in other companies | 1,678,417 | 3,012,320 |
| Advances for investments | 18,387 | |
| | 538,080,641 | 499,098,279 |

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As at 31 December 2007 and 2006, the caption Investments in associated companies consists of:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Unitel | 145,838,919 | 116,979,117 |
| Universo Online, Inc (UOL) (i) | 69,535,950 | 51,827,526 |
| CTM - Companhia de Telecomunicações de Macau, SARL (CTM) | 28,607,601 | 30,296,559 |
| Médi Télécom | 12,603,496 | 9,798,765 |
| Banco Best, SA | 7,250,840 | 7,362,020 |
| Páginas Amarelas, SA (Páginas Amarelas) | 3,299,170 | 3,721,127 |
| Hungaro Digital KFT | 3,155,246 | 2,477,113 |
| INESC - Instituto de Engenharia de Sistemas e Computadores (ii) | 2,992,787 | 2,992,787 |
| Guiné Telecom, SARL (ii) | 2,907,534 | 2,907,534 |
| Lisboa TV - Informação e Multimédia, SA (iii) | | 3,534,312 |
| Other companies | 3,346,103 | 3,458,879 |
| | 279,537,646 | 235,355,739 |
| Adjustments for investments in associated companies (Note 39) | (5,900,321) | (5,900,321) |
| | 273,637,325 | 229,455,418 |

- (i) As at 31 December 2007, the fair value of our investment in UOL amounted to Euro 161 million, which compares to a carrying value of Euro 127 million, including goodwill. The fair value of this investment is based on the market price of UOL shares, which are listed on the São Paulo stock market.
- (ii) As at 31 December 2007, these investments are fully adjusted for.
- (iii) The investment in this company is held by PT Conteúdos, a fully owned subsidiary of PT Multimedia, which as at 31 December 2007 is no longer part of the Portugal Telecom Group, following the conclusion of its spin-off on November 2007.

As at 31 December 2007 and 2006, the caption Goodwill, net of impairment losses consists of:

| | 2007 | 2006 |
|------------------|--------------------|--------------------|
| Páginas Amarelas | 83,754,434 | 83,754,434 |
| UOL | 57,299,334 | 53,773,291 |
| Unitel | 26,498,503 | 26,498,503 |
| Other companies | | 586,144 |
| | 167,552,271 | 164,612,372 |

During 2007 and 2006, there were no impairment losses recognized on the above mentioned carrying values of goodwill.

Loans granted to associated companies and other companies are primarily to finance its operations and to develop new businesses and do not have a defined maturity date. As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Médi Télécom | 72,112,464 | 68,106,243 |
| Sportinveste Multimédia (i) | 35,318,668 | 35,318,668 |
| INESC (ii) | 3,292,066 | 3,292,066 |
| Sport TV (iii) | | 12,500,000 |
| Other companies | 4,306,374 | 2,041,301 |
| | 115,029,572 | 121,258,278 |
| Adjustments for loans granted to associated companies and other companies (Note 39) | (3,292,066) | (3,292,066) |
| Adjustments related with the equity accounting on financial investments (Note 39) (iv) | (16,543,265) | (15,948,043) |
| | 95,194,241 | 102,018,169 |

- (i) This caption includes Euro 30,023,168 (Note 43) of additional paid-in capital contributions and Euro 5,295,500 of shareholder loans granted to this associated company.
- (ii) This loan is fully adjusted for its expected realizable value.
- (iii) As at 31 December 2006, these loans were granted by PT Multimedia, which as at 31 December 2007 is no longer part of the Portugal Telecom Group, following the conclusion of its spin-off on November 2007.
- (iv) This caption corresponds to accumulated losses resulting from the equity method of accounting in excess of the value of investments in associated companies, which for that reason are recorded as a reduction to the value of loans granted to those associated companies. If accumulated losses resulting from the equity method of accounting exceed the total investment amount (including loans) of any associated company, a provision is recorded under the caption Provisions for other risks and costs - Other, whenever the Group has assumed responsibilities with that associated company. As at 31 December 2007 and 2006, this provision amounted to Euro 3,634,576 and Euro 4,548,077 (Note 39), respectively. As of those dates, accumulated negative equity accounting adjustments are related to the investment in Sportinveste Multimedia.

As at 31 December 2007 and 2006, the caption Investment in other companies consisted of:

| | 2007 | 2006 |
|--|------------------|------------------|
| Guinetel | 296,545 | 966,277 |
| Janela Digital | 900,790 | 586,696 |
| Archways (i) | | 2,997,158 |
| Other companies | 481,082 | 1,277,212 |
| | 1,678,417 | 5,827,343 |
| Adjustments for investments in group companies (Note 39) | | (2,815,023) |
| | 1,678,417 | 3,012,320 |

(i) This company was fully consolidated as at 31 December 2007.

During 2007 and 2006, the profit and loss caption Equity in earnings of associated companies, net consists of:

| | 2007 | 2006 |
|--------------|--------------------|--------------------|
| Unitel | 91,752,183 | 82,477,320 |
| CTM | 16,951,994 | 14,815,486 |
| UOL | 13,055,606 | 6,150,137 |
| Médi Télécom | 3,081,353 | 45,571,110 |
| Other | 1,286,521 | (18,408,197) |
| | 126,127,657 | 130,605,856 |

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A summarized financial data of the main associated companies as at 31 December 2007 and for the year ended on that date is presented below:

| | Direct percentage of ownership | Total assets | Total liabilities | Shareholders equity | Operating revenues | Net income |
|--------------|--------------------------------------|---------------|-------------------|------------------------|-----------------------|-------------|
| Unitel | 25.00% | 726,217,471 | 142,861,795 | 583,355,676 | 648,843,741 | 367,008,732 |
| Médi Télécom | 32.18% | 1,079,180,662 | 1,040,015,044 | 39,165,618 | 438,440,719 | 9,575,367 |
| UOL | 29.00% | 295,020,991 | 55,241,853 | 239,779,138 | 181,713,739 | 45,019,331 |
| CTM | 28.00% | 149,053,702 | 46,883,698 | 102,170,004 | 207,438,458 | 60,542,836 |

A summarized financial data of the main associated companies as at 31 December 2006 and for the year ended on that date is presented below:

| | Direct percentage of ownership | Total assets | Total liabilities | Shareholders equity | Operating revenues | Net income |
|--------------|--------------------------------------|---------------|-------------------|------------------------|-----------------------|-------------|
| Unitel | 25.00% | 657,489,749 | 189,573,281 | 467,916,468 | 517,082,106 | 329,909,280 |
| Médi Télécom | 32.18% | 1,146,312,081 | 1,115,862,221 | 30,449,860 | 425,073,848 | 141,613,145 |
| UOL | 29.00% | 263,143,894 | 84,428,287 | 178,715,607 | 165,095,125 | 21,207,369 |
| CTM | 28.00% | 165,642,343 | 57,440,347 | 108,201,996 | 209,126,648 | 52,912,450 |

32. Other investments

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|-------------------|--------------------|
| Financial investments available for sale (Note 3.1.ii) | | 99,744,129 |
| Real estate investments, net of accumulated amortisation | 23,024,202 | 26,344,787 |
| Other financial investments | 4,211,218 | 6,302,163 |
| | 27,235,420 | 132,391,079 |

The fair value of financial investments available for sale was determined based on their listed price as of the balance sheet date, and the change in the fair value was recognised in accumulated earnings until the moment investments are disposed of. The movement in the fair value of financial investments available for sale during 2007, was as follows:

| | Balance 31 Dec 2006 | Change in fair value | Disposals (Note 44.d) | Balance 31 Dec 2007 |
|------------------------------|------------------------|-------------------------|--------------------------|------------------------|
| Banco Espírito Santo (BES) | 95,340,000 | 14,978,600 | (110,318,600) | |
| Telefónica | 4,404,129 | 703,812 | (5,107,941) | |
| | 99,744,129 | 15,682,412 | (115,426,541) | |

Following the disposal of the investments in BES and Telefónica, Portugal Telecom has recorded in 2007 gains amounting to Euro 35,698,600 (Note 17) and Euro 2,951,908 (Note 17) under the caption "Net gains on financial assets and other investments", respectively, corresponding to the accumulated changes in the fair value of these investments until the date of the disposal, previously recorded in shareholders' equity.

Real state investments relate to land and buildings owned by PT Comunicações that are not used in its operating activities. These assets are recorded at acquisition cost net of accumulated amortization and impairment losses, if any. PT Comunicações periodically assesses impairment analysis on these assets. As at 31 December 2007, the total carrying value and fair value of real state with acquisition cost above Euro 50,000 amounted to approximately Euro 20 million and Euro 25 million, respectively.

PT Comunicações received rents from lease contracts in 2007 and 2006 amounting to Euro 1,468,871 and Euro 1,827,441 (Note 17), respectively. During the years 2007 and 2006, amortization costs amounted to Euro 831,201 and Euro 1,043,266 (Note 17) respectively, and no impairment losses were recognized.

Regarding real estate investments, investments totaling Euro 7,869,802 are installed in properties of third parties or on public property, and investments amounting to Euro 13,240,021 are not yet registered in PT Comunicações' name.

As at 31 December 2007 and 2006, other financial investments were recorded at acquisition cost net of impairment losses, if any, and consisted of the following:

| | 2007 | 2006 |
|---|-------------------|-------------------|
| Lea Louise (i) | 7,903,379 | |
| Tagusparque | 1,296,875 | 1,296,875 |
| Vortal | 687,514 | 687,514 |
| Seguradora Internacional | 617,224 | 704,448 |
| Cypress (ii) | | 3,016,754 |
| Other | 4,734,872 | 6,477,901 |
| | 15,239,864 | 12,183,492 |
| Adjustments for other investments (Note 39) | (11,028,646) | (5,881,329) |
| | 4,211,218 | 6,302,163 |

(i) During 2007, Portugal Telecom has disposed 90% of its share in this company, which held investments in Congo. Following this disposal, the investment in this company is now fully provided for and is accounted for at cost, while in 2006 was fully consolidated.

(ii) The investment in this company was held by PT Multimedia as at 31 December 2006.

33. Intangible assets

During 2007 and 2006, the movements in intangible assets were as follows:

| | Balance 31 Dec 2006 | Changes in the consolidation perimeter | Discontinued operations | Increases | Foreign currency translation adjustments | Other | Balance 31 Dec 2007 |
|--------------------------------------|------------------------|--|----------------------------|--------------------|--|--------------------|------------------------|
| Cost | | | | | | | |
| Industrial property and other rights | 3,187,464,243 | (539,867) | (207,561,435) | 360,266,362 | 189,260,382 | 29,216,969 | 3,558,106,654 |
| Goodwill | 1,284,041,510 | (9,153,926) | (254,516,010) | | 54,279,165 | | 1,074,650,739 |
| Other intangible assets | 26,944,906 | (286,308) | | 3,699,472 | 112,013 | 3,852,901 | 34,322,984 |
| In-progress intangible assets | 17,672,184 | | (277,194) | 49,395,608 | 2,369,139 | (39,881,559) | 29,278,178 |
| | 4,516,122,843 | (9,980,101) | (462,354,639) | 413,361,442 | 246,020,699 | (6,811,689) | 4,696,358,555 |
| Accumulated depreciation | | | | | | | |
| Industrial property and other rights | 1,008,817,783 | (537,016) | (48,787,295) | 268,931,858 | 67,164,818 | (5,772,013) | 1,289,818,135 |
| Other intangible assets | 16,423,797 | (278,764) | | 5,838,449 | (107,485) | 1,540,996 | 23,416,993 |
| | 1,025,241,580 | (815,780) | (48,787,295) | 274,770,307 | 67,057,333 | (4,231,017) | 1,313,235,128 |
| | 3,490,881,263 | (9,164,321) | (413,567,344) | 138,591,135 | 178,963,366 | (2,580,672) | 3,383,123,427 |

| | Balance 31 Dec 2005 | Changes in the consolidation perimeter | Increases | Foreign currency translation adjustments | Other | Balance 31 Dec 2006 |
|--------------------------------------|------------------------|--|---------------------|--|--------------------|------------------------|
| Cost | | | | | | |
| Industrial property and other rights | 3,054,360,600 | 20,204,865 | 130,552,346 | (56,093,523) | 38,439,955 | 3,187,464,243 |
| Goodwill | 1,252,866,414 | | 41,767,243 | (16,912,229) | 6,320,082 | 1,284,041,510 |
| Other intangible assets | 23,881,640 | | 3,209,235 | 1,423,843 | (1,569,812) | 26,944,906 |
| In-progress intangible assets | 18,145,079 | | 52,979,684 | (1,715,966) | (51,736,613) | 17,672,184 |
| | 4,349,253,733 | 20,204,865 | 228,508,508 | (73,297,875) | (8,546,388) | 4,516,122,843 |
| Accumulated depreciation | | | | | | |
| Industrial property and other rights | 739,141,197 | 5,804,386 | 290,439,334 | (19,709,750) | (6,857,384) | 1,008,817,783 |
| Other intangible assets | 8,492,066 | | 5,488,771 | (260,331) | 2,703,291 | 16,423,797 |
| | 747,633,263 | 5,804,386 | 295,928,105 | (19,970,081) | (4,154,093) | 1,025,241,580 |
| | 3,601,620,470 | 14,400,479 | (67,419,597) | (53,327,794) | (4,392,295) | 3,490,881,263 |

The changes in the consolidation perimeter during 2007 are mainly related to the disposals of TV Cabo Macau and Lea Louise (Exhibit I). The changes in the consolidation perimeter during 2006 are mainly related to the disposal of PrimeSys TI.

Following the approval of the spin-off of PT Multimédia at the last Annual General Meeting of Portugal Telecom held on 27 April 2007, PT Multimedia was classified as a discontinued operation (Note 20), and after the conclusion of the spin-off on 7 November 2007 PT Multimédia is no longer part of the Portugal Telecom Group as at 31 December 2007.

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Increases in accumulated depreciation during 2007 are related to continued operations and were recorded under the caption Depreciation and amortization . During 2006, increases in accumulated depreciation include Euro 276,501,987 related to continued operations, which were included in the caption Depreciation and amortization ,

and Euro 19,426,118 related to discontinued operations, which were included in the caption Discontinued operations .

As at 31 December 2007, the caption Industrial property and other rights includes the following items:

- Euro 339,964,723 related to the acquisition of the Basic Network from the Portuguese State. This amount corresponds to the difference between the amount paid on 27 December 2002 (Euro 365 million) and: (i) the concession rent of 2002 (Euro 16,604,413), which was recorded in the income statement as a cost of the year 2002 because the acquisition occurred only at the end of the year; and (ii) the gain obtained from a QTE lease transaction (Euro 8,430,864) in 2003 with various equipment allocated to the Basic Network, which was considered in the determination of the fair value attributable to the Basic Network in connection with its acquisition by Portugal Telecom;
- Euro 1,934,591,520 related to 50% of (i) the value allocated to the Band A licenses owned by Vivo under the purchase price allocation of certain subsidiaries of Brazil which were incorporated in Vivo, and (ii) the cost of Band B mobile telecommunications licenses obtained by Vivo to operate in certain Brazilian states;
- Euro 717,007,270 related to software licenses;
- Euro 374,839,515 related to a UMTS license obtained by TMN, including Euro 133,092,912 from previous periods and Euro 241,746,603 (Note 7.d) capitalized during the year 2007. In 2000 TMN and the other mobile operators have assumed the commitment of making contributions to the information society during the period through the maturity of the license (2015). At the time it was not possible to reliably estimate how the commitments would be fulfilled, therefore Portugal Telecom did not recognize this commitment as a cost of the license and as a liability. In May 2007, pursuant to an agreement between TMN and the Portuguese State, and based on contributions already made, the outstanding commitments were valued at Euro 355 million. During the second half of 2007, TMN reached an agreement with the Government, which established that (a) Euro 260 million should be realized through the E Initiatives (an initiative lead by the government which offers to school teachers and students laptops and discounts in internet services) and (b) Euro 95 million should be realized through the subsidization of equipments, services discounts and network investments. The amount related to the E Initiatives was recognized as a license cost in 2007 for the amount of its net present value (Euro 233 million), and the Euro 95 million will be recorded when incurred as its expected that these investments will be made in the

normal course of the business of TMN. In addition, TMN assumed the payment of one third of the Oniway's commitment, which amounted to Euro 8 million;

- Euro 95,998,811 related to terminal equipment rented to post-paid customers of mobile businesses, which are being amortised over the period of the related rental contracts;
- Euro 42,575,000 related to contracts signed by PT Comunicações in 2007 for the acquisition of satellite capacity until 2015, which were recorded as capital leases (Note 7.a); and
- Euro 32,278,678 resulting from the MTC's purchase price allocation and related to the value attributed to the agreement entered into with the other shareholders of MTC, which guarantees to Portugal Telecom the control of MTC.

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As at 31 December 2007 and 2006, the goodwill related to subsidiaries was as follows:

| | 2007 | 2006 |
|--|----------------------|----------------------|
| Vivo (i) | 750,381,297 | 692,801,517 |
| Wireline business | | |
| PT.com | 162,624,017 | 162,624,017 |
| PT Comunicações (international carrier business) | 75,634,389 | 75,634,389 |
| PT Prime (Data & Corporate business) | 32,126,523 | 32,126,523 |
| Other | 570,204 | 570,204 |
| | 270,955,133 | 270,955,133 |
| PT Multimedia | | |
| Pay TV and Cable Internet (ii) | | 254,516,010 |
| Other businesses (Note 7.d) | | |
| MTC | 37,216,652 | 40,499,689 |
| PT SI | 8,956,960 | 8,956,960 |
| Cabo Verde Telecom | 7,124,252 | 7,124,252 |
| Web-Lab (iii) | | 6,543,675 |
| TV Cabo Macau (iv) | | 2,610,251 |
| Other | 16,445 | 34,023 |
| | 53,314,309 | 65,768,850 |
| | 1,074,650,739 | 1,284,041,510 |

(i) The increase in the goodwill of Vivo is mainly related to the Brazilian Real appreciation against the Euro in 2007 (Euro/Brazilian Real exchange rate of 2.8118 as at 31 December 2006, as compared to 2.5963 as at 31 December 2007).

(ii) Following the approval of the spin-off of PT Multimédia at the last Annual General Meeting of Portugal Telecom held on 27 April 2007, PT Multimedia was classified as a discontinued operation (Note 20).

(iii) This company was liquidated in in 2007 and the related goodwill was derecognized, with a corresponding charge to net income being recorded under the caption Other costs, net .

(iv) The investment in this company was disposed of in January 2007 for an amount of Euro 3,108,957 (Exhibit I).

For impairment analysis purposes, goodwill was allocated to cash generating units, which correspond to reportable business segments (Note 7). The Company's management has concluded, based on estimated cash flows for those segments discounted using the applicable discount rates, that as at 31 December 2007 the book value of financial investments, including goodwill, did not exceed its recoverable amount.

34. Tangible assets

During 2007 and 2006 the movements in tangible assets were as follows:

| | Balance 31 Dec 2006 | Changes in the consolidation perimeter | Discontinued operations | Increases | Foreign currency translation adjustments | Other | Balance 31 Dec 2007 |
|--|------------------------|--|----------------------------|----------------------|--|----------------------|------------------------|
| Cost | | | | | | | |
| Land | 80,701,925 | | (2,536,060) | 69,550 | 916,414 | (65,529) | 79,086,300 |
| Buildings and other constructions | 994,010,394 | (690,905) | (41,689,480) | 19,985,588 | 4,292,819 | 17,158,778 | 993,067,194 |
| Basic equipment | 11,693,392,675 | (6,580,133) | (592,065,927) | 392,951,324 | 212,738,612 | 70,289 | 11,700,506,840 |
| Transportation equipment | 83,151,249 | (140,853) | (6,719,774) | 12,836,409 | 151,595 | (11,668,384) | 77,610,242 |
| Tools and dies | 22,364,493 | (42,376) | (240,069) | 2,537,465 | 411,426 | 297,133 | 25,328,072 |
| Administrative equipment | 1,040,518,167 | (627,411) | (60,499,407) | 63,684,649 | 11,548,390 | 918,314 | 1,055,542,702 |
| Other tangible assets | 68,698,713 | | (17,322,602) | 1,561,968 | (78,606) | (500,322) | 52,359,151 |
| In-progress tangible assets | 202,969,026 | | (7,557,835) | 233,416,082 | 15,077,570 | (281,337,059) | 162,567,784 |
| Advances to suppliers of tangible assets | 332,613 | | (663,882) | 628,943 | (25,042) | (5,786) | 266,846 |
| | 14,186,139,255 | (8,081,678) | (729,295,036) | 727,671,978 | 245,033,178 | (275,132,566) | 14,146,335,131 |
| Accumulated depreciation | | | | | | | |
| Land | 12,329,972 | | | | | (49,241) | 12,280,731 |
| Buildings and other constructions | 561,196,222 | (566,965) | (14,454,140) | 49,435,848 | 1,043,696 | 1,369,195 | 598,023,856 |
| Basic equipment | 8,696,866,112 | (5,739,792) | (360,337,269) | 700,821,336 | 144,583,390 | (222,489,094) | 8,953,704,683 |
| Transportation equipment | 43,232,754 | (79,185) | (4,013,203) | 15,170,378 | 38,445 | (9,802,567) | 44,546,622 |
| Tools and dies | 18,458,676 | (35,691) | (199,540) | 1,109,858 | 182,551 | (13,276) | 19,502,578 |
| Administrative equipment | 848,234,080 | (582,192) | (38,317,829) | 79,965,453 | 7,273,738 | (13,649,791) | 882,923,459 |
| Other tangible assets | 63,788,249 | | (14,690,691) | 1,791,559 | 5,149,474 | (6,082,560) | 49,956,031 |
| | 10,244,106,065 | (7,003,825) | (432,012,672) | 848,294,432 | 158,271,294 | (250,717,334) | 10,560,937,960 |
| | 3,942,033,190 | (1,077,853) | (297,282,364) | (120,622,454) | 86,761,884 | (24,415,232) | 3,585,397,171 |

| | Balance 31 Dec 2005 | Changes in the consolidation perimeter | Increases | Foreign currency translation adjustments | Other | Balance 31 Dec 2006 |
|--|------------------------|--|--------------------|--|----------------------|------------------------|
| Cost | | | | | | |
| Land | 79,629,860 | | 2,312,775 | (272,885) | (967,825) | 80,701,925 |
| Buildings and other constructions | 936,482,427 | 1,743,311 | 56,727,434 | (2,207,897) | 1,265,119 | 994,010,394 |
| Basic equipment | 11,217,237,559 | 79,181,389 | 455,369,922 | (69,566,280) | 11,170,085 | 11,693,392,675 |
| Transportation equipment | 76,931,737 | | 20,068,542 | (372,063) | (13,476,967) | 83,151,249 |
| Tools and dies | 20,240,728 | (21,360) | 1,498,937 | (145,963) | 792,151 | 22,364,493 |
| Administrative equipment | 964,421,977 | 381,682 | 82,916,060 | (4,694,126) | (2,507,426) | 1,040,518,167 |
| Other tangible assets | 65,655,643 | | 3,829,650 | (103,776) | (682,804) | 68,698,713 |
| In-progress tangible assets | 152,051,621 | | 241,376,013 | (7,353,249) | (183,105,359) | 202,969,026 |
| Advances to suppliers of tangible assets | 1,359,837 | | (470,221) | 9,898 | (566,901) | 332,613 |
| | 13,514,011,389 | 81,285,022 | 863,629,112 | (84,706,341) | (188,079,927) | 14,186,139,255 |

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| Accumulated depreciation | | | | | | |
|-----------------------------------|----------------------|-------------------|---------------------|---------------------|----------------------|-----------------------|
| Land | 12,417,562 | | | | (87,590) | 12,329,972 |
| Buildings and other constructions | 519,591,043 | 683,228 | 48,899,458 | (571,856) | (7,405,651) | 561,196,222 |
| Basic equipment | 8,019,715,144 | 33,285,575 | 761,886,334 | (48,402,612) | (69,618,329) | 8,696,866,112 |
| Transportation equipment | 39,693,211 | | 14,742,687 | (225,130) | (10,978,014) | 43,232,754 |
| Tools and dies | 17,753,878 | (92) | 826,139 | (82,138) | (39,111) | 18,458,676 |
| Administrative equipment | 777,628,771 | 529,212 | 85,220,550 | (2,893,519) | (12,250,934) | 848,234,080 |
| Other tangible assets | 65,208,659 | | 2,274,369 | (447,067) | (3,247,712) | 63,788,249 |
| | 9,452,008,268 | 34,497,923 | 913,849,537 | (52,622,322) | (103,627,341) | 10,244,106,065 |
| | 4,062,003,121 | 46,787,099 | (50,220,425) | (32,084,019) | (84,452,586) | 3,942,033,190 |

The changes in the consolidation perimeter during 2007 are mainly related to the disposals of TV Cabo Macau and Lea Louise (Exhibit I). The changes in the consolidation perimeter during 2006 are mainly related to the disposal of PrimeSys TI.

Following the approval of the spin-off of PT Multimédia at the Annual General Meeting of Portugal Telecom held on 27 April 2007, PT Multimedia was classified as a discontinued operation (Note 20), and after the conclusion of the

spin-off on 7 November 2007 PT Multimédia is no longer part of the Portugal Telecom Group as at 31 December 2007.

Increases in accumulated depreciation during 2007 are related to continued operations and were recorded under the caption Depreciation and amortization . Increases in accumulated depreciation during 2006 include Euro 854,211,820 related to continued operations, which were included in the caption Depreciation and amortization , and Euro 59,637,717 related to discontinued operations, which were included in the caption Discontinued operations .

In 2007, the column Other includes respectively Euro 15 million and Euro 21 million related to the write-off and disposal of certain fixed assets at PT Comunicações, which were included under the captions of Other costs, net and Net gains on disposals of fixed assets of the wireline business. In 2006, the column Other includes (i) Euro 51 million related to adjustments to the value of certain CDMA equipments at Vivo (Note 15), (ii) Euro 11 million related to the write-off of certain fixed assets at PT Comunicações, and (iii) Euro 6 million related to the impact of the change in the estimated useful life of certain tangible assets at PT Multimedia.

The following situations regarding tangible assets should be mentioned:

- Euro 1,103,300,380 of tangible assets of PT Comunicações are related to the Concession, under the terms of the Modification Agreement of the Concession;
- Euro 19,759,332 of tangible assets of PT Comunicações are located outside Portugal, including participations in submarine cable consortiums; and
- In previous years, PT Comunicações, PT Prime and TMN entered into QTE lease contracts, which comprised the sale of certain telecommunications equipment to foreign entities. Simultaneously, those entities entered into leasing contracts with special purpose entities, which made conditional sale agreements to sell the related equipment to PT Comunicações, PT Prime and TMN, at an amount equivalent to the initial sales price. Group companies maintained the legal ownership of those equipments, continuing to be able to sell or substitute any equipment. These transactions correspond to a sale and lease-back and, accordingly, the sale of the equipment was not recorded and the equipment continued to be included in the Company's consolidated balance sheet. On December 2007, some of these contracts were early terminated upon decision of the counterparty without any costs for Portugal Telecom (Note 30).

35. Debt

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | | 2006 | |
|--|----------------------|----------------------|----------------------|----------------------|
| | Short-term | Long-term | Short-term | Long-term |
| Exchangeable bonds | | 689,407,731 | | |
| Bonds | 96,290,875 | 3,061,702,959 | | 3,133,646,046 |
| Bank loans | | | | |
| External loans | 429,216,931 | 940,374,402 | 381,866,643 | 1,075,326,685 |
| Domestic loans | 2,073,991 | 530,120 | 24,994,569 | 28,075,839 |
| Other loans | | | | |
| Commercial paper | 323,688,504 | | 749,411,565 | |
| External loans | 271,700 | | 460,231 | 271,654 |
| Commitments under the UMTS license | 55,911,577 | 144,659,000 | | |
| Liability related to equity swaps on treasury shares (Note 41.3) | 323,178,913 | | 187,612,393 | |
| Leasings | 25,452,994 | 124,001,602 | 28,378,629 | 230,216,908 |
| | 1,256,085,485 | 4,960,675,814 | 1,372,724,030 | 4,467,537,132 |

35.1. Exchangeable bonds

On 28 August 2007, PT Finance issued exchangeable bonds totaling Euro 750,000,000, exchangeable into fully paid ordinary shares of Portugal Telecom, which had the following terms:

- Exchange price: Euro 13.9859 per ordinary share of Portugal Telecom, adjusted to Euro 11.60 on 30 October 2007, following the spin-off of PT Multimedia, according to the terms and conditions of the bonds;
- Nominal value: Euro 50,000;
- Maturity: 28 August 2014 unless previously redeemed, acquired, cancelled or converted; and
- Fixed interest rate: 4.125% per annum, paid semi-annually.

In accordance with IFRS, exchangeable bonds represent a compound instrument and accordingly the market value of the equity component as of the date the bonds were issued amounted to Euro 57,145,442 (Note 41) and was recorded in shareholders' equity, while the financial liability component is recorded through the amortized cost.

As at 31 December 2007, the fair value of the exchangeable bonds amounted to Euro 791 million.

35.2. Bonds

On 7 April 1999, PT Finance issued notes totaling Euro 1,000,000,000 under a Global Medium Term Note (GMTN) Programme, with an annual fixed interest rate of 4.625% and maturity in April 2009. The Company acquired in previous years certain of these bonds (held by the Company in treasury) with a notional amount of Euro 120,500,000, which were cancelled in November 2004. As at 31 December 2007, the notional amount of these bonds outstanding totals Euro 879,500,000.

On 1 August 2003, Vivo Participações issued bonds amounting to 500 million Brazilian Reais (Euro 96 million as at 31 December 2007 corresponding to the 50% consolidated in Portugal Telecom s balance sheet), with a maturity of five years and bearing an annual interest at a rate corresponding to 104.4% of the CDI rate.

On 1 May 2005, Vivo Participações issued bonds amounting to 1 billion Brazilian Reais (Euro 193 million as at 31 December 2007 corresponding to the 50% consolidated in Portugal Telecom s balance sheet), with a maturity of ten years and bearing an annual interest rate ranging between 103.3% and 104.2% of the CDI.

In 2005, PT Finance issued three Eurobonds under the GMTN Programme, with the following amounts and maturities:

- On 24 March 2005, issued Eurobonds totaling Euro 1,000,000,000 at an annual interest rate of 3.75% and maturity in 2012;
- On 24 March 2005, issued Eurobonds totaling Euro 500,000,000 at an annual interest rate of 4.375% and maturity in 2017;
- On 16 June 2005, issued Eurobonds totaling Euro 500,000,000 at an annual interest rate of 4.5% and maturity in 2025.

Expenses incurred at the date of these bonds were issued, which are related to roundings in defining the coupon rate and to commissions, are deferred and recorded as a deduction to these loans, and recognized in earnings through the life of the bonds. As at 31 December 2007, the balance of these prepaid expenses amounted to Euro 10,378,792.

As at 31 December 2007, the maximum possible nominal amount of outstanding notes issued under the GMTN Programme established by PT Finance amounted to Euro 7,500,000,000, of which Euro 2,879,500,000 were outstanding as at 31 December 2007.

As at 31 December 2007, the fair value of the bonds issued amounted to Euro 2,951 million.

35.3. Bank loans

As at 31 December 2007 and 2006, bank loans are denominated in the following currencies:

| | 2007 | | 2006 | |
|----------------|-----------------------------|----------------------|-----------------------------|----------------------|
| | Currency of the notional | Euro | Currency of the notional | Euro |
| Euro | 773,402,571 | 773,402,571 | 945,336,195 | 945,336,195 |
| US Dollar | 13,375,741 | 9,086,163 | 28,128,423 | 21,357,952 |
| Brazilian Real | 1,529,060,685 | 588,938,368 | 1,505,081,850 | 535,273,437 |
| Other | | 768,342 | | 8,296,152 |
| | | 1,372,195,444 | | 1,510,263,736 |

In 2003, the Company entered into a Revolving Credit Facility amounting to Euro 500 million, with a maturity of 2 years and an extension option. In 2005, the maturity of this facility was renegotiated with 50% of the loan payable in February 2009 and the remainder in February 2010.

In 2004, Portugal Telecom and PT Finance obtained three other Revolving Credit Facilities totaling Euro 550 million, as follows:

- On 24 June 2004, with an initial amount of Euro 150 million, increased to Euro 300 million in 2007, and an initial maturity of four years, which was extended to six years in 2005 and to eight years in 2007;
- On 18 October 2004, with an amount of Euro 100 million and an initial maturity of three years, which was extended to five years in 2005; and
- On 22 October 2004, with an amount of Euro 150 million and a maturity of three years and six months.

As at 31 December 2007, the Group had used an amount of Euro 150 million in connection with these four standby facilities.

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As at 31 December 2007, Vivo also had available standby facilities in the total amount of R\$ 1,160 million, of which no amount was being used at that date.

As at 31 December 2007, loans obtained from the European Investment Bank (EIB) and KfW amounted to, respectively, Euro 605 million and Euro 5 million, maturing up to 2014.

As at 31 December 2007 and 2006, the bank loans of Portugal Telecom and its group companies bear interest at annual interest rates, equivalent to loans denominated in Euros, which vary between:

| | 2007 | 2006 |
|---------|-------|-------|
| Maximum | 5.20% | 5.46% |
| Minimum | 3.00% | 3.00% |

As at 31 December 2007 , the fair value of total bank loans amounted to Euro 1,335 million.

35.4. Commercial paper

Portugal Telecom has entered into committed short-term commercial paper programs, amounting to a total of Euro 875,000,000. As at 31 December 2007, the Company had used an amount of Euro 323,688,504, with maturity in January 2008 and interest at an annual average rate of 4.60%. The fair value as at 31 December 2007 of outstanding commercial paper is similar to its carrying value.

35.5. Commitments under the UMTS license

This amount corresponds to the present value of the payments related to the commitments assumed by TMN under the UMTS license (Note 33).

35.6. Leasings

Financial leasing obligations recorded as at 31 December 2007 are mainly related to the lease of vehicles and buildings and to contracts for the acquisition of satellite capacity. The reduction occurred in this caption is primarily explained by the contribution of the multimedia business as at 31 December 2006, which amounted to approximately Euro 143 million.

35.7. Medium and long-term debt

As at 31 December 2007, long-term debt mature on the following years:

| | |
|--------------------------|----------------------|
| 2009 | 1,122,489,793 |
| 2010 | 226,250,963 |
| 2011 | 159,840,002 |
| 2012 | 1,282,203,996 |
| 2013 and following years | 2,169,891,060 |
| | 4,960,675,814 |

35.8. Covenants

As at 31 December 2007, the Company had several covenants related to its indebtedness, which have been fully complied with as at that date, as follows:

- **Change in control**

The exchangeable bonds, the credit facilities amounting to Euro 1,050 million and certain loans obtained from EIB totaling Euro 598 million as at 31 December 2007, grant the right to the lenders of demanding the repayment of all amounts due in the case of any change in the control of Portugal Telecom.

- **Credit rating**

Certain loan agreements with the EIB, totaling Euro 343 million as at 31 December 2007, stated that Portugal Telecom may be asked to present a guarantee acceptable by the EIB if, at any time, the long-term credit rating assigned by the rating agencies to Portugal Telecom was reduced to BBB/Baa2 or less. As a result of Portugal Telecom's downgrade on 3 August 2006 to BBB- by S&P, to Baa2 by Moody's and to BBB by Fitch, the Company negotiated with EIB revised terms and conditions for these loans. The agreement between the two entities, signed on 23 February 2007, allows PT to present the guarantee only in the case of a downgrade from the current rating (BBB- by S&P, Baa2 by Moody's and BBB by Fitch).

- **Control/disposal of subsidiaries**

The credit facility amounting to Euro 500 million states that Portugal Telecom must, directly or indirectly, maintain majority ownership and control of each material subsidiary. Material subsidiaries are those companies whose total assets are equal or exceed 10% of total consolidated assets or whose total revenues are also equal or exceed 10% of total consolidated revenues. As of the date of this filing there are no outstanding amounts related to this credit facility.

- **Disposals of assets**

The credit facility amounting to Euro 100 million and certain EIB loans totaling Euro 599 million as at 31 December 2007 include certain restrictions regarding the disposal of assets by Portugal Telecom. Following the agreement signed with EIB on 23 February 2007 mentioned above, the bank waived its rights related to this covenant solely for the PT Multimedia spin-off.

- **Financial ratios**

The facility of Euro 500 million and the facility of Euro 150 million state that the ratio Consolidated Net Debt/EBITDA should not be higher than 3.5. The credit facility of Euro 100 million, states that the ratio Consolidated Net Debt/EBITDA should not be higher than 4.0. In addition, the conditions (spread and maturity) applicable to the facility of Euro 500 million and to the Euro 300 million facility obtained in June 2004 may be changed if the ratio Consolidated Net Debt/EBITDA is higher than, respectively, 2.5 and 2.25. As at 31 December 2007, this ratio stood at 1.9.

- **Negative Pledge**

The Global Medium Term Notes, the exchangeable bonds and the facilities totaling Euro 1,050 million are subject to negative pledge clauses, which restrict the pledge of security interests in the assets of companies included in the consolidation.

36. Accounts payable

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|-------------------------------|----------------------|----------------------|
| Accounts payable-trade | 726,507,575 | 706,367,545 |
| Fixed asset suppliers | 310,118,957 | 347,216,526 |
| Accounts payable to employees | 22,693,009 | 18,382,030 |
| Other | 49,562,622 | 43,123,122 |
| | 1,108,882,163 | 1,115,089,223 |

37. Accrued expenses

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--------------------------------|--------------------|--------------------|
| Supplies and external services | 256,280,710 | 299,237,991 |
| Interest expense (i) | 188,695,831 | 196,902,460 |
| Vacation pay and bonuses | 107,293,868 | 111,835,095 |
| Discounts to clients | 53,500,672 | 39,057,657 |
| Other | 35,279,847 | 33,184,329 |
| | 641,050,928 | 680,217,532 |

(i) As at 31 December 2007 and 2006, this caption included (a) Euro 44.7 million and Euro 58.5 million (Note 42), respectively, related to the fair value of the interest component of the exchange rate and interest rate derivatives contracted by Vivo, and (b) Euro 13.7 million and Euro 11.2 million (Note 42), respectively, related to the fair value of exchange rate and interest rate derivatives contracted by several Group companies.

38. Deferred income

As at 31 December 2007 and 2006, this caption consists of:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Current deferred income | | |
| Advance billings | | |
| Pre-paid mobile traffic | 129,224,776 | 111,408,166 |
| Penalties imposed to customers relating to violations of contracts | 45,031,350 | 39,942,294 |
| Other advance billings | 76,102,570 | 41,948,176 |
| Other | 35,697,771 | 22,439,675 |
| | 286,056,467 | 215,738,311 |

39. Provisions and adjustments

During the years 2007 and 2006, the movements in this caption were as follows:

| | Balance 31 Dec 2006 | Changes in the consolidation perimeter | Discontinued operations | Increases | Decreases | Foreign currency translation adjustments | Other | Balance 31 Dec 2007 |
|---|------------------------|--|----------------------------|--------------------|---------------------|--|----------------------|------------------------|
| Adjustments | | | | | | | | |
| For doubtful accounts receivable (Notes 25 and 26) | 424,611,862 | (326,253) | (63,075,788) | 104,873,101 | (7,561,496) | 7,458,925 | (98,201,278) | 367,779,073 |
| For inventories (Note 27) | 24,632,948 | | (7,555,757) | 761,252 | (1,981,787) | 1,032,940 | (513,224) | 16,376,372 |
| For investments (Note 31 and 32) | 33,836,782 | 7,620,942 | (3,076,928) | 1,302,893 | (903,796) | 221,617 | (2,237,212) | 36,764,298 |
| | 483,081,592 | 7,294,689 | (73,708,473) | 106,937,246 | (10,447,079) | 8,713,482 | (100,951,714) | 420,919,743 |
| Provisions for risks and costs | | | | | | | | |
| Litigation (Note 46) | 52,386,942 | | (137,000) | 40,991,892 | (2,210,664) | 3,925,349 | (25,472,417) | 69,484,102 |
| Taxes | 43,655,078 | (22,689) | (6,423,765) | 10,871,672 | (13,464,072) | 1,436,574 | (1,301,846) | 34,750,952 |
| Other | 111,743,038 | (773,190) | (5,843,708) | 9,908,852 | (379,335) | 3,586,804 | 12,696,059 | 130,938,520 |
| | 207,785,058 | (795,879) | (12,404,473) | 61,772,416 | (16,054,071) | 8,948,727 | (14,078,204) | 235,173,574 |
| | 690,866,650 | 6,498,810 | (86,112,946) | 168,709,662 | (26,501,150) | 17,662,209 | (115,029,918) | 656,093,317 |

Changes in the

Foreign currency

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| | Balance 31 Dec 2005 | consolidation perimeter | Increases | Decreases | translation adjustments | Other | Balance 31 Dec 2006 |
|--|------------------------|----------------------------|--------------------|----------------------|----------------------------|----------------------|------------------------|
| Adjustments | | | | | | | |
| For doubtful accounts receivable (Notes 25 and 26) | 373,818,493 | 521,587 | 283,188,936 | (42,065,033) | (6,258,490) | (184,593,631) | 424,611,862 |
| For inventories (Note 27) | 28,247,571 | | 2,653,654 | (5,247,510) | (227,079) | (793,688) | 24,632,948 |
| For investments (Note 31 and 32) | 65,270,472 | | 6,336,241 | (36,098,033) | 310,993 | (1,982,891) | 33,836,782 |
| | 467,336,536 | 521,587 | 292,178,831 | (83,410,576) | (6,174,576) | (187,370,210) | 483,081,592 |
| Provision for risks and costs | | | | | | | |
| Litigation (Note 46) | 74,717,074 | | 26,460,483 | (2,286,421) | (1,924,893) | (44,579,301) | 52,386,942 |
| Taxes | 68,293,691 | | 13,960,219 | (32,635,330) | (1,391,010) | (4,572,492) | 43,655,078 |
| Other | 135,511,379 | | 5,374,211 | (12,385,262) | (934,093) | (15,823,197) | 111,743,038 |
| | 278,522,144 | | 45,794,913 | (47,307,013) | (4,249,996) | (64,974,990) | 207,785,058 |
| | 745,858,680 | 521,587 | 337,973,744 | (130,717,589) | (10,424,572) | (252,345,200) | 690,866,650 |

The changes in the consolidation perimeter during 2007 are mainly related to the disposals of TV Cabo Macau and Lea Louise (Exhibit I).

Following the approval of the spin-off of PT Multimédia at the last Annual General Meeting of Portugal Telecom held on 27 April 2007, PT Multimedia was classified as a discontinued operation (Note 20), and after the conclusion of the spin-off on November 2007 is no longer part of the Portugal Telecom Group as at 31 December 2007.

As at 31 December 2007 and 2006, the caption Provisions for risks and costs was classified in the balance sheet in accordance with the expected settlement date, as follows:

| | 2007 | 2006 |
|------------------------------|--------------------|--------------------|
| Current provision | | |
| Litigation | 41,120,207 | 32,053,458 |
| Taxes | 27,326,736 | 26,512,397 |
| Other | 54,893,257 | 46,585,636 |
| | 123,340,200 | 105,151,491 |
| Non-current provision | | |
| Litigation | 28,363,895 | 20,333,484 |
| Taxes | 7,424,216 | 17,142,681 |
| Other | 76,045,263 | 65,157,402 |
| | 111,833,374 | 102,633,567 |
| | 235,173,574 | 207,785,058 |

The provision for taxes relates to probable tax contingencies, which were estimated based on internal information and the opinion of external tax advisors.

As at 31 December 2007 and 2006, the caption Provisions for risks and costs - Other, consists of:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Asset retirement obligation (Note 3.g) | 71,211,681 | 58,867,102 |
| Customer retention programs (i) | 48,381,701 | 42,607,492 |
| Negative financial investments (Note 31) (ii) | 3,634,576 | 4,548,077 |
| Other | 7,710,562 | 5,720,367 |
| | 130,938,520 | 111,743,038 |

- (i) This provision was recognised by TMN and Vivo to settle future liabilities relating to customer retention programmes and was computed based on present catalogue costs and estimated usage levels.
- (ii) This provision relates to accumulated losses in affiliated companies resulting from the application of the equity method of accounting exceeding the corresponding total invested amount, including loans (Notes 2.a).

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The increases in provisions and adjustments in 2007 and 2006 were recognised in the income statement as follows:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Provisions and adjustments | 150,849,660 | 288,106,111 |
| Equity in losses of affiliated companies | 5,997,142 | 7,588,684 |
| Income taxes (Notes 19 and 28) | 9,430,412 | 8 545 381 |
| Discontinued operations - other costs (Note 20) | | 16,456,669 |
| Costs of products sold (Note 11) | 197,841 | 1,159,694 |
| Curtailement costs, net (Note 9.5) | | 11,528,257 |
| Other | 2,234,607 | 4,588,948 |
| | 168,709,662 | 337,973,744 |

The decreases in these captions in 2007 and 2006 were recognised in the income statement as follows:

| | 2007 | 2006 |
|---|-------------------|--------------------|
| Provisions and adjustments | 22,913,191 | 69,378,844 |
| Costs of products sold (Note 11) | 1,957,157 | 3,279,638 |
| Equity in earnings of affiliated companies | 892,076 | 36,675,164 |
| Income taxes (Notes 19 and 28) | 622,021 | |
| Discontinued operations - other costs (Note 20) | | 14,078,590 |
| Indirect taxes (Note 14) | | 4,214,639 |
| Discontinued operations - commercial costs | | 1,874,213 |
| Other | 116,705 | 1,216,501 |
| | 26,501,150 | 130,717,589 |

In 2007 and 2006, the profit and loss caption Provisions and adjustments consists of:

| | 2007 | 2006 |
|--|--------------------|--------------------|
| Increases in provisions and adjustments for doubtful receivables and other | 150,849,660 | 288,106,111 |
| Decreases in provisions and adjustments for doubtful receivables and other | (22,913,191) | (69,378,844) |
| Direct write-off of accounts receivable | 2,986,716 | 11,051,654 |
| Collections from accounts receivable which were previously written-off | (3,889,466) | (13,142,566) |
| | 127,033,719 | 216,636,355 |

The amount in the column Other movements under the caption Adjustments for doubtful accounts receivable relates mainly to the write-off of balances previously fully provided for (Note 25).

In the caption of Provisions for risks and costs Litigation, the reduction in column Other in the year 2006 is mainly related to the unfavorable resolution of a legal action against Vivo related to the privatization of Telebrás in 1998, following which Vivo paid an amount of Euro 26 million.

40. Other current and non-current liabilities

As at 31 December 2007 and 2006, these captions consist of:

| | 2007 | 2006 |
|---|--------------------|--------------------|
| Other current liabilities | | |
| Accounts payable from QTE transactions (Notes 3.1.ix) and 30) | 35,324,314 | 46,332,009 |
| Dividends payable (i) | 5,680,966 | 8,909,070 |
| Other (ii) | 26,303,667 | 27,254,810 |
| | 67,308,947 | 82,495,889 |
| Other non-current liabilities | | |
| Accounts payable from QTE transactions (Notes 3.1.ix) and 30) | 470,140,303 | 627,430,804 |
| Fair value of derivative financial instruments (Note 42) | 47,808,141 | 44,048,655 |
| Other (iii) | 3,824,096 | 11,065,915 |
| | 521,772,540 | 682,545,374 |

-
- (i) This caption is related to unpaid dividends declared by Brasilcel's subsidiaries.
- (ii) As at 31 December 2007 and 2006, this caption includes primarily an account payable to the shareholders of the subsidiaries of Brasilcel in connection with a reverse stock split undertaken in 2005. In this transaction, the shares issued by the various companies were grouped in lots, with each lot exchanged for a new share. Because certain shareholders did not possess a sufficient number of shares to receive a new share in exchange, an auction of the shares not attributed/exchanged was undertaken. Each company recognized the value received in this auction as a payable to the former shareholders, which will be reduced to the extent the former shareholders request those amounts.
- (iii) This caption includes primarily accrued expenses in connection with certain loans obtained by Vivo where the interest component is payable in more than 12 months.

41. Shareholders Equity

During 2006 and 2007, the movements in this caption were as follows:

| | Share capital | Capital issued premium | Treasury shares | Legal reserve | Reserve for treasury shares | Accumulated earnings | Total equity excluding minority interests |
|--|----------------------|------------------------|----------------------|--------------------|-----------------------------|----------------------|---|
| Balance as at 31 December 2005 | 1,128,856,500 | 91,704,891 | (102,044,948) | 179,229,361 | 125,428,500 | 405,216,985 | 1,828,391,289 |
| Share capital increase through the incorporation of reserves | 338,656,950 | (91,704,891) | | (121,523,559) | (125,428,500) | | |
| Increase of free reserves through a share capital reduction | (1,072,413,675) | | | | | 1,072,413,675 | |
| Acquisition of treasury shares through equity swaps | | | (171,984,398) | | | | (171,984,398) |
| Cash settlement of equity swaps over treasury shares (Note 41.3) | | | 86,416,953 | | | | 86,416,953 |
| Dividends paid (Notes 22 and 44.i) | | | | | | (526,402,838) | (526,402,838) |
| Earnings allocated to the legal reserve | | | | 25,001,079 | | (25,001,079) | |
| Income recognized directly in equity | | | | | | 172,069,067 | 172,069,067 |
| Income recognized in the income statement | | | | | | 866,759,657 | 866,759,657 |
| Balance as at 31 December 2006 | 395,099,775 | | (187,612,393) | 82,706,881 | | 1,965,055,467 | 2,255,249,730 |
| Share capital increase | 79,019,955 | | | (79,019,955) | | | |
| Share capital reduction | (440,254,035) | | | | | 440,254,035 | |
| Acquisition of treasury shares, through equity swaps (Note 41.3) | | | (607,692,439) | | | | (607,692,439) |
| Acquisition of treasury shares (Note 41.3) | | | (1,050,271,924) | | 1,050,271,924 | (1,050,271,924) | (1,050,271,924) |
| Cancellation of treasury shares (Note 41.3) | (3,091,695) | | 1,050,271,924 | | (1,047,180,229) | | |
| Cash settlement of equity swaps over treasury shares (Note 41.3) | | | 472,125,919 | | | | 472,125,919 |
| Dividends paid (Notes 22 and 44.i) | | | | | | (516,506,816) | (516,506,816) |
| Spin-off of PT Multimédia (Note 20) | | | | | | (405,328,608) | (405,328,608) |
| Equity component of exchangeable bonds (Note 35) | | | | | | 57,145,442 | 57,145,442 |
| Earnings allocated to the legal reserve | | | | 3,086,213 | | (3,086,213) | |
| Income recognized directly in equity | | | | | | 391,640,857 | 391,640,857 |
| Income recognized in the income statement | | | | | | 741,859,736 | 741,859,736 |
| Balance as at 31 December 2007 | 30,774,000 | | (323,178,913) | 6,773,139 | 3,091,695 | 1,620,761,976 | 1,338,221,897 |

41.1. Share capital

As approved at the Annual General Meeting held on 27 April 2007, Portugal Telecom has completed on 22 May 2007 its share capital increase of Euro 79,019,955, through the incorporation of legal reserve, and its share capital reduction of Euro 440,254,035, for the release of excess capital through the creation of free reserves in the same amount.

On 28 September 2007, under the terms of the share buyback program approved at the General Shareholders Meeting held on 27 April 2007, Portugal Telecom acquired 103,056,500 of its own shares, through the physical exercise of equity swaps (Note 41.3). As resolved also in the General Meeting held on 27 April 2007 and for the purposes of the execution of the share buyback program and the corresponding share capital reduction, Portugal Telecom has reduced its share capital by Euro 3,091,695 (Note 41.3) through the cancellation of these 103,056,500 treasury shares.

As a result of the referred operations, Portugal Telecom's fully subscribed and paid share capital as at 31 December 2007, amounted to Euro 30,774,000 and was represented by 1,025,800,000 shares, with a nominal value of three cents each with the following distribution:.

- 1,025,799,500 ordinary shares; and
- 500 Class A shares.

The following matters may not be approved in a General Shareholders Meeting against the majority of the votes corresponding to Class A shares:

- Authorization for the acquisition of ordinary shares representing more than 10% of the share capital by shareholders that directly or indirectly perform competing activities to those of the companies within a dominant relation with Portugal Telecom;
- Amendments to the by-laws and share capital increases, as well as the limitation or suppression of pre-emptive rights and the establishing of standards for share capital increases to be resolved by the Board of Directors;
- Issuing of bonds or other securities, establishing the issue value for these securities to be resolved by the Board of Directors and limitation or suppression of pre-emptive rights in the issuing of bonds convertible into shares, as well as establishing the standards for the issuing of bonds of such nature to be resolved by the Board of Directors;
- The passing of resolutions on the application of the financial year results, in the case of dividend distribution to the shareholders in a percentage superior to 40% of distributable profits;
- Election of the Board of the General Shareholders Meeting;
- Approval of the general goals and fundamental principles of the Company's policies;
- Definition of the general principles of the policy of shareholdings in companies, as well as, in the cases where those principles require prior General Shareholders Meeting authorization, the passing of resolutions on the respective acquisitions and sales;
- Moving the Company's registered offices within the municipality of Lisbon or to a neighbouring municipality.

In addition, the election of one third of the total number of Directors, including the Chairman of the Board of Directors, requires the approval of a majority of the votes of the Class A shares.

41.2. Capital issued premium

This caption resulted from premiums generated in capital increases made by Portugal Telecom. According to Portuguese law, applicable to companies listed in stock exchanges under the supervision of Comissão do Mercado de Valores Mobiliários (CMVM , the Portuguese securities and stock exchange regulator), these amounts can only be used to increase share capital or to absorb accumulated losses (without it being necessary to first use other reserves). This amount cannot be used to pay dividends or to acquire treasury shares. The total capital issued premium was used in the share capital increase effective on 11 May 2006, as approved at the Annual General Meeting of 21 April 2006.

41.3. Treasury shares

As at 31 December 2007 and 2006, this caption includes equity swaps contracted by Portugal Telecom up to those dates that are recognised as an effective acquisition of treasury shares, thus implying the recognition of a corresponding financial liability (Note 35).

During 2006 and 2007, the movements in these captions were as follows:

| | Number of shares | Nominal value | Premiums and discounts | Carrying value | Carrying value per share |
|---|-------------------|-------------------|------------------------|--------------------|--------------------------|
| Balance as at 31 December 2005 | 13,240,000 | 13,240,000 | 88,804,948 | 102,044,948 | 7.71 |
| Equity swaps over treasury shares | 18,740,000 | 6,559,000 | 165,425,398 | 171,984,398 | |
| Cash settlement of equity swaps over treasury shares | (11,340,000) | (3,969,000) | (82,447,953) | (86,416,953) | |
| Change in the nominal value of each share | | (8,606,000) | 8,606,000 | | |
| Balance as at 31 December 2006 | 20,640,000 | 7,224,000 | 180,388,393 | 187,612,393 | 9.09 |
| Equity swaps over treasury shares (i) | 63,412,972 | 1,902,389 | 605,790,050 | 607,692,439 | |
| Acquisitions of treasury shares (Note 41.1) | 103,056,500 | 3,091,695 | 1,047,180,229 | 1,050,271,924 | |
| Cancellation of treasury shares (Note 41.1) | (103,056,500) | (3,091,695) | (1,047,180,229) | (1,050,271,924) | |
| Cash settlement of equity swaps over treasury shares (ii) | (48,810,043) | (1,464,301) | (470,661,618) | (472,125,919) | |
| Change in the nominal value of each share | | (6,604,800) | 6,604,800 | | |
| Balance as at 31 December 2007 | 35,242,929 | 1,057,288 | 322,121,625 | 323,178,913 | 9.17 |

- (i) This caption is net of an amount of Euro 28.5 million related to the reset of equity swaps over 20,640,000 of its own shares, since Portugal Telecom gave up the right to the dividends related to the spin-off of PT Multimédia attributable to the shares of the equity swaps.

- (ii) During 2007, equity swaps over 48,810,043 of its own shares were cash settled, having Portugal Telecom received an amount of Euro 32,188,194 (Note 17) resulting from the difference between the exercise price and the market price of Portugal Telecom's shares as of the dates of the financial settlement.

41.4. Legal reserve

Portuguese law provides that at least 5% of each year's profits must be appropriated to a legal reserve until this reserve equals the minimum requirement of 20% of share capital. This reserve is not available for distribution to shareholders but may be capitalized or used to absorb losses, once all other reserves and retained earnings have been exhausted. A portion of the legal reserve amounting to Euro 121,523,559 and Euro 79,019,955 was used in the share capital increases effective on 11 May 2006 and 22 May 2007, respectively. As at 31 December 2007, the legal reserve is already fully incorporated, corresponding to more than 20% of share capital.

41.5. Reserve for treasury shares

The reserve for treasury shares is related to the recognition of a non-distributable reserve equivalent to the nominal value of the shares cancelled or to the acquisition cost of treasury shares held by the Company. This reserve has the same legal regime as the legal reserve. The total reserve for treasury shares was used in the share capital increase effective on 11 May 2006, as approved at the Annual General Meeting of 21 April 2006. As at 31 December 2007, this reserve was related to shares cancelled on 20 December 2007.

41.6. Accumulated earnings

As at 31 December 2007 and 2006, this caption consisted of:

| | 2007 | 2006 |
|---|----------------------|----------------------|
| Income and expenses recognized directly in equity | | |
| Net actuarial losses (Notes 9.1 and 9.2) | (1,365,360,771) | (1,650,597,836) |
| Hedge accounting of financial instruments (Note 42.2) | (617,041) | 3,984,931 |
| Investments available for sale | | 22,968,096 |
| Cumulative foreign currency translation adjustments and other (i) | 839,593,851 | 637,337,339 |
| | (526,383,961) | (986,307,470) |
| Tax effect | 362,188,945 | 430,471,597 |
| | (164,195,016) | (555,835,873) |
| Reserves and retained earnings | 1,043,097,256 | 1,654,131,683 |
| Net income attributable to equity holders of the parent | 741,859,736 | 866,759,657 |
| | 1,620,761,976 | 1,965,055,467 |

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- (i) This caption includes mainly the translation adjustments of assets and liabilities denominated in foreign currencies as from 1 January 2004 up to the balance sheet date (Note 3.q)), and is mainly related to Portugal Telecom's investment in Brazil, whose currency translation adjustments amounted to Euro 875 million as at 31 December 2007, mainly related to the investment in Vivo.

42. Financial instruments**42.1. Financial risks**

Portugal Telecom is primarily exposed to (i) market risks related mainly to changes in foreign currency exchange rates and in interest rates, (ii) credit risks and (iii) liquidity risks. The main objective of Portugal Telecom's financial risk management is to reduce these risks to a lower level. Portugal Telecom enters into derivative financial instruments to manage its risk exposure to changes in interest rates and foreign currency exchange rates.

The contracting of these derivatives is made after careful analysis of associated risks and rewards, taking into consideration information obtained from different institutions. These transactions are subject to authorization from Portugal Telecom's Executive Committee. The positions held by the Company, as well as the relevant financial markets, are periodically monitored. The fair value of these derivatives is determined on a regular basis in order to assess the economic and financial implications of different scenarios.

Foreign currency exchange rate

Foreign currency exchange rate risks are mainly related to our investments in Brazil and other foreign countries, and to our debt denominated in currencies different from the functional currency of the country where the borrowing company operates.

As at 31 December 2007, the net exposure (assets minus liabilities) to Brazil amounted to R\$ 7,536 million (Euro 2,903 million at the Euro/Real exchange rate as at 31 December 2007), of which more than approximately 90% is related to our investment in Vivo.

The Group is also exposed to foreign currency exchange-rate risks related to debt denominated in foreign currencies different from the Group companies' functional currencies. As at 31 December 2007, these risks were basically related to:

- Debt denominated in US Dollars contracted by Portugal Telecom amounting to US\$ 43 million (Euro 29 million at the Euro/US Dollar exchange rate as at 31 December 2007), for which Portugal Telecom has contracted an exchange rate and interest rate derivative;
- Debt denominated in US Dollars contracted by Vivo amounting to US\$ 195 million (Euro 133 million), for which Vivo has contracted exchange and interest rate derivatives, which hedged more than 90% of this debt at that date.
- Debt denominated in Japanese Yenes contracted by Vivo amounting to ¥ 33,028 million (Euro 201 million), for which Vivo has contracted exchange rate and interest rate derivatives, which hedged 100% of the debt at that date.
- Debt denominated in Euro contracted by Vivo amounting to Euro 8 million, for which Vivo has contracted exchange rate and interest rate derivatives, which hedged 100% of this debt at that date.
- An exchange rate derivative contracted by Portugal Telecom with a notional of US\$ 218 million (put) and Euro 200 million (call). This derivative is classified in the balance sheet as a financial instrument held for trading, since it did not comply with the requirements to account for as a hedge financial instrument (Note 42.2).

As required by IFRS 7, the effects of hypothetical changes of relevant risk variables on income statement and shareholders' equity of Portugal Telecom are as follows:

- The impact of the appreciation (devaluation) of the Euro/Real exchange rate by 0.1 from 2.5963 to 2.4963 (2.6963), would be an increase (decrease) in Portugal Telecom's net assets as at 31 December 2007 by approximately Euro 116 million (Euro 108 million);
- The impact of the US Dollar appreciation (devaluation) against the Euro by 0.01 in Portugal Telecom's held for trading exchange rate derivative mentioned above, would be a decrease (increase) in net financial expenses amounting to approximately Euro 1 million (Euro 1 million);
- Most of non-derivative financial assets and liabilities (cash and cash equivalents, trade receivables and payables, and debt) are denominated in the functional currency either directly or indirectly through the use of derivatives. Therefore, changes in exchange rates would have no material effects on the income statement and shareholders' equity of the companies where those assets and liabilities are recorded.

Interest rate

Interest rate risks basically impact our financial expenses on the floating interest rate debt. Portugal Telecom is exposed to these risks primarily in the Euro zone and in Brazil (Vivo). With the purpose of reducing the impact of these risks, the Group has entered into interest-rate swaps, swapping floating rate into fixed rate debt.

As at 31 December 2007, 64.0% of the Company's debt was, directly or indirectly through the use of interest rate derivatives, set in fixed rates. The remaining 36.0% is exposed to changes in market interest rates. If all market interest rates had been higher (lower) by 1% during the year ended 31 December 2007, net interest expenses would have been higher (lower) by an amount of approximately 2.9 million (2.9 million).

The Group has also entered into some derivatives, which include an interest rate component, that are classified as held for trading derivatives, although its economic goal is to hedge currency or interest rate risk. If the market interest rates had been higher (lower) by 1% during the year ended 31 December 2007, interest expenses net of interest income in respect of these instruments would have been lower (higher) by an amount of approximately Euro 1.4 million (Euro 1.4 million).

Interest rate risks also results from the exposure to changes in the fair value of Portugal Telecom's long term fixed-rate debt due to changes in market interest rates.

Credit risk

Credit risk is related to the risk that a third party fails on its contractual obligations resulting in a financial loss to the Group. Portugal Telecom is subject to credit risks in its operating and treasury activities.

Credit risks in operations are basically related to outstanding receivables from services rendered to our customers (Notes 25 and 26). These risks are monitored on a business-to-business basis, and Portugal Telecom's management of these risks aims to: (a) limit the credit granted to customers, considering the profile and the aging of receivables of each customer; (b) monitor the evolution of the level of credit granted; (c) perform an impairment analysis of its receivables on a regular basis; and (d) assess the market risk where the customer is located. Accordingly, the criteria used to compute these adjustments is based on these risks.

The Group does not have any significant credit risk exposure to any single customer, since trade receivables consist of a large number of customers, spread across several businesses and geographical areas.

Adjustments for accounts receivable are computed taking into consideration primarily: (a) the risk profile of the customer, whether it is a corporate or a residential customer; (b) the aging of the receivables, which differs from business to business; (c) the financial condition of the customers; and (d) the market risk where the customer is located.

The movement of these adjustments for the year ended 31 December 2007 and 2006 is disclosed in Note 39. As at 31 December 2007, the Group believes that there was no further credit adjustment required in excess of the adjustments for accounts receivable included in Note 39.

As at 31 December 2007, approximately 20% of the Group's accounts receivables not adjusted for were already due with maturities above one hundred and eighty days.

Risks related to treasury activities result mainly from the cash investments made by the Group. In order to dilute these risks, Portugal Telecom's policy is to invest its cash for short time periods, entering in agreements with highly rated financial institutions and diversifying counterparties.

Liquidity risks

These risks may occur if the sources of funding, including operating cash inflows, divestments, credit lines and cash flows obtained from financing operations, do not match with our financing needs, such as operating and financing outflows, investments, shareholder remuneration and debt repayments.

In order to mitigate liquidity risks, the Group seeks to maintain a liquidity position and an average maturity of debt that allows it to repay its short-term debt and, at the same time, pay all its contractual obligations, as mentioned below. As at 31 December 2007, the amount of available cash plus the undrawn amount of Portugal Telecom's committed commercial paper lines (cash immediately available upon a 2-day notice) and Portugal Telecom's standby facilities totaled Euro 3,286 million. Excluding foreign businesses, this amount was Euro 2,672 million. As at 31 December 2007, Vivo had also available standby facilities in the amount of R\$ 1,160 million, of which no amount had been drawn at that date. The average maturity of Portugal Telecom's net debt as at 31 December 2007 is 6.7 years.

The capital structure of Portugal Telecom is managed in order to ensure that its businesses will be able to continue as a going concern and the maximizing of the return to stakeholders. The capital structure of the Group includes debt (Note 35), cash and cash equivalents, short-term investments (Note 24) and equity attributable to equity holders of the parent, comprising issued capital, treasury shares, reserves and accumulated earnings (Note 41). The Group reviews periodically its capital structure considering the risks associated with each of the above mentioned classes of the capital structure.

As at 31 December 2007, the gearing ratio, determined as the proportion of net debt (debt minus cash and cash equivalents and short-term investments) to net debt plus equity increased to 67.8%, from 54.7% as at 31 December 2006. The equity plus long-term debt to total assets ratio increased from 53.4% to 53.7% as at 31 December 2007.

The main contractual obligations are those related to indebtedness (Note 35) and related interest, post retirement benefits payments, operating leases (Note 13) and unconditional purchase obligations. The following table presents Portugal Telecom's expected contractual obligations and commercial commitments as at 31 December 2007:

| | Total | 2008 | 2009 | 2010 | 2011 | 2012 | More than five years |
|---|-----------------|----------------|----------------|--------------|--------------|----------------|-------------------------|
| Indebtedness | 6,216.8 | 1,256.1 | 1,122.5 | 226.3 | 159.8 | 1,282.2 | 2,169.9 |
| Interest on indebtedness (i) | 2,008.0 | 318.0 | 243.3 | 189.6 | 180.9 | 178.7 | 897.4 |
| Post retirement benefits payments (ii) | 1,327.0 | 203.8 | 193.6 | 179.9 | 139.4 | 115.2 | 495.1 |
| Operating lease obligations | 454.3 | 115.9 | 64.2 | 56.2 | 46.5 | 44.0 | 127.5 |
| Unconditional financial commitments (iii) | 478.8 | 216.9 | 23.8 | 23.8 | 55.5 | 31.8 | 127.1 |
| Total contractual obligations | 10,484.9 | 2,110.7 | 1,647.4 | 675.7 | 582.2 | 1,651.9 | 3,817.0 |

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- (i) Portugal Telecom's expected obligations related to interest on indebtedness are based on the Company's assumptions regarding interest rates on our floating rate debt, and therefore actual interest obligations could vary significantly from these amounts depending on market interest rates.
- (ii) These amounts correspond to the undiscounted payments to be made by Portugal Telecom related to salaries due to pre-retired and suspended employees and to expected contributions to the funds. The total amount differs from the net accrued post retirement liability recognized in the consolidated balance sheet primarily because this amount is related to the discounted unfunded obligations.
- (iii) As described in Note 43, unconditional purchase obligations arise generally related to (a) contractual agreements with our fixed asset suppliers (including all amounts related to the acquisition of network assets, telecommunications equipment and terminal equipments), (b) the remaining commitments related to the TMN's UMTS license and (c) the contractual agreement for the acquisition of a 3G license at Vivo.

42.2. Derivative financial instruments

Equity derivatives

In order to increase its exposure to PT Multimedia, Portugal Telecom contracted in previous years with a financial institution equity swaps over 30,575,090 shares of PT Multimedia, representing 9.9% of PTM's share capital, which were recorded on the balance sheet at fair value through profit and loss.

During the first half of 2007, a gain amounting to Euro 77,428,725 (Note 7.d) was booked in connection with the change in fair value of these equity swaps up to May 2007, when these equity swaps were cash settled, and as a result Portugal Telecom has received an amount of Euro 94,477,028 (Note 44.f).

Hedging financial instruments

Portugal Telecom analyses its financial instruments regularly in order to identify those that comply with the criteria established by IAS 39 to be classified as hedging instruments. As at 31 December 2007 and 2006, the following financial instruments were classified as cash flow and fair value hedges (amounts in millions of euros, including 100% of Vivo's financial instruments):

31 Dec 2007

Euro million

| Company | Notional amount | Transaction | Average maturity (years) | Economic goal |
|-------------------------|-----------------|-------------------------|--------------------------|---|
| Cash flow hedge | | | | |
| Portugal Telecom | 72.3 | EUR Interest rate swaps | 4.1 | Eliminate the risk of interest rate fluctuations in loans |
| Fair value hedge | | | | |
| Portugal Telecom | 28.9 | Currency swaps EUR/USD | 4.0 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 15.2 | Currency swaps EUR/BRL | 0.1 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 247.5 | Currency swaps USD/BRL | 2.2 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 400.6 | Currency swaps JPY/BRL | 0.7 | Eliminate the risk of exchange rate fluctuations in loans |

31 Dec 2006

Euro million

| Company | Notional amount | Transaction | Average maturity (years) | Economic goal |
|-------------------------|-----------------|------------------------------|--------------------------|---|
| Cash flow hedge | | | | |
| Portugal Telecom | 399.0 | EUR Interest rate swaps | 6.8 | Eliminate the risk of interest rate fluctuations in loans |
| Fair value hedge | | | | |
| Portugal Telecom | 40.3 | Cross currency swaps EUR/USD | 5.0 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 565.8 | Cross currency swaps BRL/USD | 0.8 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 320.4 | Cross currency swaps BRL/JPY | 1.3 | Eliminate the risk of exchange rate fluctuations in loans |

Financial instruments held for trading

As at 31 December 2007 and 2006, Portugal Telecom had contracted the following financial instruments which, according with IAS 39, are classified as held for trading derivatives (amounts in million of euros, including 100% of Vivo's financial instruments):

31 Dec 2007

Euro million

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| Company | Notional amount | Transaction | Average maturity (years) | Economic goal |
|--------------------|-----------------|-------------------------|--------------------------|--|
| Portugal Telecom | 27.4 | EUR interest rate swaps | 4.7 | Previous cash flow hedges |
| Portugal Telecom | 200.0 | EUR Call / USD Put | 1.3 | Restructure of previous derivative financial instruments |
| Cabo Verde Telecom | 1.2 | Currency swap EUR/USD | 1.9 | Eliminate the risk of exchange rate and interest rate fluctuations in loans |
| Vivo | 3.3 | Currency swaps USD/BRL | 1.3 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 42.4 | BRL Interest rate swaps | 2.1 | Hedge changes in fair value of loans due to changes in benchmark interest rate |
| Vivo | 422.8 | BRL Interest rate swaps | 0.1 | Eliminate the risk of interest rate fluctuations in loans |
| Vivo | 35.6 | USD Interest rate swaps | 0.5 | Eliminate the risk of interest rate fluctuations in loans |
| Mobitel | 17.2 | Currency swaps USD/BRL | 2.4 | Eliminate the risk of exchange rate fluctuations in loans |

31 Dec 2007

Euro million

| Company | Notional amount | Transaction | Average maturity (years) | Economic goal |
|--------------------|-----------------|--------------------------------------|--------------------------|--|
| Portugal Telecom | 251.6 | EUR Interest rate swaps | 5.5 | Instruments resulting from previous hedgings |
| Portugal Telecom | 200.0 | EUR Call / USD Put | 2.3 | Restructure of previous derivative financial instruments |
| Portugal Telecom | 275.8 | Equity swaps on PT Multimedia shares | 1.6 | Increase exposure to PT Multimedia |
| Cabo Verde Telecom | 2.1 | Cross currency swap EUR/USD | 2.9 | Eliminate the risk of exchange rate and interest rate fluctuations in loans |
| Vivo | 12.5 | Cross currency swaps BRL/USD | 1.0 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 1.9 | Cross currency swaps BRL/EUR | 0.4 | Eliminate the risk of exchange rate fluctuations in loans |
| Vivo | 875.8 | BRL Interest rate swaps | 0.5 | Hedge changes in fair value of loans due to changes in benchmark interest rate |
| Vivo | 176.5 | USD Interest rate swaps | 0.8 | Hedge changes in fair value of loans due to changes in benchmark interest rate |
| Mobitel | 16.6 | Cross currency swaps BRL/USD | 3.3 | Eliminate the risk of exchange rate fluctuations in loans |

Fair value of financial instruments

The movement in the fair value of derivatives during 2007 and 2006 was as follows (amounts in millions of euros):

| | Balance 31 Dec 2006 | Fair value adjustment Income | Reserves | Additions and settlements | Foreign currency translation adjustments and other | Balance 31 Dec 2007 |
|--|------------------------|---------------------------------|--------------|---------------------------------|--|------------------------|
| Fair value hedges | | | | | | |
| Exchange rate and interest rate (i) | (94.1) | (97.4) | | 103.2 | (5.7) | (94.0) |
| Derivatives held for trading | | | | | | |
| Exchange rate (ii) | (35.0) | (11.5) | | | | (46.5) |
| Exchange rate and interest rate | (11.2) | (1.7) | | 2.2 | (3.0) | (13.7) |
| Interest rate | (7.4) | (0.2) | | 8.2 | 0.1 | 0.8 |
| Equity swaps over PT Multimedia shares (Notes 7.d and 44.f) | 17.0 | 77.4 | | (94.5) | | |
| Cash flow hedges | | | | | | |
| Interest rate (Note 40.6) | 4.0 | 8.3 | (4.6) | (8.3) | | (0.6) |
| | (126.7) | (25.1) | (4.6) | 10.9 | (8.6) | (154.1) |

(i) This caption includes a liability of Euro 11 million recorded at Portugal Telecom, which has an average maturity of 4.0 years and a liability of Euro 83 million recorded at Vivo with an average maturity of 1.5 years.

(ii) This liability has a maturity of 1.3 years.

| | Balance 31 Dec 2005 | Fair value adjustment Income | Reserves | Additions and settlements | Foreign currency translation adjustments and other | Balance 31 Dec 2006 |
|---|------------------------|---------------------------------|-------------|---------------------------------|--|------------------------|
| Fair value hedges | | | | | | |
| Interest rate and exchange rate | (122.3) | (125.1) | | 151.3 | 2.0 | (94.1) |
| Derivatives held for trading | | | | | | |
| Exchange rate | (26.6) | (8.4) | | | | (35.0) |
| Exchange rate and interest rate | 36.3 | (9.5) | | (38.3) | 0.3 | (11.2) |
| Interest rate | (5.3) | (3.7) | | 1.7 | (0.0) | (7.4) |
| Equity swaps over PT Multimedia shares (Note 44.f) | 42.0 | 1.8 | | (26.8) | | 17.0 |
| Cash flow hedges | | | | | | |
| Interest rate | (21.6) | 7.0 | 25.6 | (7.0) | | 4.0 |
| | (97.6) | (137.9) | 25.6 | 81.0 | 2.2 | (126.7) |

In 2007 and 2006, the fair value adjustments related to derivatives were recorded in the following income statement captions (amounts in millions of euros):

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| | 2007 | | | 2006 | | | | |
|--|----------------------|---|---|--------|----------------------|---|---|-------|
| | Net interest expense | Net foreign currency exchange losses/ (gains) | Net losses/ (gains) on financial assets (Note 17) | Total | Net interest expense | Net foreign currency exchange losses/ (gains) | Net losses/ (gains) on financial assets (Note 17) | Total |
| Fair value hedges | | | | | | | | |
| Interest rate and exchange rate | 42.8 | 54.6 | | 97.4 | 69.0 | 56.1 | | 125.1 |
| Derivatives held for trading | | | | | | | | |
| Exchange rate | | | 11.5 | 11.5 | | | 8.4 | 8.4 |
| Exchange rate and interest rate | | 3.8 | (2.1) | 1.7 | | 5.4 | 4.1 | 9.5 |
| Interest rate | | | 0.2 | 0.2 | | | 3.7 | 3.7 |
| Equity swaps over PT Multimedia shares | | | (77.4) | (77.4) | | | (1.8) | (1.8) |
| Cash flow hedges | | | | | | | | |
| Interest rate | (8.3) | | | (8.3) | (7.0) | | | (7.0) |
| | 34.6 | 58.4 | (67.8) | 25.1 | 62.0 | 61.4 | 14.4 | 137.9 |

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As at 31 December 2007, the derivatives contracted by the Company recognized at fair value were recorded in the following balance sheet captions (amounts in millions of euros):

| | Assets | | Liabilities Accrued expenses (Note 37) | Other liabilities (Note 40) | Total |
|-------------------------------------|---------------------------|---------------|---|-----------------------------------|----------------|
| | Short term investments | Debt | | | |
| Fair value hedges | | | | | |
| Exchange rate and interest rate | | (49.3) | (44.7) | | (94.0) |
| Derivatives held for trading | | | | | |
| Exchange rate | | | | (46.5) | (46.5) |
| Exchange rate and interest rate | | | (13.7) | | (13.7) |
| Interest rate | 1.5 | | | (0.7) | 0.8 |
| Cash flow hedges | | | | | |
| Interest rate | | | | (0.6) | (0.6) |
| | 1.5 | (49.3) | (58.4) | (47.8) | (154.1) |

As at 31 December 2006, the derivatives contracted by the Company recognized at fair value were recorded in the following balance sheet captions (amounts in millions of euros):

| | Assets | | | Liabilities Accrued expenses (Note 37) | Other liabilities (Note 40) | Total |
|---|---------------------------|---------------------------|---------------|---|-----------------------------------|----------------|
| | Short term investments | Other assets (Note 30) | Debt | | | |
| Fair value hedges | | | | | | |
| Exchange rate and interest rate | | | (35.6) | (58.5) | | (94.1) |
| Derivatives held for trading | | | | | | |
| Exchange rate | | | | | (35.0) | (35.0) |
| Exchange rate and interest rate | | | | (11.2) | | (11.2) |
| Interest rate | 1.7 | | | | (9.0) | (7.4) |
| Equity swaps over PT Multimedia shares | | 17.0 | | | | 17.0 |
| Cash flow hedges | | | | | | |
| Interest rate | | 4.0 | | | | 4.0 |
| | 1.7 | 21.0 | (35.6) | (69.7) | (44.0) | (126.7) |

42.3. Other disclosures on financial instruments

The carrying amounts of each of the following categories, as defined in IAS 39, were recognized as follows (amounts in millions of euros):

| Caption | 2007 | 2006 |
|---|-----------|-----------|
| Financial assets carried at amortised cost | | |
| Cash and cash equivalents | 664.6 | 548.5 |
| Short-term investments (Note 24) | 1,170.3 | 1,535.2 |
| Accounts receivable - trade (Note 25) | 1,308.7 | 1,182.8 |
| Accounts receivable - other (i) | 101.7 | 201.9 |
| Other current and non-current assets - QTE transactions (Note 30) | 505.5 | 673.8 |
| Investments in group companies - loans (Note 31) | 95.2 | 102.0 |
| | 3,846.0 | 4,244.2 |
| Financial assets carried at fair value through profit and loss | | |
| Other non-current assets - held for trading derivatives (Note 42.2) | | 17.0 |
| Derivatives designated and effective as hedging instruments carried at fair value | | |
| Other non-current assets/(liabilities) - interest rate derivatives - cash flow hedges (Note 42.2) | (0.6) | 4.0 |
| Bank loans - exchange and interest rate derivatives - fair value hedges (Note 42.2) (ii) | (49.3) | (35.6) |
| Accrued expenses - exchange and interest rate derivatives - fair value hedges (Note 42.2) (iii) | (44.7) | (58.5) |
| | (94.6) | (90.1) |
| Available-for-sale investments carried at fair value | | |
| Other investments (Note 32) | | 99.7 |
| Financial liabilities carried at amortised cost | | |
| Debt - exchangeable bonds (Note 35) | (689.4) | |
| Debt - bonds (Note 35) | (3,158.0) | (3,133.6) |
| Debt - bank loans (ii) | (1,322.9) | (1,474.6) |
| Debt - other loans (Note 35) | (324.0) | (750.1) |
| Debt - UMTS license (Note 35) | (200.6) | |
| Debt - equity swaps on treasury shares (Note 35) | (323.2) | (187.6) |
| Accounts payable (Note 36) | (1,108.9) | (1,115.1) |
| Accrued expenses | (582.7) | (610.5) |
| Other current liabilities | (32.0) | (36.2) |
| | (7,741.5) | (7,307.8) |
| Derivatives held for trading | | |
| Accrued expenses - Exchange rate and interest rate derivatives (Note 42.2) | (13.7) | (11.2) |
| Other non-current liabilities - Exchange rate derivatives (Note 42.2) | (46.5) | (35.0) |
| Other non-current liabilities - Interest rate derivatives (Note 42.2) | (0.7) | (9.0) |
| | (60.9) | (55.3) |
| Financial liabilities recorded according to IAS 17 | | |
| Debt - finance leases (Note 35) | (149.5) | (258.6) |
| Other current and non-current liabilities - QTE transactions (Note 40) | (505.5) | (673.8) |
| | (654.9) | (932.4) |

- (i) The balance sheet caption "Accounts receivable - other" includes certain assets, such as trial deposits, which do not meet the requirements to be classified as a financial asset, and therefore were excluded from this caption.

- (ii) Total bank loans include its notional amounts which were carried at amortised cost and the fair value of certain exchange and interest rate derivatives.

Except for debt, whose fair value is disclosed in Note 35, and for derivatives, which are recorded at fair value, as mentioned in Note 42.2, the fair value of the remaining financial assets and liabilities is similar to their carrying amounts. The fair value of derivatives and debt of domestic businesses is based on external valuations, while the fair value of derivatives and debt of Vivo is based on internal valuations computed based on discounted cash flows method.

43. Guarantees and financial commitments

As at 31 December 2007, the Company has presented guarantees and comfort letters to third parties, as follows:

| | |
|--|-------------------|
| Bank guarantees and other guarantees given to Tax Authorities | 47,706,622 |
| Bank guarantees given to Portuguese courts for outstanding litigation | 1,671,428 |
| Bank guarantees given to other entities | |
| On behalf of TMN | 35,566,299 |
| On behalf of PT Comunicações | 9,276,796 |
| Other bank guarantees | 8,873,652 |
| | 53,716,747 |
| Comfort letters given to other entities | 2,770,859 |

Bank guarantees given on behalf of TMN include a guarantee presented in connection with cross-border lease transactions contracted by TMN (Note 34) and guarantees presented to ANACOM related to TMN's obligations under the UMTS licenses acquired in December 2000. Bank guarantees given on behalf of PT Comunicações were presented to Municipal Authorities and are mainly related to the repayment of taxes and other fees in connection with Portugal Telecom's use of public rights-of-way.

As at 31 December 2007, the Company had also assumed the following financial commitments, in addition to those recorded in the financial statements:

(a) In June 2006, Médi Télécom entered into a medium and long-term contract with a consortium of Moroccan banks, for a total amount of Euro 544 million. The funds raised were used to repay all the medium and long term debt, denominated in foreign currencies, previously issued under loan contracts entered into with a consortium led by International Finance Corporation and the banks ABN Amro and Société Générale.

As was the case under the loans repaid, under the provisions of the new loan agreements, Médi Télécom is required to attain certain financial performance levels. In accordance with the financing transaction, the major shareholders of Médi Télécom, Portugal Telecom, through PT Móveis (32.18%), Telefónica Móviles España (32.18%) and Banque Marocaine du Commerce Extérieur (17.59%), signed a Shareholders Support Deed, under which they are committed to make future capital contributions to Médi Télécom (in the form of capital or

shareholders' loans), if this is necessary to cover possible shortfalls in the agreed financial targets. On October 2006, the other shareholders of Médi Télécom also signed the Shareholders Support Deed.

Under this agreement, these parties committed to make contributions (capital subscription or loans), proportional to their stakes in the company, up to a total of Euro 168 million, of which Euro 50 million are related to the repayment of debt, and ends as soon as Médi Télécom reaches a Net Debt/EBITDA ratio of less than 2.0. As at 31 December 2007, following the renegotiation of the Shareholders Support Deed during 2006, the maximum liability to Portugal Telecom amounts to Euro 54 million, which is proportional to its stake in Médi Télécom.

(b) Portugal Telecom signed a Shareholders' Agreement with the other shareholders of Sportinveste Multimédia, in which Portugal Telecom committed to give additional paid-in capital contributions up to a maximum of Euro 40,000,000. As at 31 December 2007, Portugal Telecom had already granted additional paid in capital contributions to Sportinveste Multimédia amounting to Euro 30,023,168 (Note 31).

(c) Under the purchase agreement for the UMTS license, TMN has committed to make contributions of Euro 95 million for the development of the information society in Portugal during the period through the maturity of the license (2015).

(d) As at 31 December 2007, the Group had assumed purchase commitments to suppliers amounting to Euro 172 million, essentially related to equipment.

(e) Vivo was the winning bidder for the acquisition of a 3G license, after price bids were opened at the head-office of Anatel, in the Band J lots, with 10+10MHz width, with exception of lots VII and X. Vivo offer, for all Band J lots acquired, was approximately R\$ 1, 1 billion for a period of 15 years with possibility of one extension up to 15 additional years. At least 10% of it should be paid at the time of the execution of the Terms of Authorization. The balance that is left unpaid 90% may be paid in six equal and annual installments, with a grace period of three years. The Official Result of the Auction will be disclosed by Anatel in 2008 and contracts will only be executed within up to ten days after the referred publication.

As at 31 December 2007, the guarantees given by third parties on behalf of the Company, in connection with bank loans (Note 35), were as follows:

| | |
|---|-------------|
| - Guarantees in favor of European Investment Bank | 120,361,001 |
| - Guarantee from the Portuguese State to Kreditanstalt Für Wiederaufbau | 4,752,458 |

As at 31 December 2007, Portugal Telecom had bank deposits amounting to Euro 24 million the use of which was restricted due to the cross-border lease transactions entered into by the Group (Note 34). As at the same date, Vivo had tangible assets and financial applications given as guarantees for legal proceedings that amounted to Euro 21 million and Euro 47 million, respectively.

44. Statement of cash flows

- (a) The increase in payments related to income taxes is primarily explained due to full utilization of tax losses carried forward from Portugal Telecom's tax consolidation group at the end of 2006, following which Portugal Telecom has paid income taxes in 2007 amounting to approximately Euro 170 million.
- (b) The caption Payments relating to indirect taxes and other includes primarily payments related to the expenses recorded in the income statement caption Indirect taxes (Note 14), and also payments and collections of Value-Added Tax in Portugal.
- (c) These captions include basically cash payments from new short term financial applications entered into and cash receipts from the short term applications matured. Net cash receipts amounting to Euro 364,940,527 and Euro 1,764,028,679 in 2007 and 2006, respectively, are mainly related with the movements occurred in loans obtained (Note 44.h). The decrease in net cash receipts resulting from short-term financial applications, is basically related to the reduction in net cash payments from loans repaid.

(d) During the years ended 31 December 2007 and 2006, cash receipts resulting from financial investments were as follows:

| | 2007 | 2006 |
|----------------------|--------------------|------------------|
| Africatel (Note 17) | 116,999,817 | |
| BES (Note 32) | 110,318,600 | |
| Telefónica (Note 32) | 5,107,941 | |
| TV Cabo Macau | 3,108,957 | |
| Directel Macau | 1,209,122 | |
| Iris Capital Fund | | 2,328,287 |
| Other | 2,902,469 | 107,048 |
| | 239,646,906 | 2,435,335 |

(e) During the years ended 31 December 2007 and 2006, cash receipts resulting from dividends were as follows:

| | 2007 | 2006 |
|----------------------|-------------------|-------------------|
| Unitel (i) | 72,949,311 | 15,024,110 |
| CTM | 16,222,842 | 15,038,429 |
| Banco Espírito Santo | 2,632,000 | 1,344,000 |
| Páginas Amarelas | 2,434,000 | 2,283,714 |
| Other | 561,767 | 577,564 |
| | 94,799,920 | 34,267,817 |

(i) In 2007, this caption includes the dividends received from Unitel related to its earnings of 2006 and 2005 amounting to Euro 46 million and Euro 27 million (Note 26), respectively. In 2006, this caption includes the dividends received from Unitel related to its earnings of 2004.

(f) In 2007, the caption Cash receipts resulting from other investing activities includes mainly Euro 94,477,028 related to the cash settlement of equity swaps over shares of PT Multimedia (Note 42) and Euro 32,188,194 related to the cash settlement of equity swaps over Portugal Telecom's treasury shares (Note 17). In 2006, this caption includes primarily Euro 26,772,985 related to equity swaps over shares of PT Multimedia (Note 42), and an amount of Euro 23,513,275 related to the financial settlement of equity swaps over Portugal Telecom's treasury shares (Note 17).

(g) During the years ended 31 December 2007 and 2006, payments resulting from financial investments were as follows:

| | 2007 | 2006 |
|---------------|------------------|-------------------|
| Siresp | 1,466,516 | |
| MTC (i) | | 57,489,375 |
| BES (ii) | | 19,320,000 |
| Web-Lab (iii) | | 6,418,036 |
| Mobitel (iv) | | 3,574,460 |
| Other | 1,876,021 | 6,372,334 |
| | 3,342,537 | 93,174,205 |

(i) This caption includes Euro 108,648,089 paid from the acquisition of a 34% stake in the share capital of MTC, net of an amount of Euro 51,158,714 related to cash and cash equivalents of MTC as at 1 September 2006, the date on which this company was included for the first time in the consolidation perimeter.

(ii) This caption is related to Portugal Telecom's share in the capital increase of Banco Espírito Santo occurred in 2006.

(iii) This caption corresponds to the acquisition by Portugal Telecom of the remaining 10% stake in the share capital of Web-Lab from the former shareholders of this company.

(iv) During 2006, PT Brasil acquired the remaining 4.26% stake in Mobitel. As a result, PT Brasil now owns 100% of Mobitel.

(h) These captions are basically related to commercial paper and other bank loans which are regularly renewed.

In 2007, cash receipts from loans obtained net of cash payments from loans repaid amounted to Euro 223,459,521.

In 2006, cash payments from loans repaid net of cash receipts from loans obtained amounted to Euro 1,733,486,143, and included primarily: (i) Euro 899,500,000 related to the repayment of the notes issued by PT Finance on 21 February 2001; (ii) Euro 460,000,000 related to the partial repayment of the Multicurrency Credit Facility entered into in 2003; and (iii) Euro 390,335,000 related to the repayment of convertible bonds issued by PT Finance in December 2001.

(i) During the years ended 31 December 2007 and 2006, the Group payments regarding dividends were as follows:

| | 2007 | 2006 |
|------------------------------------|--------------------|--------------------|
| Portugal Telecom (Notes 22 and 41) | 516,506,816 | 526,402,838 |
| MTC | 12,275,947 | 13,095,694 |
| Africatel | 11,225,634 | |
| Cabo Verde Telecom | 7,519,738 | 6,011,557 |
| Other | 5,198,833 | 6,698,263 |
| | 552,726,968 | 552,208,352 |

(j) During the years ended 31 December 2007 and 2006, the caption Other payments resulting from financing activities includes respectively Euro 43 million and Euro 68 million related to payments made by Vivo in connection with exchange rate derivatives.

45. Related parties

a) Associated companies and jointly controlled entities

Balances as at 31 December 2007 and 2006 and transactions occurred during 2007 and 2006 between Portugal Telecom and associated companies and jointly controlled entities (related to the 50% share not owned by the Portugal Telecom in Vivo) are as follows:

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| Company | Loans granted (Note 31) | | Accounts receivable | | Accounts payable | |
|-------------------------|-------------------------|--------------------|---------------------|-------------------|-------------------|-------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Médi Télécom | 72,112,464 | 68,106,243 | 6,850,319 | 11,182,595 | 1,604,300 | 2,187,396 |
| Sportinveste Multimédia | 35,318,668 | 35,318,668 | 320,422 | 68,094 | | |
| Inesc (i) | 3,292,066 | 3,292,066 | 490,756 | 502,718 | 13,738 | |
| Siresp | 2,302,230 | 980,951 | 3,752,822 | 1,756,418 | | 21,000 |
| Multitel | 918,459 | 73,212 | 3,514,930 | 3,312,295 | 180,935 | 356,141 |
| Unitel (ii) | 339,651 | 379,651 | 7,559,522 | 38,419,763 | 2,708,033 | 67,147 |
| Sport TV | | 12,500,000 | | 3,262,598 | | 8,786,037 |
| Vivo | | | 23,466,477 | 11,883,846 | 92,701 | 100,295 |
| Páginas Amarelas | | | 10,974,342 | 9,286,412 | 43,817,942 | 50,104,723 |
| Caixanet | | | 3,233,842 | 3,949,043 | | |
| PT-ACS | | | 1,618,869 | 1,795,715 | 341,132 | 4,647,135 |
| Guiné Telecom | | | 653,805 | 3,403,513 | 2,366,124 | 6,048,598 |
| Fundação PT | | | 554,192 | 3,357,638 | | |
| Octal TV | | | | 421,888 | | 7,533,309 |
| Lisboa TV | | | | 101,841 | | 6,045,831 |
| Other companies | 746,034 | 607,487 | 6,068,308 | 4,864,390 | 1,361,164 | 2,445,304 |
| | 115,029,572 | 121,258,278 | 69,058,606 | 97,568,767 | 52,486,069 | 88,342,916 |

(i) Loans granted to this company were fully provided for.

(ii) Accounts receivable from Unitel as at 31 December 2006 include dividends receivable of Euro 27 million (Note 26).

| Company | Costs | | Revenues | | Interest obtained | |
|-------------------------|-------------------|--------------------|--------------------|-------------------|-------------------|------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Páginas Amarelas | 62,873,287 | 65,140,640 | 2,508,598 | 2,693,756 | | |
| PT-ACS | 5,852,155 | 14,863,053 | 577,805 | 431,526 | | |
| Unitel | 8,176,711 | 9,384,922 | 13,743,098 | 15,426,658 | 25,598 | |
| Médi Télécom | 8,759,660 | 8,454,156 | 10,288,272 | 6,741,641 | 2,878,902 | 2,619,304 |
| Guiné Telecom | 832,311 | 1,230,690 | 1,411,566 | 1,381,694 | | |
| Sportinveste Multimédia | 950,233 | 1,156,493 | 331,263 | 598,599 | | |
| Intelsat | 1,314,303 | 1,052,877 | | | | |
| Caixanet | 506,036 | 189,704 | 9,654,715 | 12,265,075 | | |
| CTM | 176,371 | 121,187 | 344,010 | 241,088 | | |
| Vivo | | | 54,557,592 | 46,277,328 | | |
| Other companies | 693,176 | 2,021,381 | 16,882,899 | 6,530,124 | 334,708 | 60,954 |
| | 90,134,243 | 103,615,103 | 110,299,818 | 92,587,489 | 3,239,208 | 2,680,258 |

The terms and contractual conditions in agreements entered by Portugal Telecom and subsidiaries are similar to those applicable to other independent entities in similar transactions. Activities developed in connections with those agreements include mainly:

- Call center services rendered by Mobitel to Vivo;
- Expenses incurred by PT Comunicações related to services rendered by Páginas Amarelas in connection with the agreement entered into by both entities, under which Páginas Amarelas is responsible for production, publishing and distribution of PT Comunicações telephone

directories, as well as selling advertising space in the directories.

b) Shareholders

Some of the major shareholders of Portugal Telecom are financial institutions and, in the ordinary course of business, Portugal Telecom entered into various transactions with those entities. Transactions occurred during 2007 and balances as at 31 December 2007 between Portugal Telecom and its major shareholders are as follows(including VAT):

| Company | Services rendered and sales | Acquisitions | Interest and related expenses obtained and (paid) | Accounts receivable | Accounts payable |
|--------------------------------|-----------------------------|--------------------|---|---------------------|-------------------|
| Caixa Geral de Depósitos Group | 34,598,987 | 4,725,489 | 4,430,690 | 7,250,860 | 151,343 |
| Visabeira Group | 28,838,011 | 74,637,100 | | 15,259,295 | 23,648,630 |
| BES Group | 26,998,873 | 38,724,440 | 13,518,034 | 4,421,339 | 158,244 |
| Barclays | 233,439 | 9,986 | (17,017,283) | 180,224 | |
| Controlinveste | 127,995 | 3,127,783 | | 61,728 | 278,300 |
| | 90,797,305 | 121,224,798 | 931,441 | 27,173,446 | 24,236,517 |

The terms and contractual conditions in agreements entered by Portugal Telecom and shareholders are similar to those applicable to other independent entities in similar transactions. Under these agreements, the financial institutions listed above rendered financial consultancy and insurance services.

In connection with the incorporation of Brasilcel, Portugal Telecom and Telefónica entered into a strategic agreement, which allows Portugal Telecom to acquire up to 1.5% of Telefónica's share capital and Telefónica to acquire up to 10% of Portugal Telecom's share capital. As at 31 December 2007, Telefónica held 9.16% of Portugal Telecom's share capital.

Portugal Telecom entered into a Shareholders' Agreement with Telefónica to manage Vivo and is party to certain international traffic agreements with Telefónica Group companies, which have substantially the same conditions as similar agreements with independent parties.

c) Other

During the years ended 31 December 2007 and 2006, the remunerations of executive and non-executive board members, which were established by the Remunerations Committee, are as follows:

| | 2007 | | | 2006 | | |
|-----------------------------|------------------|---------------------|----------------------------|------------------|---------------------|----------------------------|
| | Fixed | Performance Plan | Variable Non- recurring | Fixed | Performance Plan | Variable Non- recurring |
| Executive board members | 4,039,271 | 3,692,969 | 5,480,331 | 4,669,866 | 3,812,872 | 9,705,048 |
| Non-executive board members | 1,280,272 | | | 1,611,589 | 299,639 | 966,876 |
| | 5,319,543 | 3,692,969 | 5,480,331 | 6,281,455 | 4,112,511 | 10,671,924 |

The variable component of remunerations of the Board of Directors include extraordinary payments to board members, namely indemnities, termination payments, extraordinary bonus proposed by reference shareholders and approved by the Remunerations Committee and hiring bonus. In 2007, indemnities amounted to approximately Euro 500 thousand.

During the years ended 31 December 2007 and 2006, fixed remuneration of key employees of the Portugal Telecom Group management amounted to Euro 7,093,734 and Euro 8,346,129, respectively, and variable remuneration amounted to Euro 4,554,000 and Euro 3,851,016, respectively.

The fixed and variable remunerations of the Portugal Telecom Group officers, as described under paragraph 3 of article 248-B of the Portuguese Securities Code, are determined within each Group's operating company, through a compensation committee composed by four directors of Portugal Telecom and its Corporate Officer with responsibilities concerning Human Resources. As to the determination of the fixed remunerations, an internal harmonisation procedure has been carried out, taking into account each officer's functions and the companies where such functions have been performed, and a benchmark with similar companies has also been done. Officers' variable remunerations are determined by the above mentioned compensation committees of the operating subsidiary companies based on such companies' results taking into account both quantitative indicators, namely operational (such as ARPU, Churn and Net Adds) and financial (such as EBITDA, CAPEX and OPEX) and qualitative indicators (such as management and leadership), which are weighted as a whole together with the functions performed by the officer and the importance of the operating company within the Portugal Telecom Group.

In addition to the above mentioned remunerations, Executive Board members and key employees are also entitled to fringe benefits that are primarily utilized in their daily functions, in connection with a policy defined for the Portugal Telecom Group, and some of them are also entitled to post retirement benefits under the plans of PT Comunicações, as described in Note 9.

One of Portugal Telecom's non-executive board members is executive director of Heidrick & Struggles - Consultores de Gestão, Lda, which during the normal course of business rendered consultancy services to Portugal Telecom amounting to approximately Euro 3.6 million.

46. Litigation

46.1. Regulatory authorities

a) Claims for municipal taxes and fees

Pursuant to a statute enacted on 1 August 1997, as an operator of a basic telecommunications network, Portugal Telecom was exempt from municipal taxes and rights-of-way and other fees with respect to its network in connection with its obligations under the Concession. The Portuguese Government has advised Portugal Telecom in the past that this statute confirmed the tax exemption under our Concession. The Portuguese Government has advised Portugal Telecom it will continue to take the necessary actions in order for PT Comunicações to maintain the economic benefits contemplated by the Concession. At this time, Portugal Telecom cannot be sure that the Portuguese courts will accept that this statute resolves claims for municipal assessments and taxes for the period prior to its enactment.

In 1999, the municipality of Oporto filed a lawsuit claiming the repayment of taxes and other fees in connection with the use by PT Comunicações of public rights-of-way in 1998. The Lower Tax Court of Oporto ruled in favor of PT Comunicações in March 2003, declaring the regulations of the Municipality of Oporto, under which such taxes and other fees were deemed to be owed by PT Comunicações, to be unconstitutional. The Municipality of Oporto subsequently appealed this decision to the Administrative Central Court, and then PT Comunicações submitted its response thereto. This appeal is pending before the Administrative Central Court.

If this claim is upheld against PT Comunicações, other municipalities might seek to make or renew claims against PT Comunicações. Portuguese law provides for a four-year statute of limitations for claims for taxes or other similar governmental charges. The statute of limitation for taxable events that occurred prior to 1 January 1998 is five years.

Since the statute of limitations for such claims has expired, Portugal Telecom do not expect that any further claims will be made against PT Comunicações, but Portugal Telecom cannot be certain about this.

Law 5/2004 of 10 February 2004 established a new rights-of-way regime in Portugal whereby each municipality may establish a fee, up to a maximum of 0.25% of each wireline services bill, to be paid by the customers of those wireline operators whose network infrastructures are located in each such municipality. This regime was implemented in 2005 but does not affect the lawsuit described above pursuant to the former statute.

Some municipalities however, continue to persist that the Law 5/2004 of February 10th 2004 does not expressly revoke other taxes that the municipalities wish to establish, because the Law 5/2004 is not applicable to the public municipality domain, as well as to the private municipality domain, but instead it is applicable to the public federal domain, as well as to the private federal domain and to regional public domain, as well as to the private regional domain.

Presently there exists a claim between the Municipality of Seixal and PT Comunicações, and we believe that the same will occur with the Municipality of Aveiro.

b) Regulatory Proceedings

Portugal Telecom Group companies are regularly involved in regulatory inquiries and investigations involving their operations. In addition, ANACOM, the European Commission, and the Autoridade da Concorrência regularly make inquiries and conduct investigations concerning compliance with applicable laws and regulations. Current inquiries and investigations include several investigations by the Autoridade da Concorrência related to (i) PT.com (this complaint was formerly against Telepac, which merged with PT.com in December 2004); and (ii) PT Comunicações for alleged anti-competitive practices in the public wireline telephone market and for granting discriminatory discounts on leased lines. Portugal Telecom considers that group companies have consistently followed a policy of compliance with all relevant laws. The Group continually reviews commercial offers in order to reduce the risk of competition law infringement. The Group believes that most of the complaints that have resulted in such investigations should be dismissed due to the nature of the alleged abuses and the novelty of the relevant competition laws. However, if group companies are found to be in violation of applicable laws and regulations in these or other regulatory inquiries and investigations, they could become subject to penalties, fines, damages or

other sanctions. It is however permitted under Portuguese law to appeal any adverse decision to the Courts. The appeal will suspend the decisions of Autoridade da Concorrência.

In 2004, the Autoridade da Concorrência initiated a proceeding against PT Comunicações, referred to as a statement of objections, alleging that PT Comunicações was denying access to the ducts in which the basic telecommunications network is installed. In June 2005, the Autoridade da Concorrência issued a revised statement of objections on this matter. PT Comunicações has responded to this statement of objections and does not believe it has violated applicable law and regulations. However, on 1 August 2007, the Autoridade da Concorrência imposed a fine of Euro 38 million on PT Comunicações. PT Comunicações appealed to the Commerce Court of Lisbon, on 30 August 2007. This appeal suspends the decision of Autoridade da Concorrência.

In April 2007, the Autoridade da Concorrência accused PT Comunicações of alleged abuse of dominant position for granting discriminatory discounts on lease lines. In response to this accusation, PT Comunicações contested the alleged by the Autoridade da Concorrência. PT Comunicações is permitted under Portuguese law to appeal any adverse decision of the Autoridade da Concorrência to the Courts. The appeal suspends the decision of the Autoridade da Concorrência.

On 8 June 2005, Portugal Telecom was informed through the press that Sonaecom, SGPS, SA (Sonaecom a competitor of Portugal Telecom) had filed a complaint against it with the European Commission, under article 82 of the EU Treaty, alleging abuse of dominant position in the Portuguese market in connection with the Company's provision of fixed line services through the subsidiary PT Comunicações. Sonaecom requested that the European Commission require Portugal Telecom to separate its cable television and fixed line telecommunications operations a so-called structural remedy. However, on 2 February 2006 the Commission responded that the complaint should be addressed to the Portuguese Autoridade da Concorrência. To Portugal Telecom knowledge, proceedings before the European Commission related to this complaint are now closed. Portugal Telecom has not received further information about whether Sonaecom intends to pursue this matter with the Autoridade da Concorrência, following the spin-off of the PT Multimédia business.

Sonaecom has also submitted a complaint to the European Commission alleging illegal state aid in connection with the Portuguese Government's sale of the basic telecommunications network to PT Comunicações in 2002 and the exemption from the payment of municipal taxes granted to PT Comunicações as part of its Concession Agreement.

Sonaecom is claiming that the purchase price for the basic network was below market value, thereby adversely affecting the Portuguese State. Sonaecom also claims that the absence of a public tender offer and the absence of independent valuations to set a minimum disposal price constituted state aid. Pursuant to its Concession Agreement, PT Comunicações was exempted from the payment of municipal taxes from 1995 until such exemption was revoked by Law 5/2004 of 10 February 2004. This is in contrast to the situation affecting new telecommunications operators after the liberalization of the telecoms market in 2000. In order for new operators to build their infrastructure, they were required to pay municipal taxes for the use of municipal sub-soil. Sonaecom claims this discrimination against new operators represents a case of illegal state aid which harmed both new operators and the municipalities. Portugal Telecom have not received information from the European Commission or the Portuguese authorities regarding this complaint.

In April 2006, the European Commission sent a formal request to the Portuguese Government to abandon the special rights it holds as the sole owner of Portugal Telecom's Class A shares. The European Commission believes that the special powers granted to the Portuguese Government through the sole ownership of the Class A shares act as a disincentive for investment by other EU member states in a manner that violates European Community Treaty rules. Should the Portuguese authorities not take satisfactory steps to remedy the alleged infringement of EU law, the European Commission may decide to refer the case to the European Court of Justice. As at 31 January 2008, the European Commission informed that the case over special rights held by the Portuguese State in Portugal Telecom was referred to the European Court of Justice. As at 31 January 2008, the European Commission informed that the case related to the special rights that the Portuguese Government holds over Portugal Telecom would be trialled by the European Justice Court.

c) Other Legal Proceedings

On 23 April 2001, PT Comunicações submitted a claim to the Lisbon administrative court, contesting the legality of an ANACOM administrative decision of 21 February 2001, which instructed PT Comunicações to change its billing structure for the connection of ISPs to its fixed line network from a model based on revenue sharing to one based on call origination charges and established maximum prices that PT Comunicações is permitted to charge ISPs for Internet interconnection service. PT Comunicações has claimed that ANACOM's administrative decision was issued

in contravention of Portuguese and EU law. If PT Comunicações is successful in its initial claim, it plans to request compensation for any losses suffered in connection with the implementation of its reference Internet access offer of 1 March 2001.

In April 2003, TVI-Televisão Independente, SA, or TVI, a television company, filed a claim against the Portuguese State and PT Comunicações in the Lisbon Administrative Court. In 1990, TVI and SIC, another television company, were awarded licenses for the provision of television channels pursuant to a public tender process. TVI claims that when it tendered for the television channel license, it chose not to use the publicly-owned backbone network to carry its signals but to build and operate its own network, and that it made this decision on the basis of the prices of the publicly-owned backbone network. TVI argues that when PT Comunicações subsequently took control over that network and became the provider of that network for carriage of television signals, PT Comunicações lowered the prices (on which TVI argues it based its decision) charged to SIC and RTP, the national television company, and that this violated several principles and provisions of Portuguese law. The price decreases are alleged to have been made under the Pricing Convention entered into by Portugal Telecom with the Portuguese State and the Portuguese telecommunications regulator in 1997, which regulated our network prices.

TVI is claiming an amount of about Euro 64 million from the Portuguese State and PT Comunicações. TVI claims that this amount reflects the excess of the cost to it of building and operating its own network over the prices it would have paid had it chosen to use the publicly-owned backbone network, as well as loss of profit which it would have made had it used that network, which TVI argues is more extensive and more developed than its own. PT Comunicações strongly disagrees with TVI's claims. On 20 June 2003, PT Comunicações submitted its response to TVI's claim, arguing that (i) the statute of limitations on TVI's claim for compensation has run because the claim relates to events that occurred more than ten years ago, (ii) the decrease in prices charged by PT Comunicações for the use of the publicly-owned backbone network did not violate Portuguese law because it does not require that the prices charged for use of such network remain unchanged; and (iii) TVI's claim for damages and losses is neither legally nor factually sustainable. The Portuguese State has also submitted its response to TVI's claim, and PT Comunicações is currently waiting for the Lisbon Administrative Court to set a date for the preliminary hearing.

In September 2003, HLC - Telemedia, SGPS, S.A., Horácio Luís de Brito Carvalho and HLC - Engenharia e Gestão de Projectos, SA (collectively, HLC) filed a law suit against PT Comunicações in the Lisbon Civil Court seeking to

be compensated by Euro 15 million. HLC is arguing that PT Comunicações (i) ceased rendering fixed telephone services; (ii) ceased rendering interconnection services; and (iii) interrupted the rendering of PT Comunicações leased line services and that these actions caused HLC to go bankrupt, injured HLC's image and resulted in Horácio Luís de Brito Carvalho becoming personally liable for certain of HLC's losses. PT Comunicações disagrees with HLC's claim and responded to it in November 2003. HLC answered this response in December 2003. The Lisbon Civil Court has determined which facts have been established in connection with this claim and which facts have yet to be established. PT Comunicações is now waiting for the court to set a date for the final hearing.

In March 2004, TV TEL Grande Porto - Comunicações, SA, or TVTEL, a telecommunications company based in Oporto, filed a claim against PT Comunicações in the Lisbon Judicial Court. TV TEL alleged that PT Comunicações, since 2001, has unlawfully restricted and/or refused access to the telecommunication ducts of PT Comunicações in Oporto, thereby undermining and delaying the installation and development of TV TEL's telecommunications network. TV TEL alleges that PT Comunicações intended to favor both itself and CATVP TV Cabo Portugal, S.A, a PT Multimédia subsidiary and a direct competitor of TV TEL.

TV TEL is claiming an amount of approximately Euro 15 million from Portugal Telecom for damages and losses allegedly caused and yet to be sustained by that company as a result of the delay in the installation of its telecommunications network in Oporto. In addition, TV TEL has demanded that PT Comunicações be required to give full access to its ducts in Oporto. PT Comunicações submitted its defense to these claims in June 2004, stating that (1) TV TEL did not have a general right to install its network in PT Comunicações's ducts, (2) all of TV TEL's requests were lawfully and timely responded to by PT Comunicações according to its general infrastructure management policy, and (3) TV TEL's claims for damages and losses were not factually sustainable. The preliminary hearing in this proceeding has been completed and PT Comunicações expects that a date for a trial will be set in the near future.

46.2. Claims and legal actions**Proceedings with probable losses**

As at 31 December 2007 and 2006, there were several claims and legal actions against certain subsidiaries of the Group in which losses are considered probable in accordance with the definitions of IAS 37. For those claims and legal actions, the Group recorded provisions (Note 39), based on the opinion of its internal and external legal counsel, to cover the probable future outflows, as follows:

| | 2007 | 2006 |
|--------------|-------------------|-------------------|
| Civil claims | 45,080,214 | 34,589,283 |
| Labor claims | 18,964,920 | 15,915,554 |
| Other | 5,438,968 | 1,882,105 |
| | 69,484,102 | 52,386,942 |

Proceedings with possible losses

As at 31 December 2007 and 2006, there were several claims and legal actions against certain subsidiaries of the Group, for which the most important ones are described above and whose settlement is considered to be possible based on the information provided by its legal counsel. The nature of those claims and legal actions is as follows:

| | 2007 | 2006 |
|--------------|--------------------|--------------------|
| Civil claims | 164,377,467 | 155,603,666 |
| Labor claims | 36,011,041 | 21,521,774 |
| Other (i) | 526,363,887 | 396,550,612 |
| | 726,752,395 | 573,676,052 |

(i) In 2007, this caption includes Euro 441 million related to Portugal Telecom's 50% share in possible contingencies at Vivo, which are primarily related to tax issues, including income taxes and other indirect taxes, and an amount of Euro 71 million related to possible tax contingencies at companies operating in Portugal.

In addition to the above mentioned contingencies, during 2007 Portugal Telecom received a tax inspection report for the years 2004 and 2005, raising questions to the deductability of certain financial costs incurred in 2004 and 2005 amounting to Euro 100 million and Euro 97 million, respectively. As at 31 December 2007, Portugal Telecom had not yet received any additional liquidation relating to this matter and, based on the opinion of its tax advisers, it believes that even if this liquidation is received in the future, there are arguments that support the Company's position.

47. Subsequent events

There were no relevant events after 31 December 2007.

EXHIBIT

- a. Subsidiary companies**

- b. Associated companies**

- c. Companies consolidated using the proportional method**

I. Subsidiaries

The following companies were included in the consolidation as at 31 December 2007 and 2006.

Subsidiaries located in Portugal:

| Company | Head office | Activity | Percentage of ownership | | Dec 2006 Effective |
|---|---------------|--|--|-----------|--------------------|
| | | | Direct | Effective | |
| Portugal Telecom (parent company) (Note 1) | Lisbon | Holding company. | | | |
| Cabo TV Açoreana, SA (a) | Ponta Delgada | Distribution of television signals by cable and satellite in the Azores area. | | | 48.98% |
| Cabo TV Madeirense, SA (a) | Funchal | Distribution of television signals by cable and satellite in the Madeira area. | | | 41.92% |
| DCSI Dados, Computadores e Soluções Informáticas, Lda. (b) | Lisbon | Provision of IT systems and services. | | | 100.00% |
| Directel - Listas Telefónicas Internacionais, Lda. (Directel) | Lisbon | Publication of telephone directories and operation of related data bases. | Africatel (100%) | 78.00% | 100.00% |
| Empracine - Empresa Promotora de Actividades Cinematográficas, Lda. (a) | Lisbon | Developing activities on movies exhibition. | | | 58.36% |
| Empresa de Recreios Artísticos, Lda. (ERA) (a) | Lisbon | Cinema exhibition. | | | 53.65% |
| Fundação PT (c) | Lisbon | Provide social care services. | Portugal Telecom (51%) PT Comunicações (18%) TMN (18%) PT Inovação (2.5%) | 89.50% | 95.64% |

| | | | | | | |
|---|------------------|--|----------------|--------|--|--------|
| Grafilme Sociedade Impressora de Legendas, Lda. (a) | Lisbon | Providing services on audiovisual subtitling. | | | | 32,46% |
| Infonet Portugal Serviços de Valor Acrescentado, Lda | Lisbon | Commercialization of value added products and services in the área of information and communication by computer through access to the Infonet world network. | PT Prime (90%) | 90.00% | | 90.00% |
| Janela Digital - Informativo e Telecomunicações, Lda (Janela Digital) (c) | Caldas da Rainha | Development of IT solutions to the real state market. | PT.com (50%) | 50.00% | | 50.00% |
| Lusomundo Audiovisuais, SA (a) | Lisbon | Import, commercialization, distribution and production of audiovisual products. | | | | 58.43% |
| Lusomundo Cinemas, SA (a) | Lisbon | Cinema exhibition. | | | | 58.43% |
| Lusomundo Editores, SA (a) | Lisbon | Movies distribution. | | | | 58.43% |

| Company | Head office | Activity | Direct | Percentage of ownership | | Dec 2006 Effective |
|--|-------------|---|-------------------------|-------------------------|-----------|--------------------|
| | | | | Dec 2007 | Effective | |
| Lusomundo - Sociedade Investimentos Imobiliários, SGPS, SA (Lusomundo SII) (a) | Lisbon | Management of Real Estate. | | | | 58.36% |
| Lusomundo Imobiliária 2, SA (a) | Lisbon | Management of Real Estate. | | | | 58.24% |
| Portugal Telecom Inovação, SA (PT Inovação) | Aveiro | Innovation, research, development and integration of telecommunications services and engineering solutions and training services in telecommunications. | Portugal Telecom (100%) | | 100.00% | 100.00% |

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| | | | | | |
|---|--------|---|--|---------|---------|
| Previsão Sociedade Gestora de Fundos de Pensões, SA (Previsão) | Lisbon | Pension fund management. | Portugal Telecom (82.05%) | 82.05% | 78.12% |
| Postal Network - Prest. Serviços de Gestão Infra-estrut.comunic. ACE (c) | Lisbon | Providing postal network services. | PT Prime (51%) | 51.00% | 51.00% |
| PT Acessos de Internet Wi-Fi, SA | Lisbon | Provides wireless Internet access services. | Portugal Telecom (100%) | 100.00% | 100.00% |
| Portugal Telecom Associação de Cuidados de Saúde (c) | Lisbon | Provide services of medical care | PT Comunicações (93.90%) PT Prime (6.10%) | 100.00% | 100.00% |
| PT Centro Corporativo, SA | Lisbon | Providing consultant service to Group companies. | Portugal Telecom (100%) | 100.00% | 100.00% |
| PT Comunicações, SA (PT Comunicações) | Lisbon | Establishment, management and operation of telecommunications infrastructures and provision of public telecommunication services and telebroadcasting services. | PT Portugal (100%) | 100.00% | 100.00% |
| PT Compras Serviços de Consultoria e Negociação, SA | Lisbon | Providing consultant and negotiation services related with the buying process. | Portugal Telecom (100%) | 100.00% | 100.00% |
| PT Contact - Telemarketing e Serviços de Informação, SA (PT Contact) | Lisbon | Production, promotion and sale of information systems, including information products and services and related technical assistance. | PT Comunicações (100%) | 100.00% | 100.00% |
| PT Conteúdos - Actividade de Televisão e de Produção de Conteúdos, SA (former TV Cabo Audiovisuais) (a) | Lisbon | Production and sale of television programs and advertising management. | | | 58.43% |
| PT Corporate | Lisbon | Providing all services available in the Group, in the fixed line and mobile telecommunications and information systems. | PT Comunicações (100%) | 100.00% | 100.00% |
| PT Investimentos Internacionais, SA (PT II) | Lisbon | Business advisory board service installment, consultation, administration and business management. Elaboration of projects and economic studies and manage investments. | Portugal Telecom (100%) | 100.00% | 100.00% |

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| | | | | | |
|---|--------|--|------------|---------|---------|
| PT Meios - Serviços de Publicidade e Marketing, SA (d) | Lisbon | Purchase, sale and exchange of space advertising, analysis of marketing investment projects. | | | 100.00% |
| PT Móveis - Serviços de Telecomunicações, SGPS, SA (PT Móveis) | Lisbon | Management of investments in the mobile business. | TMN (100%) | 100.00% | 100.00% |
| PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, SA (a) | Lisbon | Management of investments in the multimedia business. | | | 58.43% |

| Company | Head Office | Activity | Percentage of Ownership | | |
|--|-------------|---|-------------------------|--------------------|--------------------|
| | | | Direct | Dec 2007 Effective | Dec 2006 Effective |
| PT Multimédia - Serviços de Apoio à Gestão , SA (a) | Lisbon | Providing management support services. | | | 58.43% |
| PT Portugal, SGPS, SA | Lisbon | Management of investments. | Portugal Telecom (100%) | 100.00% | 100.00% |
| PT Prestações-Mandatária de Aquisições e Gestão de Bens, SA (PT Prestações) | Lisbon | Acquisition and management of assets. | PT Comunicações (100%) | 100.00% | 100.00% |
| PT Prime - Soluções Empresariais de Telecomunicações e Sistemas, SA | Lisbon | Provision of development and consultancy services in the areas of electronic commerce, contents and information technology. | PT Comunicações (100%) | 100.00% | 100.00% |
| PT Prime Tradecom - Soluções Empresariais de Comércio Electrónico, SA (Tradecom) | Lisbon | Provision of development and consultancy services in the areas of electronic commerce, contents and information technology. | Portugal Telecom (66%) | 66.00% | 66.00% |

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| | | | | | |
|---|--------|--|--|---------|---------|
| PT Pro, Serviços Administrativos e de Gestão Partilhados, SA | Lisbon | Shared services center. | Portugal Telecom (100%) | 100.00% | 100.00% |
| Pro Share (e) | Lisbon | Shared services center. | PT Pro (50%) | 50.00% | |
| PT Rede Fixa, SGPS, SA | Lisbon | Management of investments. | Portugal Telecom (100%) | 100.00% | 100.00% |
| PT Sistemas de Informação, SA (PT SI) | Oeiras | Provision of IT systems and services. | Portugal Telecom (99.8%) PT Comunicações (0.1%) TMN (0.1%) | 100.00% | 100.00% |
| PT Televisão por Cabo, SGPS, SA (a) | Lisboa | Management of investments in television by cable market. | | | 58.43% |
| PT Ventures, SGPS, SA (PT Ventures) | Lisbon | Management of investments in international markets. | Portugal Telecom (100%) | 100.00% | 100.00% |
| PT.com Comunicações Interactivas, SA | Lisbon | Services rendered development and sale of communication product services, information and multimedia services. | PT Comunicações (100%) | 100.00% | 100.00% |
| PT Imobiliária, SA | Lisbon | Administration of real estate assets, real estate investment consultancy, management of property developments, purchase and sale of real estate. | Portugal Telecom (100%) | 100.00% | 100.00% |
| Superemprego - Sistemas de Informação para Gestão de Recursos Humanos, SA (c) | Lisbon | Management and collection of information about the labor market. | PT.com (63.75%) | 63.75% | 63.75% |
| Telemática - Consultores de Telecomunicações e Informática, Lda.(f) | Lisbon | Supply of computer equipment, training and installations. | | | 100.00% |

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| Company | Head Office | Activity | Percentage of Ownership | | Dec 2006 Effective |
|--|-------------|---|---|--------------------|--------------------|
| | | | Direct | Dec 2007 Effective | |
| TMN Telecomunicações Móveis Nacionais, SA | Lisbon | Provision of mobile telecommunications services and the establishment, management and operation of telecommunications networks. | PT Portugal (100%) | 100.00% | 100.00% |
| TPT - Telecomunicações Públicas de Timor, SA (TPT) | Lisbon | Purchase, sale and services rendering of telecommunications products and information technologies in Timor | PT Ventures (75.16%) PT Ásia (0.98%) | 76.14% | 76.14% |
| TV Cabo Portugal, SA (a) | Lisbon | Distribution of television by cable, conception, realization, production and broadcasting of television programs, operation of telecommunications services. | | | 58.43% |
| Web-Lab, SGPS, SA (b) | Lisbon | Managemnt of investments. | | | 90.00% |

(a) These companies were included in the Multimedia business and are no longer part of the Portugal Telecom Group following the conclusion of the spin-off of this business on November 2007.

(b) These companies were liquidated during 2007.

(c) These companies were consolidated by the equity method in 2007.

(d) This company was merged into PT Compras on December 2007.

(e) This company was incorporated during the fourth quarter of 2007 by PT Pro and PT Multimédia with the purpose of being the shared services center of PT Multimédia. This company was accounted for by the equity method during 2007.

(f) This company was merged into PT Contact on August 2007.

Subsidiaries located in Brazil:

| Company | Head Office | Activity | Percentage of Ownership | | Dec 2006 Effective |
|--|-------------|--|--|--------------------|--------------------|
| | | | Direct | Dec 2007 Effective | |
| Mobitel, SA | São Paulo | Call center services. | PT Brazil (100%) | 100.00% | 100.00% |
| Portugal Telecom Brazil, SA (PT Brazil) | São Paulo | Management of investments. | Portugal Telecom (99.95%) PT Comunicações (0.05%) | 100.00% | 100.00% |
| Portugal Telecom Inovação Brazil, Ltda. | São Paulo | Development of information technologies and telecommunications services. | PT Inovação(100%) | 100.00% | 100.00% |
| PT Multimedia.com Brazil, Ltda. (PTM.com Brazil) | São Paulo | Management of investments. | PT Brazil (100%) | 100.00% | 100.00% |
| PT Multimedia.com Participações, SA (a) | São Paulo | Management of investments. | | | 100.00% |

(a) This company was liquidated during 2007.

Subsidiaries located in Africa:

| Company | Head Office | Activity | Percentage of Ownership | | Dec 2006 Effective |
|-----------------------|-------------|---|---------------------------|--------------------|--------------------|
| | | | Direct | Dec 2007 Effective | |
| Cabo Verde Móvel | Praia | Mobile telecommunications services in Cabo Verde. | Cabo Verde Telecom (100%) | 31.20% | 40.00% |
| Cabo Verde Multimédia | Praia | Multimedia telecommunications services in Cabo Verde. | Cabo Verde Telecom (100%) | 31.20% | 40.00% |

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| | | | | | |
|---|----------|--|--|---------|---------|
| Cabo Verde Telecom | Praia | Fixed and mobile telecommunications services in Cabo Verde. | Africatel (40%) | 31.20% | 40.00% |
| Contact Cabo Verde Telemarketing e Serviços de Informação, SA | Praia | Call and contact center services. | PT Contact (100%) | 100.00% | 100.00% |
| CST Companhia Santomense de Telecomunicações, SARL. | São Tomé | Fixed and mobile telecommunication services in São Tomé e Príncipe. | Africatel (51%) | 39.78% | 51.00% |
| Directel Cabo Verde Serviços de Comunicação, Lda. | Praia | Publication of telephone directories and operation of related databases in Cabo Verde | Directel (60%) Cabo Verde Telecom (40%) | 59.28% | 76.00% |
| Directel Uganda Telephone Directories, Limited (a) | Uganda | Publication of telephone directories. | Directel (100%) | 78.00% | 100.00% |
| Elta - Empresa de Listas Telefónicas de Angola, Lda. | Luanda | Publication of telephone directories. | Directel (55%) | 42.90% | 55.00% |
| Guinetel, S.A. (a) | Bissau | Provision of public telecommunications services. | Africatel (55%) | 42.90% | 55.00% |
| Kenya Postel Directories, Ltd. | Nairobi | Production, editing and distribution of telephone directories and other publications. | Directel (60%) | 46.80% | 60.00% |
| LTM - Listas Telefónicas de Moçambique, Lda. | Maputo | Management, editing, operation and commercialization of listings of subscribers and classified telecommunications directories. | Directel (50%) | 39.00% | 50.00% |
| Lusomundo Moçambique, Lda. (b) | Maputo | Cinema exhibition. | | | 58.43% |
| Mobile Telecommunications Limited | Namíbia | Mobile cellular services operator | Africatel (34%) | 26.52% | 34.00% |

(a) These companies were consolidated by the equity method in 2007.

(b) This company was included in the Multimedia business and is no longer part of the Portugal Telecom Group following the conclusion of the spin-off of this business on November 2007.

Other subsidiaries:

| Company | Head Office | Activity | Percentage of Ownership | | Dec 2006 Effective |
|---|-------------|---|----------------------------------|--------------------|--------------------|
| | | | Direct | Dec 2007 Effective | |
| AGTEL, BV (a) | Amsterdam | Management of investments. | PT Ventures (100%) | 100.00% | |
| Archways (b) | Beijing | Remote access services. | China Pathway Logistics BV (70%) | 46.20% | 46.20% |
| Canal 20 TV, SA (c) | Madrid | Distribution of TV products. | | | 29.22% |
| China Pathway Logistics BV | Amsterdam | Management of investments. | PT Ventures (66,00%) | 66.00% | 66.00% |
| CVTEL, BV (a) | Amsterdam | Management of investments. | PT Ventures (100%) | 100.00% | |
| Directel Macau Listas Telefónicas, Lda. (d) | Macau | Publication of telephone directories and operation of related databases in Macau. | | | 80.00% |
| Direct Media Ásia | Hong Kong | Publication of B2B and other related telephone directories either in paper or electronic support. | Direcel (99%) PT Ásia (1%) | 78.22% | 100.00% |

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| | | | | | |
|--|--------------|---|--|---------|---------|
| Lea Louise BV (e) | Amsterdam | Management of investments. | | | 100.00% |
| Lusomundo España, SL (Lusomundo Madrid Espana) (c) | | Management of investments relating to activities in Spain in the audiovisuals business. | | | 58.43% |
| Africatel (f) | Amsterdam | Management of investments | PT Ventures (78%) | 78.00% | 100.00% |
| Portugal Telecom Argentina S.A. (g) | Buenos Aires | Provider of telecommunications services. | Portugal Telecom (10.01%) PT Ventures (40.00%) | 50.01% | 50.01% |
| Portugal Telecom Ásia, Lda. (PT Ásia) | Macau | Promotion and marketing of telecommunications services. | Portugal Telecom (95.92%) PT Comunicações (4.04%) | 99.96% | 99.96% |
| Portugal Telecom Europa, S.P.R.L. (PT Europa) (g) | Brussels | Technical and commercial management consultancy in the communication area with respect to the European market and community matters. | Portugal Telecom (98.67%) | 98.67% | 98.67% |
| Portugal Telecom Internacional Finance B.V | Amsterdam | Obtaining financing for the group in international markets. | Portugal Telecom (100%) | 100.00% | 100.00% |
| Timor Telecom, SA | Timor | Provider of telecommunications services in Timor | TPT (54.01%) | 41.12% | 41.12% |
| TV Cabo Macau, SA (d) | Macau | Distribution of television and audio signals, installation and operation of a public telecommunications system and provision of video services, in Macau. | | | 87.49% |

-
- (a) These companies were incorporated during 2007 and were consolidated by the equity method in 2007.
- (b) This company was fully consolidated for the first time in 2007. As at 31 December 2006, this company was accounted for by the equity method.
- (c) These companies were included in the Multimedia business and are no longer part of the Portugal Telecom Group following the conclusion of the spin-off of this business on November 2007.
- (d) These investments were disposed of in 2007.

- (e) During the first half of 2007, PT Ventures has disposed 90% of its investment in this company, and therefore this company is no longer a subsidiary of Portugal Telecom.
- (f) On July 2007, PT Ventures has disposed of 22% of its investment in this company.
- (g) These companies were consolidated by the equity method in 2007.

II. Associated companies

The associated companies as at 31 December 2007 and 2006 are as detailed below.

Associated companies located in Portugal:

| Company | Head Office | Activity | Direct | Percentage of ownership | | Dec 2006 Effective |
|--|-------------|--|--|-------------------------|-----------|--------------------|
| | | | | Dec 2007 | Effective | |
| BEST Banco Electrónico de Serviço Total, SA (Banco Best) | Lisbon | Provision of e.banking services. | PT.com (34%) | | 34.00% | 34.00% |
| Caixanet - Telemática e Comunicações, SA | Lisbon | Provision of e.banking services. | PT Prime (10%) PT SI (5%) | | 15.00% | 15.00% |
| Distodo - Distribuição e Logística, Lda. (a) | Lisbon | Stocking, sale and distribution of audiovisual material. | | | | 29.22% |
| Entigere Entidade Gestora Rede Multiserviços, Lda. | Lisbon | Networks management. | PT Ventures (25%) | | 25.00% | 29.00% |
| INESC Instituto de Engenharia de Sistemas e Computadores, SA | Lisbon | Scientific research and technological consultancy. | Portugal Telecom (26.36%) PT Comunicações (9.53%) | | 35.89% | 35.89% |
| Lisboa TV Informação e Multimedia, SA (a) | Lisbon | Television operations, notably production and commercialization of programs and publicity. | | | | 23.37% |
| Multicert Serviços de Certificação Electrónica, SA | Lisbon | Supply of electronic certification services. | PT Prime (20%) | | 20.00% | 20.00% |
| Octal TV, SA. (a) | Lisbon | Development, commercialization, training and consultancy in systems for interactive and broad band television. | | | | 11.69% |
| Páginas Amarelas, SA (Páginas Amarelas) | Lisbon | Production, editing and distribution of telephone directories and publications. | Portugal Telecom (24.88%) PT Prime (0.125%) | | 25.00% | 25.00% |
| Siresp Gestão de Rede Digitais de Segurança e Emergência, SA | Lisbon | Networks management. | PT Ventures (30.55%) | | 30.55% | 15.27% |

| | | | | | | |
|---|--|--------|---|--|--------|--------|
| SGPICE | Sociedade de Gestão de Portais de Internet e Consultoria de Empresas, SA | Lisbon | Developing activities providing global products and services for internet support. | PT Comunicações (11.11%) Portugal Telecom (11.11%) | 22.22% | 28.72% |
| Socofil | Sociedade Comercial de Armazenamento e Expedição de Filmes, Lda. (a) | Lisbon | Distribution, exhibition, import and export of audiovisual products. | | | 26.29% |
| Sportinvest Multimédia, SGPS, SA | | Lisbon | Management of investments. | Portugal Telecom (50%) | 50.00% | 50.00% |
| Tele Larm Portugal Sinais, SA | Transmissão de | Lisbon | Provision of transmission, services, supervision of alarms, telemasurement, telecontrol and data exchange services. | PT Prime (50%) | 50.00% | 50.00% |
| TV Lab - Serviços e Equipamentos Interactivos, SA | | Lisbon | Developing digital tv interactive solutions. | PT.com (50%) | 50.00% | 50.00% |
| Wisdown Tele Vision Produtos de Televisão, Lda | Serviços e | Lisbon | Development of services and products related to new technology in the TV market | PT .com(50%) | 50.00% | 50.00% |

(a) These companies were included in the Multimedia business and are no longer part of the Portugal Telecom Group following the conclusion of the spin-off of this business on November 2007.

Associated companies located in Africa:

| Company | Head Office | Activity | Direct | Percentage of ownership | | Dec 2006 Effective |
|---|-------------|--|--------------------|-------------------------|-----------|--------------------|
| | | | | Dec 2007 | Effective | |
| Guiné Telecom Companhia de Telecomunicações da Guiné-Bissau, S.A.SAR.L. | Bissau | Provision of public telecommunications services. | Africatel (40.14%) | | 31.31% | 40.14% |
| Médi Télécom | Casablanca | Provision of mobile services in Morocco. | PT Móveis (32.18%) | | 32.18% | 32.18% |
| Multitel - Serviços de Telecomunicações, Lda. | Luanda | Provision of data communications services and digital information communication services, in Angola. | Africatel (35%) | | 27.30% | 35.00% |

| | | | | | |
|------------------------------|--------|--|-----------------|--------|--------|
| Teledata de Moçambique, Lda. | Maputo | Operation and commercialization of public data telecommunications services and other telematic services. | Africatel (50%) | 39.00% | 50.00% |
| Unitel | Luanda | Mobile telecommunications services, in Angola. | Africatel (25%) | 19.50% | 25.00% |

Other associated companies:

| Company | Head Office | Activity | Direct | Percentage of ownership | |
|--|-------------|---|---|-------------------------|-----------|
| | | | | Dec 2007 | Dec 2006 |
| | | | | Effective | Effective |
| CTM Companhia de Telecomunicações de Macau, S.A.R.L. | Macau | Provision of public telecommunications services, in Macau. | PT Comunicações (3%) PT Ventures (25%) | 28.00% | 28.00% |
| Hungaro Digital KFT | Budapest | Provision of telecommunications services. | PT Ventures (44.62%) | 44.62% | 44.62% |
| Telesat - Satellite Communications, Limited (a) | Macau | Operation of land based satellite stations, commercialization of private telecommunications network services. | | | 22.22% |
| UOL, Inc. | São Paulo | Provides Internet services and produces Internet contents. | PT SGPS(22.17.%)PT Brazil (6.83%) | 29.00% | 29.00% |

(a) This company was disposed of in 2007.

III. Companies consolidated using the proportional method

Companies consolidated using the proportional method located in Brazil:

| Company | Head Office | Activity | Direct | Percentage of ownership | | Dec 2006 Effective |
|--|-------------|------------------------------------|---|-------------------------|-----------|--------------------|
| | | | | Dec 2007 | Effective | |
| Avista | São Paulo | Management of investments. | Brasilcel (100%) | | 50.00% | 50.00% |
| Vivo, SA (a) | Curitiba | Mobile cellular services operator. | Vivo Participações (100%) | | 31.38% | 31.38% |
| Portelcom Participações, SA (Portelcom) | São Paulo | Management of investments. | Brasilcel (60.15%) Ptelecom Brazil (39.85%) | | 50.00% | 50.00% |
| Ptelecom Brazil, SA (Ptelecom) | São Paulo | Management of investments. | Brasilcel (100%) | | 50.00% | 50.00% |
| Sudeste Celular Participações, SA (Sudeste Celularl) | São Paulo | Management of investments. | Brasilcel (100%) | | 50.00% | 50.00% |
| Tagilo Participações, Lda. (Tagilo) | São Paulo | Management of investments. | Brasilcel (100.%) | | 50.00% | 50.00% |
| TBS Celular Participações, SA (TBS) | São Paulo | Management of investments. | Brasilcel (73.27%); Sudeste Celular(22.99) | | 48.13% | 48.13% |
| Vivo Participações, SA (Vivo Participações) (a) | São Paulo | Management of investments. | Brasilcel (40.85%) Portelcom (4.68%) Sudestecel (6.22%) TBS (4.87%) Avista (3.91%) Tagilo (2.41%) | | 31.38% | 31.38% |

(a) As at 31 December 2007, the voting rights in Vivo Participações are 44.43%.

Companies consolidated using the proportional method located in other countries:

| Company | Head Office | Activity | Percentage of ownership | | Dec 2006 Effective |
|-------------------------------|-------------|--|-------------------------|--------------------|--------------------|
| | | | Direct | Dec 2007 Effective | |
| Brasilcel, N.V. (Brasilcel) | Amsterdam | Management of investments. | PT Móveis (50.00%) | 50.00% | 50.00% |
| Sport TV Portugal, SA (a) | Lisbon | Conception, production, realization and commercialization of sports programs for telebroadcasting, purchase and resale of the rights to broadcast sports programs for television and provision of publicity services | | | 29.22% |

(a) This companies was included in the Multimedia business and is no longerpart of the Portugal Telecom Group following the conclusion of the spin-off of this business on November 2007.

Report and opinion of the Audit Committee

English version of the original report in Portuguese

AUDIT COMMITTEE REPORT
TO THE CONSOLIDATED ANNUAL REPORT
FOR THE YEAR OF 2007

1 Introduction

Following the amendments to its By-laws approved by the General Shareholders Meeting held on June 22nd, 2007, Portugal Telecom, SGPS, S.A. (the Company or PT SGPS) has established a corporate model under which an Audit Committee and Statutory Auditor are responsible for the supervision of the Company. On the same date, the General Shareholders Meeting has appointed the members of the current Audit Committee as well as the Company Statutory Auditor and its substitute, thus being dismissed the Supervisory Board in functions until then.

Pursuant to the terms and for the purpose of paragraph g) to Article 423-F of the Portuguese Companies Act and Article 28 of the By-laws, PT SGPS s Audit Committee hereby presents its report to the Consolidated Annual Report for the year ended on December 31, 2007.

2 Supervisory activities

Within its responsibilities and for the purpose of complying with its functions as supervisory body since June 22nd, 2007, the Audit Committee has supervised the quality and integrity of the financial information disclosure processes.

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The Audit Committee held meetings with the responsables for the preparation of the Consolidated Report and of the major subsidiaries, with the Independent Auditors and with the Statutory Auditor, having analyzed the main questions raised in the accounts closing and in the preparation of the management report. In addition, the Audit Committee has reviewed the Accounts Certificate (*Certificação Legal de Contas*) issued by the Statutory Auditor and the Independent Auditors Report, both referring to the aforementioned consolidated financial statements approved by the Board of Directors, which do not include any reserves.

The Audit Committee has overseen, since the beginning of its functions on June 22nd, 2007, the management and evolution of the Company's businesses and its compliance with the applicable legal, regulatory and accounting rules.

In particular, the Audit Committee has monitored the execution and analyzed the impact on the financial condition of the following measures, implemented as a result of the remuneration policy approved at the Company's General Shareholders Meeting, held on April 27, 2007:

- A distribution of dividends in cash of 0.475 Euros per share relating to 2006 and paid in May 18th, 2007;
- The spin-off process of the former PT - Multimédia Serviços de Telecomunicações e Multimédia, SGPS, S.A. determining a reduction of the consolidated shareholder's equity by 405,328,608 Euros;
- The changes to the Company's share capital, in particular the share capital reduction of 3,091,695 Euros, through the cancellation of 103,056,500 treasury shares, in the context of the execution of the share buyback program

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approved at the General Shareholders Meeting, which, up to December 31st, 2007, was executed in more than 50%.

The Audit Committee has also overseen the process and the financial impact of the Company's offer of Exchangeable Bonds, with maturity date in 2014, up to 750 million Euros.

The Audit Committee has also supervised the qualifications, independence and work of the Company's Independent Auditors and Statutory Auditor as well as of the quality, integrity and effectiveness of PT SGPS's internal control and risk management system and internal audit function.

As far as the internal control system is concerned, we highlight that it was certified by the Company's Independent Auditors in 2007, by reference to the year of 2006, in accordance with the requirements foreseen in *Section 404* of the *Sarbanes-Oxley Act* and on the basis of the methodology defined by *COSO (Committee of Sponsoring Organizations)*.

The aforementioned supervisory activities will be further detailed in the Audit Committee's Activities Report relating to the year of 2007 to be disclosed in the Company's website.

3 - Opinion on the consolidated report for the year 2007

In our opinion, the consolidated report for the year ended at December 31st, 2007, including the balance sheet, the income statements, the statements of recognized income and expenses, the cash flows statements and its attached notes, related to the year then ended, comply with the applicable accounting and legal provisions and the By-laws, thus the Audit

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Committee recommends its approval by PT SGPS's General Shareholders Meeting.

Lisbon, 27 February, 2008

THE CHAIRMAN

(João Manuel de Mello Franco)

THE MEMBERS

(Thomaz Paes de Vasconcellos)

(José Guilherme Xavier de Basto)

Deloitte & Associados, SROC S.A.
Inscrição na OROC nº 43
Registo na CMVM nº 231

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1050-094 Lisboa

Portugal

AUDITORS REPORT

CONSOLIDATED FINANCIAL STATEMENTS

(Translation of a report originally issued in Portuguese)

Introduction

1. Pursuant to the dispositions of article 245 of Portuguese Securities Market Code we hereby present our Auditors Report on the consolidated financial information contained in the Board of Directors Report and the consolidated financial statements of Portugal Telecom, SGPS, S.A. (the Company) for the year ended 31 December 2007, which comprise the consolidated balance sheet that presents a total of 13,122,170,886 Euros and shareholders equity of 2,081,810,188 Euros, including a net profit attributable to the shareholders of the Company of 741,859,736 Euros, the consolidated statements of profit and loss by nature, of cash flows and of recognised income and expenses for the year then ended and the corresponding notes.

Responsibilities

2. The Company s Board of Directors is responsible for: (i) the preparation of consolidated financial statements that present a true and fair view of the financial position of the companies included in the consolidation, the consolidated results of their operations, the consolidated cash flows and the consolidated statement of recognised income and expenses; (ii) the preparation of historical financial information in accordance with International Financial Reporting Standards as adopted in the European Union, which is complete, true, timely, clear, objective and licit, as required by the Portuguese Securities Market Code; (iii) the adoption of adequate accounting policies and criteria and the maintenance of appropriate system of internal control; and (iv) the disclosure of any significant facts that have influenced the operations of the companies included in the consolidation, their financial position and results of operations.

3. Our responsibility is to audit the financial information contained in the accounting documents referred to above, including verifying that, in all material respects, the information is complete, true, timely, clear, objective and licit, as required by the Portuguese Securities Market Code, and to issue a professional and independent report based on our work.

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Inscrição na OROC nº 43
Registo na CMVM nº 231

Scope

4. Our audit was performed in accordance with the Auditing Standards (*Normas Técnicas e as Directrizes de Revisão/Auditoria*) issued by the Portuguese Institute of Statutory Auditors (*Ordem dos Revisores Oficiais de Contas*), which require the audit to be planned and performed with the objective of obtaining reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes verifying, on a sample basis, evidence supporting the amounts and disclosures in the consolidated financial statements and assessing the significant estimates, based on judgments and criteria defined by the Board of Directors, used in their preparation. An audit also includes verifying the consolidation procedures and that the financial statements of the companies included in the consolidation have been appropriately audited, assessing the adequacy of the accounting policies used, their uniform application and their disclosure, taking into consideration the circumstances, verifying the applicability of the going concern concept, verifying the adequacy of the overall presentation of the consolidated financial statements and assessing if, in all material respects, the consolidated financial information is complete, true, timely, clear, objective and licit. An audit also includes verifying that the consolidated financial information included in the Board of Directors' Report is consistent with the consolidated financial statements. We believe that our audit provides a reasonable basis for expressing our opinion.

Opinion

5. In our opinion, the consolidated financial statements referred to in paragraph 1, present fairly in all material respects, the consolidated financial position of Portugal Telecom, SGPS, S.A. as of 31 December 2007 and the consolidated results of its operations, its consolidated cash flows and the recognised income and expenses for the year then ended, in conformity with International Financial Reporting Standards as adopted in the European Union and the financial information contained therein is, in terms of the definitions included in the auditing standards referred to in paragraph 4, complete, true, timely, clear, objective and licit.

Lisbon, 28 February 2008

DELOITTE & ASSOCIADOS, SROC S.A.
Represented by Manuel Maria Reis Boto

Corporate Governance Report

The purpose of this report is to disclose the corporate governance structure and practices adopted by the Company with a view to complying with the provisions of the Recommendations of the Portuguese Securities Market Commission (*Comissão do Mercado de Valores Mobiliários - CMVM*) on Corporate Governance of Listed Companies, as published in November 2005, as well as with the best international corporate governance practices. This report has been drawn up in accordance with article 7 of the Portuguese Securities Code (*Código dos Valores Mobiliários*) and the form attached to the CMVM Regulation no. 7/2001, as amended by the CMVM Regulations no. 11/2003, no. 10/2005 and no. 3/2006.

Additionally, this report aims to comply with the annual obligation to disclose the Company's corporate governance structure and practice in detail, under the terms of article 245-A of the Portuguese Securities Code, which is applicable to issuers of shares admitted to trading on a regulated market.

The adoption of the new CMVM Recommendations on the corporate governance of listed companies is currently subject to analysis and implementation within the company, and any changes to the corporate governance structure and practice are expected to be adopted in the course of the current financial year and disclosed in the corporate governance report to be published in 2009.

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CHAPTER 0. COMPLIANCE STATEMENT

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The Company fully adopts the CMVM Recommendations on the Corporate Governance of Listed Companies, as published in November 2005, except for Recommendations 4, 8 and 9, which are not complied with for the reasons identified hereunder.

The Chapters of this Corporate Governance Report that contain a description of the measures taken by the Company for compliance with the abovementioned CMVM Recommendations are identified hereunder.

| CMVM RECOMMENDATION | COMPLIANCE | REPORT |
|--|------------|---------------|
| <i>I Disclosure of Information:</i> | | |
| <i>1. The Company should ensure the existence of permanent contact</i> | Yes | Chapter 3 § 7 |

| CMVM RECOMMENDATION | COMPLIANCE | REPORT |
|--|------------|---------------|
| <i>with the market by observing the principle of shareholder equal treatment and preventing asymmetries in investor access to information. For such purpose, the company should create an investor relations department.</i> | | |
| II Exercise of Voting Rights and Shareholder Representation | | |
| <p>2. <i>The active exercise of voting rights, either directly, notably by correspondence, or by representation, should not be restricted. For this purpose, the following qualify as restrictions to the active exercise of voting rights: (a) any imposition of a prior deposit or share blocking period for participation in the general shareholders meeting in excess of 5 business days; (b) any bylaws restriction on voting by correspondence; (c) any imposition of an advance period for the receipt of voting declarations issued by correspondence in excess of 5 business days; and (d) the non-existence of voting bulletins available to shareholders for voting by correspondence.</i></p> | Yes | Chapter 4 |
| III Corporate Rules | | |
| <p>3. <i>The company should create an internal control system for an efficient detection of risks connected to the company business, to safeguard its assets and to the benefit of transparency in its corporate governance.</i></p> | Yes | Chapter 5 § 2 |
| <p>4. <i>Measures adopted to prevent the success of takeover bids should respect the interests of the company and its shareholders. Among others, defensive clauses the effect of which is to automatically cause an erosion in the company's assets in the case of control transition or of change in the composition of the management body, thus hindering the shareholders' free transferability and shareholders' free evaluation of the performance of members of the management body should be deemed contrary to such interests.</i></p> | | (1) |

| CMVM RECOMMENDATION | COMPLIANCE | REPORT |
|--|------------|---------------------|
| IV Management Body | | |
| <i>5. The management body should be composed of a plurality of members that effectively conduct the management of the company and its heads.</i> | Yes | Chapter 2 |
| <i>5-A. The management body should include a sufficient number of non-executive directors whose role is to continuously follow up and evaluate the company's management by its executive members. Members of other corporate bodies may play a complementary role, or ultimately a role of substitution if their respective supervisory powers are equivalent and actually exercised.</i> | Yes | Chapter 2 § 2 |
| <i>6. The non-executive members of the management body should include a sufficient number of independent members. Where there is only one non-executive director, he should also be independent. Independent members of other corporate bodies can play a complementary role, or ultimately a role of substitution if their respective supervisory powers are equivalent and actually exercised.</i> | Yes | Chapter 2 § 2 |
| <i>7. The management body should create internal control committees with powers to evaluate corporate structure and governance.</i> | Yes | Chapter 2 § 4 and 8 |
| <i>8. The remuneration of the members of the management body should be structured in such a way as to allow the alignment of their interests with the company's interests, and it should be annually disclosed on an individual basis.</i> | No | (2) |
| <i>8-A. A statement concerning corporate body remuneration policy should be submitted for consideration by the annual general shareholders meeting.</i> | Yes | Chapter 2 § 6 |
| <i>9. The members of the compensation committee or its equivalent</i> | No | (3) |

| CMVM RECOMMENDATION | COMPLIANCE | REPORT |
|--|----------------|----------------|
| <i>should be independent in relation to the members of the management body.</i> | | |
| <i>10. The proposal pertaining to the approval of share allotment plans, and/or share call options or based on share price variations, to members of the management body and/or to employees should be submitted to the general shareholders meeting. The proposal should contain all the data as required for a correct evaluation of the plan. The proposal should be accompanied by the plan's regulations or, where these have not yet been prepared, by the terms and conditions such regulations must comply with.</i> | Not applicable | Chapter 3 § 5 |
| <i>10-A. The company should adopt a policy for communication of irregularities allegedly occurred within the company, with the following data: indication of the means that can be used for internal communication of irregular practices, including the persons with legitimacy to receive such communications, indication of the treatment to be given to any such communications, including confidential treatment where the communicator so wishes. Such policy's general guidelines should be disclosed in the company's corporate governance report.</i> | Yes | Chapter 2 § 10 |

(1) Although it is PT's understanding that its Bylaws do not contain any defensive clauses which effect is to automatically cause an erosion in the company's assets in case of change of control or change in the composition of the management body, the CMVM understood, in its Analysis of the Compliance with the Recommendations on the Corporate Governance of Listed Companies in 2006, that PT failed to comply with Recommendation no. 4.

As no change to the Bylaws has occurred in the meantime modifying those aspects pointed out by the CMVM in the abovementioned Analysis, it is PT's understanding that it should

consider such Recommendation as non-complied with, without prejudice to the points mentioned hereinafter.

In fact, except for the special rights in favour of the State as described further on, in this matter PT's bylaws contain only a limitation on the counting of the votes of a single shareholder, whereby the votes cast by a single shareholder of ordinary shares, directly or through a representative, on his own behalf or as a representative of another shareholder, that exceed 10% of the total share capital, shall not be counted (article 13).

In truth, this provision, which intrinsically reflects and historically arose in several European countries as a measure of expansion of shareholder democracy (by reducing the voting power of major shareholders and correspondingly expanding the voting power of minorities), is also normally understood to possibly interfere with the success of takeover bids. However, notwithstanding the corresponding effect of reduction in the number of takeovers (as higher levels of shareholder participation are required to obtain control), such measure is also deemed as an incentive to the existence of more attractive conditions of takeover bids, since only higher levels of acceptance by the addressees of such takeover bids allow the attainment of control thresholds.

Furthermore, within the context of the tender offer to which PT was subject during the 2006 financial year, the abovementioned provision of the bylaws (see reference to article 13 of the Bylaws above) was particularly visible. In fact, under the terms and conditions of the general tender offer over the shares representing PT's share capital, which preliminary announcement was published on 6 February 2006 by the companies Sonacom, SGPS, SA and Sonacom, BV, the removal of the said voting restriction was a condition to which the tender offer was subject.

However, at the General Shareholders Meeting called for 2 March 2007 to vote for the said removal, even though merely within the context of the abovementioned tender offer, the proposal was rejected by a majority of votes cast and without the opposition of the class A shares.

Therefore, the situation remained unchanged, based on the conviction that limitations as provided for under the bylaws contribute to share capital dissemination and a greater transparency of the Company's Corporate Governance.

In this way, the initial part of CMVM's Recommendation seems to be complied with, in the meaning that the measures adopted to prevent (or which effect may be to prevent) the success of takeover bids should respect the interests of the company and its shareholders, which is the basis for all the examples included in the Recommendation.

(2) The Company adopts means of alignment of the interests of its directors with the interests of the company.

Only the final part of the CMVM Recommendation no. 8, pertaining to the individualized disclosure of directors' remunerations, is not complied with.

In fact, it is the Company's understanding that such final part of the CMVM Recommendation no. 8 should not be observed as it does not correspond to the best approach and understanding regarding the disclosure of remunerations. On the contrary, the general practice among other companies consisting in merely disclosing the remunerations paid to members of the management body in overall terms should rather be adopted.

Indeed, the information that is important to disclose to shareholders is the information on the overall value of remunerations paid to the members of the management body, and particularly to the management team in the Executive Committee, and the Company fully discloses such information in detail under this report.

Therefore, the Company disagrees and does not adopt the individualized disclosure of the remunerations of the members of its corporate bodies and it maintains its position that the shareholder's analysis of the performance of the Company's management should be made on an overall basis. It is up to the Compensation Committee to analyse whether the individual remuneration of each director is adequate to the functions performed, and in this way the Company understands that it complies with the ratio of the recommendation by

disclosing enough information for investors to know the costs with the management of the Company.

(3) During the 2007 financial year, PT did not fully comply with the CMVM Recommendation no. 9, since one of the members of the Compensation Committee is a non-executive independent director of the Company, which does not fall within the criteria of independence proposed by the CMVM in § 9 of Chapter I of the Appendix to the CMVM Regulation no. 7/2001.

As referred to in Chapter 3, paragraph 8 of this Corporate Governance Report, a careful consideration of two fundamental concerns underlies the proposal and selection of the members of the Compensation Committee.

On the one hand, the composition of the Compensation Committee by a majority of members that are independent from management, in accordance with the independence requirements as provided for in § 9 of Chapter I of the Appendix to CMVM Regulation no. 7/2001, allows that the respect and prevention of conflicts of Company interests with the interests of the members of the management body in this matter is ensured.

On the other hand, the presence of a non-executive director intends to ensure the articulation of this Committee with the management body. This contributes to the consideration and alignment of Company interests in the structuring and determination of the remunerations of the directors.

Thus, the hybrid model followed by the Company in this matter is aimed at ensuring independence and the best pursuit of the Company's interests, as well as reinforcing efficiency in the determination of the remunerations. For this reason, the Compensation Committee, except for the abovementioned non-executive independent director, does not include any member that renders any other kind of services to the PT Group, or that has a family relationship with members of the management body by way of marriage, kindred, or affinity in a direct line and up to the third degree.

CHAPTER 1. STRUCTURE OF THE PT GROUP

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On 31 December 2007, the PT Group was structured by business lines corresponding to 4 large core areas: Wireline Business, Mobile Business in Portugal (TMN), International Business that includes Vivo (the joint-venture with Telefónica for mobile business in Brazil) and Instrumental Companies. The Business Units are coordinated by the Group's Holding, led by its Executive Committee and with the support of the Corporate Centre, in accordance with the following chart:

Reporting by subsidiaries to the Corporate Centre is functional and not hierarchical, which allows the actual articulation of PT Group's businesses.

Prior to 7 November 2007, PT Group also included a Multimedia Business area, through the subsidiary PT Multimédia and its corresponding subsidiaries. On such date, PT Multimédia was separated from the PT Group, through a spin-off procedure consisting of a free allocation to PT's shareholders of PT's holdings in that company.

CHAPTER 2. CORPORATE GOVERNANCE MODEL

1. CORPORATE GOVERNANCE MODEL AND CHARACTERISTICS OF THE MANAGEMENT BODY

Further to the revision of the Portuguese Companies Code by the Decree-Law no. 76-A/2006, of 29 March, issuers of shares admitted to trading on a regulated market are required to choose between three corporate governance models established by such Code.

The Company is also required, as an entity with securities admitted to trading in the New York Stock Exchange (NYSE) qualifying as one of the issuers known as foreign private issuer, to comply with the mandatory rules set forth in the Sarbanes-Oxley Act, notably the Rule 10A-3 on Listing Standards Relating to Audit Committees of the Securities and Exchange Commission (SEC) and the Final Rules approved by NYSE regarding corporate governance (Section 303A Corporate Governance Standards);

In order to have full compliance with the rules applicable in the United States, the Company created an Audit Committee on 18 December 2003, which operated until 22 June 2007 as an internal committee of the Board of Directors responsible for the supervision of the financial information contained on the financial statements of the Company, the independent auditors, the internal control system and the compliance with the legal and regulatory provisions and orientations applicable to the Company.

The consolidation of the Audit Committee within the Board of Directors has positively contributed to the envisaged attractiveness of the Company in the national and U.S. markets, since the Audit Committee has assumed itself not only as a project publicly recognized as pioneer in Portugal, as it was also positively received by the U.S. market as a structure which allows an effective supervision of the corporate activity, as well as accuracy and transparency in the aspects for which it is responsible.

In this context, the Company s Board of Directors has carried out a deep reflection aiming at introducing the changes to the corporate governance model that were required to comply with

the new legal and regulatory framework. It was understood that the Anglo-Saxon governance model was a solution of continuity regarding the Portuguese and U.S. markets and it will allow an easier comparability of the Company's model with the model imposed to the companies located in the United States of America, as well as with the governance structures with which investors and international analysts are familiarized with, which in effect has proved to be the case.

Therefore, pursuant to the resolution of amendment to the by-laws that was approved at the General Meeting of Shareholders held on 22 June 2007, the Company adopted the Anglo-Saxon corporate governance model, which includes a Board of Directors, an Audit Committee composed by non-executive directors who are elected by the General Meeting of Shareholders and a Chartered Accountant.

The Company's model further includes an Executive Committee with powers delegated from the Board of Directors, which shall act on a predominantly operational basis, and the Board of Directors shall supervise the corporate activities, with the support from the Corporate Governance Committee within the scope of the respective specific powers.

The adopted Governance model keeps a power separation between Board of Directors and Executive Committee, without prejudice to the concentration in a single member of the functions of Chairman of the Board of Directors and Chief Executive Officer (CEO), and is based on four basic pillars: efficiency, simplicity, transparency and accuracy.

In the meantime, on 21 September 2007, the Chief Executive Officer announced that he will propose to the Board of Directors, after the Annual General Meeting of Shareholders for the approval of the year-end accounts, the appointment of Zeinal Bava as the Company's Chief Executive Officer. Mr. Henrique Granadeiro will continue to be the Chairman of the Board of Directors.

2. COMPOSITION OF THE BOARD OF DIRECTORS

The Board of Directors of PT is composed of a minimum number of 15 and a maximum number of 23 members, who are elected at a General Meeting of Shareholders by a majority of the votes cast. Moreover under the terms of the Bylaws, for the election of one third of the total number of directors, which shall include the Chairman of the Board of Directors, such majority shall include the votes of the majority of the class A shares. Irrespective of the share capital held, any shareholder may individually submit proposals for the election of the Board of Directors.

Additionally, and according to corporate law, a minimum of shareholders representing at least 10% of the share capital that voted against the winning proposal in the election of the Board of Directors may appoint a member of the management body. The directors are appointed for a three-year term of office, the election year is considered as a full calendar year and there are no restrictions on the re-election of directors.

As of 31 December 2007, the Board of Directors of PT had the following composition:

| | Board of Directors | Executive Committee | Independent Non-Executive Directors | No. of shares held | First Appointment and Office Term |
|-------------------------------|---------------------------|----------------------------|--|---------------------------|--|
| Henrique Granadeiro | Chairman | CEO | | 150 | 2003 31-12-2008 |
| Zeinal Bava | Member | Vice-CEO (1) | | 63,161 | 2000 31-12-2008 |
| Rodrigo Costa (2) | Member | Vice-CEO | | | 2005 31-10-2007 |
| Luís Pacheco de Melo | Member | Member | | 45 | 2006 31-12-2008 |
| João Pedro Baptista | Member | Member | | | 2006 31-12-2008 |
| António Caria | Member | Member | | 486 | 2006 31-12-2008 |
| Rui Pedro Soares | Member | Member | | 50 | 2006 31-12-2008 |
| António Viana Baptista (3) | Member | | No | 9,008 | 2000 21-2-2008 |

| | Board of Directors | Executive Committee | Independent Non-Executive Directors | No. of shares held | First Appointment and Office Term |
|--------------------------------|--------------------|---------------------|-------------------------------------|--------------------|-----------------------------------|
| Fernando Abril-Martorell (3) | Member | | No | | 2001 12-2-2005 |
| Joaquim Goes | Member | | No | 2,437 | 2000 31-12-2008 |
| Amílcar Morais Pires | Member | | No | 2,146 | 2006 31-12-2008 |
| Armando Vara (3) | Member | | No | | 2006 12-2-2008 |
| Jorge Tomé | Member | | No | | 2002 31-12-2008 |
| Nuno de Almeida e Vasconcellos | Member | | No | 9,890 | 2006 31-12-2008 |
| Rafael Mora Funes | Member | | | | 2007 31-12-2008 |
| João Mello Franco | Member | | Yes | 13,308 | 1998 31-12-2008 |
| Thomaz Paes de Vasconcellos | Member | | Yes | | 2003 31-12-2008 |
| João Xavier de Basto | Member | | Yes | | 2007 31-12-2008 |
| Franquelim Alves | Member | | Yes | | 2006 31-12-2008 |
| Gerald S. McGowan | Member | | Yes | | 2003 31-12-2008 |
| Francisco Soares | Member | | Yes | | 2006 31-12-2008 |
| Fernando Soares Carneiro | Member | | Yes | | 2006 31-12-2008 |
| Luís de Azevedo Coutinho | Member | | Yes | | 2006 31-12-2008 |

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- (1) In the course of the 2007 financial year, the director Zeinal Bava was appointed by the Board of Directors as Vice-CEO of the Company.
- (2) Director Rodrigo Costa resigned from his office in the course of the 2007 financial year.
- (3) Directors Armando Vara, António Viana Baptista and Fernando Abril-Martorell resigned from their offices in the course of the 2008 financial year.

To qualify director independence under the terms of the table above the independence criteria taken into account were the ones established in the CMVM Regulation no. 7/2001 and a Service Order approved by the Company's Board of Directors on 31 January 2008 for such purpose.

Under the terms of these provisions, directors are not considered independent non-executive directors where they are associated to any groups with specific interests in the company or find themselves in a circumstance that may affect their capacity of unbiased analysis and decision-making, including:

- (a) Members of the management body who belong to the management body of a company that is in a control position over the former, as provided for under the Portuguese Securities Code;
- (b) Members of the management body who are holders of, perform management functions in, have a contractual bond with, or act in the name or on behalf of holders of qualified shareholdings equal to or greater than 2% of the share capital or of the voting rights in the Company or of an identical percentage in a company that is in a control position over the Company, as provided for under the Portuguese Securities Code;
- (c) Members of the management body who are holders of, perform management functions in, have a contractual bond with or act in the name or on behalf of holders of qualified shareholdings equal to or in excess of 2% of the share capital or of the voting rights in the competing company;
- (d) Members of the management body who earn any remuneration, even where suspended, from the Company or from any other company in a control or group relationship with the former, except for the remuneration for the exercise of management functions;
- (e) Members of the management body who have a significant commercial relationship with the company or with any company in a control or group relationship with the former, either directly or through a third party. A significant commercial relationship is deemed to exist where there is an important service or goods provider, an important customer or an organizations that receives significant contributions from the company or controlling entity;
- (f) Members of the management body who are spouses, kindred, or have affinity in a direct line and up to the third degree with the persons referred to in the previous paragraphs.

In its turn, independence of the members of the Audit Committee, as such, shall be assessed pursuant to article 414-5 of the Portuguese Companies Code, whereby a person is deemed independent if such person is neither associated with any specific interest group in the company, nor is under any circumstance that is capable of affecting such person's unbiased analysis or decision, notably by virtue of: (a) being the holder or acting in the name or on behalf of a holder of a qualified shareholding equal to or greater than 2% of the company's share capital; or (b) having been re-elected for more than two terms of office, on a consecutive or non-consecutive basis.

It is the Audit Committee's understanding that, in view of the provisions of article 414-5 of the Portuguese Companies Code, all its members are independent. It should be mentioned that, should the CMVM understand that the re-election for any corporate body (not just the supervisory body) is relevant for the purposes of paragraph (b) of article 414-5 of the Portuguese Companies Code, the member of the Audit Committee João de Mello Franco, although elected for the first time for the supervisory body on 22 June 2007, was re-elected for more than two terms of office to perform non-executive functions in the Company's management body.

Furthermore, independence of the members of the Company's Audit Committee is also assessed according to the rules provided for under Rule 10A-3 on Listing Standards relating to audit committees approved by the Securities Exchange Commission and to the Independent Tests set out in Section 303-A on Corporate Governance Standards issued by the New York Stock Exchange (NYSE), which are applicable to such members of the Audit Committee by virtue of the Company being an entity which shares are admitted to trading on the NYSE.

The abovementioned independence criteria are complied with by all the members of the Audit Committee.

It should also be mentioned that the rules on the assessment, by the Company, of incompatibilities, independence and specialisation of the members of the Audit Committee in light of the abovementioned rules are set out in a resolution of the Audit Committee and a Service Order approved by the Board of Directors on 31 January 2008. According to these rules, all the members of the Audit Committee should be considered as independent.

The composition and functions of the Executive Committee, which is the body responsible for the management in the normal course of business of the Company, are described under item 3 below.

Appendix I hereto contains a description of the functions performed by the members of the management body in other companies, with express reference to those performed in other companies of the Group, as well as the professional qualifications and the professional activities performed by those members in the last 5 years.

The composition of the Board of Directors was changed on 12 February 2008, by virtue of the cooptation onto the Board of Directors, on such date, of Francisco Manuel Marques Bandeira, José María Álvarez-Pallete López and Santiago Fernández Valbuena to complete the 2006-2008 term of office.

3. EXECUTIVE COMMITTEE

Composition

The Executive Committee is composed by the following directors:

CEO: Henrique Granadeiro
Vice-CEO: Zeinal Bava
Members: Luís Pacheco de Melo
João Pedro Baptista
António Caria
Rui Pedro Soares

Duties

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The Board of Directors delegated the management in the normal course of business to the Executive Committee, vesting it with all the powers necessary for such purpose, with the exception of those pertaining to the matters referred to hereunder and without prejudice to the faculty of claiming some of the authorities delegated:

- Cooptation of directors;
- Request for the call of General Meetings of Shareholders;
- Annual reports and accounts to be submitted to the approval of the General Meeting of Shareholders;
- Posting bonds and personal guarantees or guarantees *in rem* by the company, the authority for which is reserved to the Board of Directors, without prejudice to the provisions of article 15(h) of the Bylaws;
- Change of the company's registered office;
- Projects for spin-offs, mergers and transformation of the company, to be proposed to the General Meeting of Shareholders, as well as acquisitions, disposals, mergers, spin-offs, as well as the main strategic partnership agreements that involve companies of the PT Group, where, in such instances, such transactions do not constitute mere internal reorganisations of the PT Group within the framework of the general goals and fundamental principles approved by the General Meeting of Shareholders;
- Projects for share capital increases to be proposed to the General Meeting of Shareholders;
- Amendments to the bylaws to be proposed to the General Meeting of Shareholders;
- Definition of the general goals and of the fundamental principles of the policies of the PT Group to be submitted for approval at the General Meeting of Shareholders, notably the definition of the sectors of investment and disinvestment, the policy for geographical expansion of its businesses and the strategic options pertaining, *inter alia*, to the technology to be adopted, network development and service rendering;
- Important extensions or reductions in the Company's business and important modifications to the Company's organization;
- Business plans, budgets and annual investment plans;
- Definition of the amount to be annually proposed to the General Meeting of Shareholders for issuance of bonds or other securities that may be subsequently resolved by the Executive Committee.

4. CORPORATE GOVERNANCE COMMITTEE

In compliance with the applicable legal or regulatory requirements, and so as to adopt existing recommendations and the best international practices, as of 31 December 2007 there is, within the Board of Directors, in addition to the Executive Committee and the Audit Committee, a committee responsible for assessing and developing the corporate governance model.

Composition

- João de Mello Franco, Chairman
- Joaquim Goes
- Jorge Tomé
- Franquelim Alves
- Francisco Pereira Soares
- Rafael Mora

Duties

The Corporate Governance Committee has the duties, powers and responsibilities as required to assist the Board of Directors in the performance of its corporate business supervision function in the following areas:

- Adoption, review and permanent evaluation of the corporate governance model, of internal rules and procedures on the Company's structure and governance, as well as of the Group's conduct principles and practices in compliance with the bylaws and the legal and regulatory provisions, and furthermore of national and international recommendations, standards and best practices on this matter;
- Evaluation of the performance of the Board of Directors.

In particular, the Corporate Governance Committee has the following assignments:

- To propose to the Board of Directors and to revise and re-evaluate the Company's corporate governance model, including its organisation structure, operation, responsibilities and internal rules of the Board of Directors;
- To study, revise and re-evaluate the Group's corporate governance principles and practices, notably concerning Group relations, and particularly Company relations with the market, the Shareholders and other Stakeholders, qualifications, independence and responsibility of Directors, as well as conflict of interest prevention and information discipline;
- To assist the Board of Directors in evaluating its performance with a view to contributing to efficiency and transparency in this procedure;
- To study, revise and re-evaluate the values, principles and practices that must govern the conduct of the Group's employees, including the study, revision, interpretation and supervision of application of the codes of ethics or conduct approved or to be approved by the Company.

During the 2007 financial year, the Corporate Governance Committee carried out various activities aimed at meeting its goals and duties, particularly for the review of the governance model and the Company's governance practices, as well as of the Group's principles and rules of conduct.

For such purpose, the Corporate Governance Committee held 5 meetings during 2007, and discussed mainly the following matters:

- Consideration of company governance and supervision models as provided for under the Portuguese Companies Code as results of the Decree-Law no. 76-A/2006, of 29 March, which culminated in the proposal to the Board of Directors for the adoption of an Anglo-Saxon type model;
- Preparation of the reply to the CMVM Public Consultation no. 3/2007 in respect of the Draft Corporate Governance Code;
- Carrying out a prior evaluation of the implications on PT of Corporate Governance Code that was approved by the CMVM;
- Proposal to the Board of Directors and Audit Committee for the adoption of internal rules and procedures in order to assess the independence of Directors and the incompatibilities, independence and expertise of the members of the Audit Committee;

- Review of the draft Service Order on the definition, identification, decision-making procedure and reporting of transactions with Related Parties;
- Proposal to the Board of Directors for review of the Internal Regulation on transactions of PT Group managers;
- Preparation of a communication to be addressed to the Board of Directors on the degree of compliance by the Company with the rules, recommendations and best practices nationally and internationally applicable in the matter of corporate structure and governance and conduct principles and practices;
- Evaluation of the Board of Directors governance practices;
- Evaluation of the draft Company Governance Report for the 2007 financial year;
- Preparation of the 2008 action plan to be submitted to the Board of Directors;
- Preparation of the self-evaluation report, including the evaluation of the Committee's operation regulation.

5. MANAGEMENT BODY OPERATING RULES

Board of Directors

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Under the terms of article 24 of the Bylaws, the Board of Directors shall set the dates or periodicity of its ordinary meetings and will meet extraordinarily whenever called upon by its Chairman or by two Directors or by the Audit Committee.

The Board of Directors may not function without the presence of the majority of its members in office. The Chairman of the Board of Directors may, in cases of recognized urgency, waive the presence of that majority if the same is ensured through voting by correspondence or by power of attorney, although a Director may not represent more than one other Director.

The Board of Directors resolutions are passed by a majority of votes cast, and the Chairman has a casting vote.

Resolutions passed and voting declarations are recorded on minutes, which shall be signed by all the members of the Board of Directors that participate in the meeting.

The meeting participants may dictate a summary of their interventions to be included in the minutes.

Executive Committee

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To better ensure the performance of its duties according to the criteria adopted on that date, the PT Board of Directors created an Executive Committee to which it delegates management in the normal course functions, while retaining supervision and control functions.

The Executive Committee sets the dates and periodicity of its ordinary meetings and will meet extraordinarily whenever called upon by its Chairman or by two of its members or by the Audit Committee.

The Executive Committee may not function without the presence of the majority of its members in office. The Chairman may, in cases of recognized urgency, waive the presence of such majority if the same is ensured through voting by correspondence or by power of attorney, and also by conference call or video conference.

Voting by correspondence and by power of attorney is permitted, although no member of the Executive Committee may represent more than one other member of the same.

Resolutions are passed by a majority of the votes cast, and the Chairman has a casting vote.

Division of powers within the Executive Committee

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Within the framework of the corporate decision-making procedure concerning PT Group's business lines and Corporate Governance, the members of the Executive Committee are responsible for the following areas:

| Executive Committee | Corporate Assignments | Executive Assignments |
|----------------------------------|---|---|
| Henrique Granadeiro CEO | <ul style="list-style-type: none"> • Strategy • Regulatory Management • Competition • Communication and Corporate Image • Human Resources • Institutional Relations • International Relations • Internal Auditing • Legal Services | <ul style="list-style-type: none"> • PT Centro Corporativo • Fundação PT |
| Zeinal Bava Deputy CEO | <ul style="list-style-type: none"> • Investor Relations • Project of Social Sustainability Model • Integrated Strategy for Information and Innovation Services • Convergence and Distribution Strategy • Integrated Networks Strategy | <ul style="list-style-type: none"> • PT Comunicações • TMN • PT PRO • PT.COM • PT Corporate • PT SI • PT Inovação • PT Wifi • PT Prime |
| Luís Pacheco de Melo Director | <ul style="list-style-type: none"> • Planning and Management Control • Financial Operations and Treasury • Financial Reporting • Corporate Finance • Financial Holdings • Internal Controls and Risk Management • Taxation | <ul style="list-style-type: none"> • PT ACS • Previsão |
| João Pedro Baptista Director | <ul style="list-style-type: none"> • Business Development • Foreign Financial Holdings | <ul style="list-style-type: none"> • PT Investimentos Internacionais • Vivo • PT Móveis • Other Subsidiaries Abroad |
| António Caria Director | <ul style="list-style-type: none"> • Quality and Customer Satisfaction • Strategy for Service Hiring | <ul style="list-style-type: none"> • PT Compras • PT Contact |
| Rui Pedro Soares Director | <ul style="list-style-type: none"> • Marketing • Security Policies • Relations with Regions, Local Authorities and Portuguese Language Communities • Environment and Energetic Efficiency | |

Powers of the Chairman of the Board of Directors and of the Chief Executive Officer

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Since April 2006, the functions of Chairman of the Board of Directors and of the Chief Executive Officer are exercised by the same officer. In this way, as at 31 December 2007, pursuant to the Bylaws and the operating rules of the Board of Directors and of the Executive Committee, the Chairman Henrique Granadeiro accumulated the functions of Chairman of the Board of Directors and of Chief Executive Officer, and so he was entrusted with the following duties:

- To represent the Board of Directors in and out of court;

- To coordinate the activity of the Board of Directors and Executive Committee, and to distribute matters among their respective members, where advisable in light of management conveniences;
- To call and conduct the meetings of the Board of Directors and Executive Committee;
- To watch over the correct execution of the Board of Directors and Executive Committee's resolutions.

In the meantime, on 21 September 2007, the Chief Executive Officer announced that he will propose to the Board of Directors, after the Annual General Meeting of Shareholders for the approval of the year-end accounts, the appointment of Zeinal Bava as the Company's Chief Executive Officer. Mr. Henrique Granadeiro will continue to be the Chairman of the Board of Directors.

Information to the members of the Board of Directors

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Under the terms defined in the relevant delegation of powers, in each meeting of the Board of Directors or whenever necessary, the Executive Committee provides information to the remaining directors about the most relevant facts concerning the execution of the delegated powers, notably about the implementation of the strategic policies and options whose general goals have been defined by the Board of Directors, as well as about the implementation of the business plans, budgets and annual investment plans approved by that same body.

The Executive Committee also provides any additional information on the management status as the Board of Directors deems fit to request, while diligently executing the actions related to any indications that may be conveyed to it by the Board of Directors as a result of any information provided.

Number of meetings of the Board of Directors and of the Executive Committee during the 2007 financial year

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As a rule, the Board of Directors meets monthly but it can, however, meet extraordinarily whenever called by its Chairman or by two Directors or by the Audit Committee. In 2007, there were 16 meetings of the Board of Directors.

The Executive Committee, in its turn, met 36 times during the year of 2007.

6. DIRECTOR REMUNERATION POLICY

Remuneration policy for Executive and Non-Executive Directors

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The remuneration of the directors of the PT Group follows two models in accordance with the best national and international practices:

- **Non-Executive Directors:** Their compensation is determined by an annual fee determined by the Compensation Committee, without attendance tickets, that takes into consideration that some Directors also perform duties in a Board delegated committee to assist the Board in its supervisory function. There is no variable remuneration for non-executive directors.

- **Executive Directors:** The remuneration of Executive Directors is determined by the Compensation Committee taking into account the short- and medium-term performance of the PT Group, as well as such performance as compared to other companies of a similar dimension and business.

The remuneration of the Chairman of the Board of Directors and Chief Executive Officer, as well as the remuneration of the other Executive Directors, is composed of a fixed portion and a variable portion, where this latter one may go up to 120% of the fixed remuneration on an yearly basis, and up to 50% of the fixed remuneration as a multi-year variable remuneration concept.

The value of the fixed remuneration of the Directors was determined on the basis of a benchmark study carried out by an international Human Resources consulting company. In this study, companies integrating the PSI 20, IBEX 35, CAC40, DJ Eurostoxx 50 indexes were analysed, as well as European telecommunications companies comparable to PT.

The determination of the annual variable remuneration to be granted within the Performance Plan as a result of the performance in 2007 takes into consideration the analysis of: (a) PT Total Shareholder Return ratio by the same concept of Group 2 of the DJ Stoxx Telecom,

where the TSR is understood as the sum of the share price variation and the value of the dividend per share; (b) the consolidated revenue growth delta as opposed to the same comparison group; (c) EBITDA growth delta as opposed to the same comparison group; (d) cost control, OPEX reduction; (e) net profit and EPS growth.

The determination of the pluriannual variable remuneration within the Performance Plan shall be calculated each year and cumulatively along the term of office and paid at the end of the same if the weighed average of all indicators during the term-of-office is equal to or greater than 80% of the established goals. This yearly and cumulative calculation shall be made according to the analysis of the following indicators: (a) PT Group ROCE evolution versus the ROCE for Group 2 of the DJ Stoxx Telecom during that same period; (b) net profit and EPS growth in the period; (c) PT TSR ratio versus the TSR ratio of the same abovementioned comparison group in the period; (d) evolution of PT Sustainability Index according to the DJSI methodology; (e) evolution of the PT Group image taking into account the growth of the customer and employee satisfaction index; (f) fulfilment of strategic goals.

In accordance with the CMVM's recommendation in this matter, the directors remuneration policy and the way in which it was implemented in 2006 were presented to the Annual General Meeting of Shareholders held on 27 April 2007, in a text included in the corporate governance report concerning the 2006 financial year.

In the meantime, the Compensation Committee that was elected on 22 June 2007 analysed the remunerations policy text then applicable within the Company and, being in favour of such policy, adopted it for execution until the end of the 2007 financial year.

Therefore, the directors remuneration policy and the way in which it was implemented in 2007 are included in this corporate governance report, in sections 6 and 7 of Chapter 2.

Alignment of Director interests with Company interests

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As describe above, PT strives to align management interests with the Company s and its Shareholders interests, in addition to further taking into consideration the alignment with the interests of its main stakeholders. For such purpose, the annual and pluriannual variable

remuneration of its Directors is dependent on their performance, as well as of its sustainability and the Directors' ability to achieve certain goals that contribute to the strategic goals of the PT Group.

Payments in connection with early termination of Director's agreements

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PT has established with some of its executive directors several individual agreements, whereby, should the directors not be re-appointed once their current term of office lapses, they will be entitled to a compensation not exceeding the remuneration they would earn in the two subsequent years, and a variable compensation was also established in some cases. In consideration of the compensation granted, departing directors undertake not to carry out a business competing with PT for a period as agreed between the parties.

In addition, under those same agreements, should PT remove such Directors from office without just cause, PT shall pay a compensation equivalent to the remuneration they would earn until the end of the then current term of office.

7. DIRECTOR REMUNERATIONS

Fixed and variable remunerations of Executive and Non-Executive Directors

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In 2007, the fixed and variable remunerations earned by executive and non-executive directors were inferior in approximately 31%, in comparison with the remunerations earned in 2006, as per note 45 on the Appendix to the Consolidated Financial Statements included in the Management Report.

Connection between Director remuneration and performance

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In order to maximize good management efforts (comment to the CMVM Recommendation no. 8 and Plan of Action of the European Commission), the variable remunerations actually attributed to the Chairman of the Board of Directors and Chief Executive Office and to each Executive Director were indexed to their performance as officers in the management body of the Company, according to the criteria set forth as relevant in the Company's remuneration policy described above.

Allotment of shares or share call options or other share incentive systems - Bonuses, non-financial benefits and profit sharing

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There are no share allotment, share call option or other share incentive system plans, nor any bonuses or non-financial benefits of any nature, profit sharing included.

See also the information set out in note 9 on the Appendix to the Consolidated Financial Statements included in the Report and Accounts.

Payments due for termination of office

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During the 2007 financial year, PT made payments to a former member of the Executive Committee for his early termination of office within the spin-off of PT Multimédia, which amount was determined through the application of the general conditions that were established within the framework of such spin-off, in the amount of 500 thousand euros.

Estimate of other non-financial benefits

Apart from those described above, no other significant non-financial benefits were granted.

In fact, the Chairman of the Board of Directors and the members of the Executive Committee are only granted, as applicable, the benefits set forth for senior officers of the Company.

8. LIST OF THE STRUCTURES SUPPORTING THE EXECUTIVE COMMITTEE

Currently, investor decisions pertaining to the allocation of capital to listed companies take into account not only economic evaluations, but also information transparency and the companies' executive management security and reliability levels. The Executive Committee created, within the scope of the powers delegated by the Board of Directors, three supporting structures in order to better perform its functions.

The composition and duties of the structures supporting the Executive Committee are as follows:

Consultive Council

*Composition**

- Luís Todo Bom, Chairman
- José de Almeida Mota
- Miguel Amaro (1)
- Aníbal Santos
- João Confraria
- José Manuel Tribolet
- José Lamego
- Ruy de Albuquerque (2)
- João Ribeiro da Fonseca
- Amílcar Martins

-
- (1) Termination of office on 31 December 2007.
 - (2) Consultive Council member Ruy de Albuquerque passed away during the course of the 2007 financial year.

Duties

The mission of the Consultive Council is to ponder, together with the Executive Committee, over major strategic issues faced by the PT Group, contributing to a corporate management of excellence.

The activity of the Consultive Council consists in contemplating, together with the Executive Committee, areas with special relevance for PT or issues which level of importance so advise, notably regulation, competition, international investments, mergers, acquisitions and disposals, technological strategies and their implication in the Group's business structure.

It is incumbent on the members of the Consultive Council, as to activities and shareholdings held or to be acquired by the PT Group to:

- Provide the Chief Executive Officer and the Executive Committee with information, analyses and opinions on matters of a regulatory, technological, economic and corporate nature;
- Analyse relevant aspects of economic trends, both as to the present and as to future prospects, notably with regard to factors capable of influencing or enhancing the PT Group business;
- Assist the Chief Executive Officer and the Executive Committee in developing corporate strategies and the best management practices;
- Issue opinions and recommendations on any matters eventually submitted to its evaluation by the Chief Executive Officer or by the Executive Committee.

The Consultive Committee held 8 meetings during the 2007 financial year, and discussed mainly the following matters:

- Optimisation of Short Term Results versus New Technologies and Capacities;

- High Investment in Broadband versus Regulatory Pressure for Open Networks and Price Reduction;
- Distribution of Results versus International Growth and Expansion;
- Priority Markets and International Growth Strategy
- The PT Group vis-à-vis its new competitor PT Multimédia.

Disclosure Committee

Composition

- Luís Sousa de Macedo, Chairman
- Francisco Nunes
- Nuno Prego
- Nuno Machado*
- Carlos Cruz

*Termination of functions during the 2007 financial year.

Duties

It is incumbent on the Disclosure Committee to: define, document and disclose procedures as appropriate for a proper collection, processing and report of information, as well as to revise all information disclosed by PT, notably: press releases, reports and accounts (annual and interim), Forms 20-F, notices to the CMVM and questionnaires sent to the media.

For such purpose, the Disclosure Committee shall approve and implement procedures and controls as required to ensure that information disclosure by PT to shareholders and investors: (i) complies with applicable laws and regulations; (ii) is accurate, complete and made in due time, and (iii) reliably represents the Group's financial position and the results of its operations in all respects as materially relevant for proper knowledge of its financial condition and performance.

The Disclosure Committee held 7 meetings during the 2007 financial year, and discussed mainly the following matters:

- Financial information to be disclosed to the market, taking into account financial and non-financial information reported by its subsidiaries;
- Review of quarterly, interim and annual result disclosures.

Sustainability Committee

Composition

- Henrique Granadeiro (Chairman)
- João Pedro Guimarães
- Luís Sousa de Macedo
- José Pedro Pereira da Costa*
- Luís Avelar
- Duarte Calheiros*
- Gonçalo Pinto Coelho
- Graça Galvão
- Miguel Amaro
- Francisco Nunes
- Nuno Prego
- Luís Moura*
- Diogo Horta e Costa
- Abílio Martins

* Termination of functions during the 2007 financial year.

Duties

It is the Sustainability Committee's responsibility to ensure that corporate sustainability is a part of and consistent with the Group's strategy and transversal to all its companies.

In order to pursue such goals, the Sustainability Committee has the following duties:

- To develop a transversal corporate sustainability strategy that is integrated and consistent with the PT Group's strategy;
- To ensure the creation within the PT Group of the conditions required for its sustainable growth, in a three-dimensional perspective, in economic, environmental and social terms, in accordance with international criteria;
- To develop, promote and supervise projects and actions as required for the proposed goals;
- To identify, define and control the best teams to carry out such projects;
- To strengthen the performance of the Fundação PT within its areas of specific activity, notably of citizenship and philanthropy;
- To guarantee internal and external communication by reinforcing the performance of the PT Group as a sustainable company and making it recognized as such;
- To control and evaluate the action plan as established and incorporated in the sustainability strategy.

The Sustainability Committee is incorporated in the Governance model of the PT Group, and reports directly to the Executive Committee.

During the 2006 financial year, the responsibilities and composition of the Sustainability Committee were redefined. Currently the Sustainability Committee is chaired by the Chief Executive Officer, and Directors of each of the Group's companies, the secretary general and the heads of the corporate units of PT have become part of the same.

Within its duties, the Sustainability Committee approved, for subsequent submission to the Company's Executive Committee, a package of measures notably related to:

- The extension of the certifications of PT Comunicações management systems, in the areas of environment and labour hygiene, health and safety, to the Group's companies not yet certified under such rules;
- The creation of an integrated risk management model;
- The improvement of the sustainable supplier selection and hiring model, notably by including contractual clauses related to Human Rights and the adoption of a supplier monitoring model better adjusted to new selection and hiring conditions; and
- The adoption of a set of energy resources rationalisation and efficient management measures for the Group.

The Executive Committee evaluated the proposals submitted and endeavoured to have the same implemented in the various companies of the Group.

9. SUPERVISION OF THE COMPANY

In accordance to amendments to the bylaws approved at the General Shareholders Meeting held on 22 June 2007, following the coming into force of legislative amendments to corporate governance models as provided for under Portuguese law, the supervision of the company became the responsibility of an Audit Committee and a Chartered Accountant, who were elected for such purpose at the abovementioned General Shareholders Meeting.

Audit Committee

*Composition**

- João de Mello Franco, Chairman
- Thomaz Paes de Vasconcellos
- José Guilherme Xavier de Basto

The Audit Committee, as a corporate body, is exclusively composed of non-executive directors, observing the requirements of article 423-B of the Portuguese Companies Code, which requires that the Audit Committee is composed by a majority of independent members as defined in article 414-5 of that same Code, and that, of such independent members, at least one of them has had higher education as appropriate to carry out his duties and has knowledge of audit and accounting.

* This composition of the Audit Committee was approved at the General Meeting of Shareholders Meeting of 22 June 2007. Until this date, the Audit Committee was composed by the members João de Mello Franco, Luís de Azevedo Coutinho and Thomaz Paes de Vasconcellos and operated as a specific committee within the Board of Directors with delegated powers in the following matters: (1) in the supervision of the quality and integrity of the financial information contained in the Company's account rendering documents, (2) in the evaluation of

the qualification and independence of the Company's External Auditors, (3) in the evaluation of the quality, integrity and efficiency of the Company's Internal Control System, (4) in the evaluation of the execution of the functions performed by the Company's External Auditors and of the Corporate Internal Auditing Office, and (5) in the evaluation of compliance with legal and regulatory provisions, and with recommendations and guidelines issued by competent authorities. Within this context, the Audit Committee held 6 meetings until the abovementioned date.

Duties

As a supervisory body, the Audit Committee has, in addition to all other powers established by law or the bylaws, the following powers:

- To check the accuracy of statutory financial statements and generally supervise the quality and integrity of the financial information contained in the Company's statutory financial statements;
- To control the financial information preparation and disclosure procedure;
- To analyse and issue its opinion on relevant matters connected to accounting and auditing aspects and impact on financial statements of changes to the accounting rules applicable to the Company and to its accounting policies;
- To control the preparation and auditing of the Company's statutory financial statements, as well as to supervise and assess internal procedures on accounting and auditing matters;
- To propose the appointment of the Chartered Accountant to the General Meeting of Shareholders;
- To control the independence of the Chartered Accountant, notably as regards the rendering of additional services;
- Direct and exclusive responsibility as to the appointment, hiring, confirmation or termination of duties and determination of remuneration of the Company's external auditors, as well as to the control over their qualifications and independence, and approval of audit and/or other services to be rendered by such external auditors or by persons associated to the same; the external auditors of the Company must report and be subject to the direct and exclusive supervision of the Audit Committee, who each year shall obtain from and review with the external auditors an External Audit Report;

- To settle any differences between the Executive Committee and the abovementioned external auditors in respect of the financial information to be included in statutory financial statements to be reported to the competent authorities, as well as in respect of the procedure of preparation of the audit reports to be issued by the said external auditors;
- To control the quality, integrity and efficiency of the risk management system, internal control system and internal audit system, including an annual review of their adequacy and efficiency, and generally to supervise the execution of the functions performed within the framework of the Company's internal audit and internal control system;
- To receive reports of irregularities, claims and/or complaints submitted by shareholders, Company employees or others, and to implement procedures aimed at receiving, registering and processing the same when related to accounting and auditing aspects, and internal control procedures on such matters;
- To comment and issue its prior opinion within its powers established by law or by the bylaws, and whenever it deems necessary or appropriate, on any reports, documentation or information to be disclosed or submitted by the Company to the competent authorities.

Since 22 June 2007 and until the end of the financial year, the Audit Committee held four meetings (an average of one every two months) with the presence of all its members.

Notwithstanding the governance model transition and the change in its composition, the Audit Committee now in office, considering its functional equivalence to the former internal committee of the Board of Directors, ensured the continuity of the works in progress and undertook new duties that are typical of a supervisory body. In this way, the following activities were started and/or carried out in the 2007 financial year, by the above two structures (This Committee's activity report for 2007 details the description of these activities):

(1) Activities in general

- Approval of its Internal Regulation in order to accommodate the powers defined under the relevant national legal and regulatory rules, as well as the responsibilities pertaining to compliance with the rules applicable to issuers known as foreign private issuers in the United States;
- Preparation of a self-evaluation report for 2007 and of an action plan for 2008.

(2) Supervision of the quality and integrity of the financial information contained in the Company's accounts

- Analysis of the annual, interim and quarterly financial information disclosed by the Company and of its compliance with the legal, regulatory and accounting requirements in force and discussion on such information at periodic meetings with the executive Director responsible, the External Auditors and/or Chartered Accountant of the Company;
- Opinion on the individual and consolidated Report and Accounts for the first half-year of 2007, as well as opinion on the individual and consolidated Report and Accounts for the 2007 financial year, to be submitted by the Board of Directors to the approval of the General Meeting of Shareholders;
- Participation in the Executive Committee meeting at which the 2007 annual accounts were discussed and approved;
- Supervision of compliance with and adequacy of accounting policies, procedures and practices and value-metrical criteria adopted, as well as regularity and quality of the Company's accounting data, by means of analysis of the reports and audits with the Corporate Internal Audit Office, the External Auditors and the Chartered Accountant;
- Follow up of the issues reported by the External Auditors by reference, notably, to the *Statement of Audit Standards no. 61*, and considering, *inter alia*, the main accounting criteria

- used, the inscription of non-usual and/or non-frequent transactions and the significant judgements adopted;
- Analysis of the procedure of preparation and report of Form-20 to the SEC.

(3) Appointment and supervision of the qualifications and independence of the External Auditors and Chartered Accountant

- Renewal of the agreement with the External Auditor of the Company (based on the evaluation of the work that was developed, qualifications and independence) and assessment of its independence, including, notably, the prior approval of services other than audit or audit-related;
- Proposal for appointment, at the General Shareholders Meeting dated 22 June 2007, of the effective and alternate Chartered Accountant of the Company, and supervision of its independence (considering, in particular, that the chartered accountant does not provide any additional services to the Company).

(4) Supervision of the quality, integrity and efficiency of the internal control and risk management system and of the internal audit and execution of functions by the External Auditors, Chartered Accountant and Corporate Internal Auditing Office

- Supervision of the efficiency of the Company's internal control and risk management system, which was evaluated and revised by the External Auditors and Corporate Internal Auditing Office;
- Analysis and approval of the working plans for the External Auditors and internal auditing function;
- Follow up of the auditing of the financial statements and internal control system carried out by the External Auditors;
- Control of the official audit, by evaluating and discussing the content of the legal account certifications and periodically meeting with the Chartered Accountant;
- Quarterly follow-up meetings as to the work carried out by the Corporate Internal Auditing Office, and monthly meetings for analysis of the main issues raised and of the implementation by the Executive Committee of the proposals submitted in such Office's reports.

(5) Whistleblowing and compliance system

- Receipt and conveyance of any irregularities communicated within the framework of the System for Qualified Communication of Undue Practices, and periodical meetings with the team responsible for handling such communications, which does not hold decision-making powers, aimed at the analysis and decision by the Audit Committee of reported matters and at the system's improvement and internal disclosure;
- For purposes of control of the management of the Company and compliance with provisions applicable under the law, regulations and the bylaws, this Committee carried out, *inter alia*, the following activities: (i) approval of rules on the assessment of independence, incompatibilities and specialisation requirements applicable to its members; (ii) supervision of the internal control system; (iii) evaluation of the external and internal audit and the audit carried out by the Chartered Accountant; and (iv) discussion and analysis of the issues raised by supervisory authorities to the Company having an impact on the financial information or compliance with the accounting policies.

Chartered Accountant

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The effective and alternate Chartered Accountant were elected at the General Meeting of Shareholders of 22 June 2007, upon proposal by the then recently elected Audit Committee, and the following were designated:

Composition

- P. Matos Silva, Garcia Jr., P. Caiado & Associados, Sociedade de Revisores Oficiais de Contas, represented by Pedro João Reis de Matos Silva as Chartered Accountant (Effective)
- Ascensão, Gomes, Cruz & Associado, Sociedade de Revisores Oficiais de Contas, represented by Mário João de Matos Gomes as Chartered Accountant (Alternate)

Duties

The Chartered Accountant has the powers and duties established under the law, and must review the accounts of the Company and check the regularity of the books, accounting records and supporting documents, the extension of cash flow and inventories of any kind of goods or

values belonging to the company or received by the company as security, deposit or otherwise, wherever deemed convenient and in the manner considered as appropriate, the accuracy of the Company's accounts, and whether accounting policies and value-metrical criteria adopted by the Company lead to a correct evaluation of its assets and results.

Up to the election of the new Audit Committee and the Chartered Accountant, on 22 June 2007, the duty of supervision of the Company was exercised, during the 2007 financial year, by a Supervisory Board, according to the law, composed by:

- Pedro João Reis de Matos Silva (Chairman)
- Gonçalo Vaz Botelho (Member)
- Ascensão, Gomes, Cruz & Associado, Sociedade de Revisores Oficiais de Contas, represented by Mário João de Matos Gomes (Member)
- José Vieira dos Reis (Alternate Member).

External Auditors

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During the 2007 financial year, the annual remuneration paid to the Company's External Auditors, Deloitte & Associados, SROC, S.A. (External Auditors), was 2,349,143 Euros, such payment corresponding to the following services:

| | 2006 | % | 2007 | % |
|--|------------------|-------------|------------------|-------------|
| Audit fees | 1,686,520 | 60% | 1,857,274 | 79% |
| Audit related fees | 679,890 | 24% | 277,978 | 12% |
| Tax fees | 52,003 | 2% | 18,900 | 1% |
| Other fees not audit nor audit-related | 382,455 | 14% | 194,991 | 8% |
| Total | 2,800,868 | 100% | 2,349,143 | 100% |

In order to safeguard the independence of External Auditors, the following powers of the Audit Committee exercised during the 2007 financial year both as a delegated committee of the Board of Directors, until 22 June 2007, as well as, after such date, as an autonomous corporate body elected at the General Meeting of Shareholders, should be highlighted:

- Appointment and hiring of External Auditors and responsibility for establishing their remuneration, as well as pre-approval of any services to be hired from the External Auditors;
- Direct and exclusive supervision by the Audit Committee;
- Annually obtaining, directly from the External Auditors, written information on the Auditors' quality control internal procedures, any substantial issues arisen within such control or following the inquiry carried out by competent authorities over the last 5 years, as well as all relations existing between the Company and the Auditors or associated persons, including all services rendered and all services in progress; in fact, the Audit Committee, in order to evaluate independence, obtained from the External Auditors information on their independence in light of the *Independence Standard Board no. 1 Independence Discussions with Audit Committees*;
- Evaluation of the qualifications, independence and performance of External Auditors;
- Definition of the Company's hiring policy concerning persons who have worked or currently work with the External Auditors;

- Review, with the External Auditors, of the scope, planning and resources to be used in their services;
- Responsibility for the settlement of any differences between the Executive Committee and the External Auditors concerning financial information;
- Definition of the annual fee limits to be paid regarding the services supplied by External Auditors and quarterly review of the contracting levels of such services.

Within this context, it should be particularly stressed that External Auditor independence was safeguarded by the implementation of the Company's policy on pre-approval of the services to be contracted with the External Auditors, which results from the application of the rules issued by the SEC on this matter. According to such policy, the Audit Committee makes an overall pre-approval of the service provision proposal made by the Auditors and a specific pre-approval of other services that will eventually be provided by the External Auditors, particularly the services other than audit and audit related .

It should also be stressed that, in accordance with SEC rules, the Audit Committee, within its responsibilities, has defined the rules on the limitations and restrictions the PT Group must comply with should there be an intention to hire employees belonging to the External Auditors company.

10. WHISTLEBLOWING

In 2005, the PT Group implemented a set of procedures called System for Qualified Communication of Undue Practices , or Whistleblowing. Within this System, undue practices mean all acts or omissions, wilful or seriously negligent, which are imputed to the conduct of corporate body members and other managing officers, heads of departments, staff and remaining employees of Group companies, notably in matters pertaining to Accounting, Internal Control or Auditing, that may be reflected in the financial statements or in information sent to the Portuguese regulatory authority, the Portuguese Securities Market Commission (CMVM), or the US regulatory authority, the U.S. Securities and Exchange Commission (SEC), or that may cause damage to the PT Group's assets.

Taking this framework into account, whistleblowing is any communication of information made by any person who believes that there is evidence of any of the following:

- Violation of a law, rule or regulation;
- Bad management;
- Abuse of authority;
- Large fund squandering.

Upon implementation, the existence of the System for Qualified Communication of Undue Practices was made public through personal communication addressed to each of the employees and by the inclusion of a text on the PT Group website.

Any employee or person outside the Group (meaning a person that does not belong to the PT Group's staff – for instance, a shareholder, customer or supplier) may communicate undue practices through a website specifically created for such purpose: <https://napq.telecom.pt>.

The communication is automatically encrypted, it may be sent from any computer (within or outside the PT Group), and its identification is virtually impossible.

Both confidentiality of the communication and the anonymity of the person reporting will be ensured at all times, unless the person concerned unequivocally intends and declares otherwise.

In no case is any kind of retaliation tolerated against those that make the said communications.

The Audit Committee ensures the receipt and follow up of communications, which are first received by a Qualified Communication Analysis Team (NAPQ – Núcleo de Análise de Participações Qualificadas), who processes the communications and sends them to the Audit Committee. The Audit Committee has powers to take the required decisions, making the same known to the CEO and CFO, as well as to other internal or external entities whose involvement is required or justified.

CHAPTER 3. INFORMATION DISCLOSURE

1. CAPITAL STRUCTURE AND MAJOR SHAREHOLDERS

Capital Structure

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Upon completion, on 31 December 2007, of the share capital reduction in the Company, in an amount of 3,091,695 Euros, by means of extinction of 103,056,500 own shares, the share capital in PT is, as from such date, thirty million seven hundred and seventy-four thousand Euros, fully paid up and represented by 1,025,800,000 (one thousand and twenty-five million and eight hundred thousand) shares with a par value of three cents each.

Five hundred of such shares are class A shares, which is equivalent to 0.0000487% of the entire share capital. Under the bylaws, a majority of class A shares must be held by the Portuguese State or other entities belonging to the State sector, and are currently held by Direcção-Geral do Tesouro. The special rights regarding class A shares are described in Chapter 5-3.

All PT ordinary shares are admitted to trading on the Eurolist by Euronext Lisbon regulated market.

Pursuant to a resolution approved at the General Meeting of Shareholders held on 22 June 2007, the Board of Directors is authorised under the bylaws to increase the share capital, on one or more occasions, as provided for by law, up to 15,000,000 Euros, provided however that the Audit Committee gives an opinion in favour of such share capital increase and the increase is preceded by a resolution of the General Meeting of Shareholders established the parameters under which it must be executed, as required by the bylaws.

Major Shareholders**Qualified holdings**

31 December 2007

| Institutions | No. of shares | % of capital |
|--------------------------------|----------------------|---------------------|
| Brandes Investments Partners | 98,943,217 | 9.65% |
| Telefónica | 93,915,644 | 9.16% |
| Espirito Santo Group | 91,311,811 | 8.90% |
| Caixa Geral de Depósitos Group | 65,341,768 | 6.37% |
| Ongoing Strategy Investments | 60,404,969 | 5.89% |
| Telmex | 38,460,000 | 3.75% |
| Fidelity | 23,592,185 | 2.30% |
| Barclays Group | 23,216,664 | 2.26% |
| Capital Group Companies | 22,996,339 | 2.24% |
| Credit Suisse | 22,683,484 | 2.21% |
| Visabeira Group | 22,667,473 | 2.21% |
| Controlinveste Comunicações | 22,284,551 | 2.17% |

Updated information on qualified holdings in the Company may be consulted at www.telecom.pt or the CMVM site.

2. RISK CONTROL SYSTEM

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As a Group whose holding is listed on the Euronext Lisbon and on the New York Stock Exchange and as an organisation having high corporate governance and internal control

demands, the PT Group has since long ago strongly committed itself to a Risk Control System.

Such commitment has gone through different stages along the different phases of the businesses and the Group's evolution, requiring that the degree of formalisation and identification of the adopted model be ever greater, with more evidences in its implementation.

In this way, in order to characterise such phases, and as any constantly dynamic organisation, the Portugal Telecom Group has started this job by building a dictionary of risks at the various levels of interaction with the Company, and intended such dictionary to work as a standard instrument for all potential threats and opportunities faced by the Group's businesses and its framework. Without prejudice to this systematisation work, it is important to mention that, although this systematisation and report exercise only started at a certain time of the Company's life, a non-explicit concern for the surroundings, strategy and operations of the Group's companies was always present in the Executive Committees of such companies.

During a first stage, considering that PT is subject to several demands imposed by regulators on the capital markets where it is listed, it has been sought to ensure, as a first priority, that compliance with all rules was ensured, thus guaranteeing that, at a second stage, implementation of the best risk management practices can be sought, an exercise that is still currently pursued.

To be more precise, PT started its first priority by identifying and evaluating risks related to financial information report, a requirement that was put forward by the Securities and Exchange Commission (SEC), and for such purpose PT identified control goals that PT should implement in order to ensure that procedures, systems and organisation having an impact prior to the execution of the financial report are subject to appropriate and operational controls taking into account the layers of the COSO(1) model, i.e.: (i) Entity Level Controls; (ii) IT Level Controls; and (iii) Process Level Controls.

(1) *Committee of Sponsoring Organizations of the Treadway Commission*

This work was carried out by the Company's Executive Committee, more directly supported by the Executive Committees of instrumental businesses and companies, and one of its major landmarks occurred at the end of 2006, with PT being the first Portuguese company to fully comply with all internal control requirements for financial reporting as required for foreign companies under section 404 of the Sarbanes-Oxley Act. All this work was followed up and supervised by the Company's Audit Committee, which, since its creation, originally as a specific committee within the Board of Directors and, since 22 June 2007, as an autonomous supervisory body composed of non-executive members of such Board elected by the General Meeting of Shareholders, had a very active role in the promotion of an appropriate and operational financial report internal control system.

Upon completion of this work, and in parallel with the same, the Company's Executive Committee, while reinforcing its 2002 commitment and further seeking to create a better support for the creation of an integrated vision of an internal control system not exclusively oriented to compliance, approved, in the end of 2007, the creation of an Internal Control and Risk Management Team, directly dependent of the Chief Financial Officer having responsibilities over the promotion of a vision of a structured and sustainable internal control system that, under the supervision of the Corporate Internal Audit, will allow the PT Group to have a structure capable of segregating the preventive and detective visions of the model that will ensure an efficient risk management in the PT Group.

Based on such commitment, PT has been extending the work already done up to 2007 to other relevant vectors in the Group's internal control structure, by continuing this activity over subsequent years and ensuring that the Group may go forward with a more structured risk management rationale permitting a more effective identification of strategic and operational risks, and making it possible to systematise the existing and the desired internal control levels in these areas.

Without prejudice to this work, the Corporate Internal Audit, as supervisor element of this model, has already started, with the Group's Executive Committees and in parallel with the work described herein, a work of identification and evaluation of such risks in order to build the annual internal audit plan. Such work will be important to contribute to the structuring of an aligned model permitting a reinforcement of the Group's Risk Control System.

As referred to above, the PT Group defined a set of control goals PT intends to see ensured at all times by its Executive Committees responsible for the Group's various procedures, systems and organisation. Such goals are materialised in the Internal Control Manuals in the various companies having a material expression in the PT Group. The definition of such control goals and the controls thereof was based on 2 COSO (applicable to Entity Level Controls and Process Level Controls) and COBIT(2) (applicable to General Information System Controls) references. (2) Control Objectives for Information and Related Technology

During the beginning of 2008 and pursuing the goal of promoting the implementation of an internal control and risk management structure beyond compliance, PT defined a set of minimum internal control requirements, particularly applicable to international businesses, which should serve as additional guidance for the Group in the definition of corporate policies.

Parallel to all the abovementioned work, the Internal Control and Risk Management Team will promote a better operation of the the Group's main procedures, systems and organisation, by seeking to promote efficiency in the same and to create greater sustainable shareholder value. Furthermore greater relevance will be given before the main stakeholders to work communication and approved internal rules, and the following are already in progress: (i) a project aimed at reinforcing a better communication of the ethics and internal control commitments that the Group wishes to establish in the control of relations with third parties, shareholders or suppliers; (ii) continuous training provided to employees in order to reinforce the framework and relevance of the Internal Control and Risk Management System.

In this way, it is important to shortly describe the risks to which the Company is subject, in order to facilitate the comprehension of the existing Risk Control System.

Main risk factors

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As an economic group that carries out its business in several business areas, the PT Group is exposed to various risks, the following being the main risk factors:

(2) *Control Objectives for Information and Related Technology*

- Regulation: To ensure follow-up of regulatory changes, given the threats and opportunities those changes represent for the competitive position of the PT Group within the businesses it is involved in. The Corporate Regulation Office is in charge of regulation risk management and should be up to date on new business regulations applicable to the sector with an impact on the PT Group, as issued by national and international entities.
- Competition: Potential reduction in the wireline service revenues as a result of the progressive effect of the wireline-mobile replacement, as well as the increase in competition by other wireline network operators. The management of this risk is a permanent concern of the Executive Committee of the Company and of its subsidiary companies Executive Committees in the quest for new and better products and services that prove to be innovating and represent value when compared to those of the competition, and that consolidate the image of the PT Group, with the final consumer, as the leader and pioneer in the telecommunications market.
- Technological evolution: Need for investments in ever more competitive businesses and with a recent history of very fast technological changes. The PT Group holds PT Inovação, a company tailored for the technological development of the Group's businesses, in terms of applied investigation, engineering services and the development of innovating solutions and services, both in the domestic and international markets.
- Strategic partnerships: To ensure alliances, joint ventures or other kinds of efficient and effective relationships that positively affect competitive capacity. The Executive Committee of PT and all its other subsidiary companies have been playing a central role in the management of this risk, by reinforcing existing opportunities.
- Selecting, hiring, developing, training and retaining employees: To ensure the capacity for counting on duly motivated persons with the correct abilities in the right places. The Corporate Human Resources Office is in charge of managing this risk by identifying the key elements of the PT Group to then use retaining strategies as appropriate to the segments defined for its management.

- Financial Markets: Change in the expected income from investments made abroad as a result of changes in several variables, notably interest rate and exchange rate. The management of the financial market risk is ensured by the Corporate Finance Office. Portugal Telecom executes agreements regarding a set of derivative financial instruments so as to minimize the risks of exposure to variations in interest and exchange rates. The execution of agreements concerning financial instruments is made after a careful analysis of risks, benefits inherent to this type of transactions and consulting with various institutions acting in this market. Such transactions are subject to prior approval by the Executive Committee and involve a permanent follow-up of the financial markets' evolution and of the positions held by the Company. The Fair Value of these instruments is determined on a regular and periodic basis throughout the year, in order to allow for a continuous evaluation of these instruments and their economic and financial implications.
- Taxation: Evolution of tax legislation and possible interpretations of the application of fiscal and para-fiscal regulations in different manners. The Taxation Team is in charge of managing this risk, by following up all tax regulations and use of tax planning opportunities. This department may be assisted by tax consulting whenever the issues under analysis are more critical, and therefore require the interpretation of an independent entity.
- Communication and Image: Portugal Telecom is a high media exposure company, and for such reason it has a critical risk level related to its ability to communicate its policies and image with its stakeholders and public opinion generally. The Corporate Communication Office is responsible for the management of this risk.
- Developing new products and services: The telecommunications business, within the competitive environment where it is inserted, depends largely on its ability to develop new products and services allowing it to fight against the loss of customers and to increase average revenue per customer.
- Social, environmental and ethical risks: The Company is subject to the general risks of a social, environmental and ethical nature that affect the business of any company or institution.

3. SHARE PRICE EVOLUTION

The following figure represents the evolution of the price of PT shares during the year 2007.

Most relevant facts announced during the 2007 financial year:

- **Announcement of a tender offer launch and update of the target company report** 12 January
- **Non-audited 2006 results** 8 February
- **New update of the tender offer target company report (increase in the shareholder remuneration package)** 20 February
- **Addendum to the updated tender offer target company report (clarification as to the minimum share buyback limit in 2.1 billion Euros)** 27 February
- **General Meeting of Shareholders rejecting approval of success conditions for tender offer** 2 March
- **Acquisition of 1.03% of the share capital through equity swaps**

- **Payment of dividend concerning the 2006 financial year 2 May**
- **Results for the first quarter of 2007 10 May**
- **Accrued acquisition of 2.07% of the share capital through equity swaps 17 May**
- **Accrued acquisition of 3.08% of the share capital through equity swaps 4 June**
- **Accrued acquisition of 4.05% of the share capital through equity swaps 15 June**
- **Accrued acquisition of 5.02% of the share capital through equity swaps 3 July**

- **Accrued acquisition of 6.17% of the share capital through equity swaps 26 July**
- **Results for the first half of 2007 7 August**
- **Strategic partnership with Helios Investors LP for sub-Saharan Africa 13 August**
- **Accrued acquisition of 8.97% of the share capital through equity swaps 13 September**
- **Spin-off terms and conditions 21 September**
- **Acquisition of 9.13% of the share capital through physical settlement of equity swaps 28 September**
- **Spin-off reference price 6 November**
- **Spin-off completion 7 November**
- **Results for the first nine months of 2007 14 November**
- **Accrued acquisition of 10.02% of the share capital through shares brought to balance sheet equity swaps 13 September**

4. DIVIDEND DISTRIBUTION

Dividend distribution policy

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The Company adopts a dividend distribution policy that takes into consideration the business opportunities of the PT Group, investor expectations and the financing needs by shareholders' equity, taking into account the capital's cost and opportunity.

The Board of Directors is exclusively responsible for the proposal of dividend distribution, subject to Portuguese legislation and the Company's bylaws.

According to the Company's bylaws, at least 40% of the distributable profits of PT(3) shall be distributed to the shareholders as dividend, although the General Shareholders Meeting may resolve, with a qualified majority of two-thirds of the votes cast, to reduce or not distribute the dividend.

(3) Calculated in light of the net income evidenced on the individual financial statements and determined according to the accounting principles in force in Portugal, after deduction of retained losses and a 5% allocation to the legal reserve until it has reached 20% of the share capital.

Concerning the resolution approving the application of profits, a majority of votes corresponding to class A shares is necessary to resolve on the distribution of dividend where the same exceed 40% of distributable net profits.

Dividend distributed in the last three financial yeas

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The gross dividend per share pertaining to the last three financial years was as follows:

- 2006 0.475 euros
- 2005 0.475 euros
- 2004 0.35 euros

Within the Tender Offer to which the Company was subject in 2006 and 2007, the Board of Directors submitted to the shareholders a remuneration package that included the payment of an annual dividend of 0.575 Euros per share in 2008-2009.

Therefore, the Board of Directors will submit to the Annual General Meeting of Shareholders a proposal for the allotment to shareholders of an amount of 0.575 euros per share, in respect of the 2007 financial year.

The said shareholder remuneration package also included a remuneration of 2.1 billion Euros for a share buyback programme, at market price, corresponding to the acquisition of a minimum of 16.5% of the share capital as on 31 December 2006, which will continue to be carried out during the 2008 financial year.

On 13 February 2008, the Company informed the market that, within the framework of the share buyback programme in progress, it holds the right to acquire a further 10,765,997 shares through equity swap agreements.

The number of own shares subject to derivative instruments contracted by the Company totalled, on such date, 63,391,786 shares, including an equity swap over 20,640,000 shares contracted under a previous share repurchase programme.

Within the framework of the share buyback programme in progress, the Company had acquired, on such date, a total of 145,808,286 shares equivalent to 12.92% of the share capital prior to the capital reduction executed on 20 December 2007, with the total amount of the share buyback programme then already implemented being 1,434 million euros.

Furthermore, during the 2007 financial year, the Company freely allotted to its shareholders its holding in its subsidiary PT Multimédia, also in accordance with the terms of the abovementioned shareholder remuneration package, thus executing the spin-off of such company and its subsidiaries, within the framework of which 180.6 million shares in PT Multimédia were disposed of.

5. PLANS FOR ALLOTMENT OF SHARES OR SHARE CALL OPTIONS

During the 2007 financial year, the Company did not adopt any share allotment plans or share call options, nor did any such plans remain in force, regarding Group directors or employees.

6. RELEVANT TRANSACTIONS WITH MEMBERS OF CORPORATE BODIES, HOLDERS OF QUALIFIED SHAREHOLDINGS OR COMPANIES WITHIN A CONTROL OR GROUP RELATIONSHIP

See note 45 to the consolidated financial statements included in the 2007 Consolidated Report and Accounts.

7. INVESTOR RELATIONS

It is PT's policy to supply clear and transparent information, on a regular basis, to its shareholders and other members of the financial community.

The Investor Relations Office was created in March 1995 for the purpose of ensuring adequate relations with shareholders, investors, analysts and financial markets generally, in particular

with the Markets and Stock Exchanges where PT is listed and their respective regulatory entities: CMVM and SEC.

This Office regularly prepares presentations, communications and press releases on quarterly, interim and annual results, as well as any inside information affecting the PT Group as a whole. It also provides all sorts of clarifications to the financial community in general - shareholders, investors (both qualified investors and retail) and analysts. Any interested party may have access the Investor Relations Office through the following contacts:

Nuno Prego

Investor Relations Office

Telephone: +351.21.500.1701

Fax: +351.21.500.0800

E-mail: nuno.prego@telecom.pt

Address: Av. Fontes Pereira de Melo, 40-9º, 1069-300 Lisboa

Company Switchboard: +351.21.500.2000

Websites: <http://www.telecom.pt>; <http://ir.telecom.pt>

The Investor Relations Office has a call centre that can be accessed through a free number and that provides clarifications to investors. It is open Monday to Friday, from 9 am to 6 pm.

During the year of 2007, PT pursued its investor relation activities, and held several events, notably road shows, presentations to investors and analysts, meetings and conference calls, and it has taken part in conferences in Europe and the United States.

In 2007, PT held a total of over 200 meetings with analysts and investors. Additionally, PT held meetings in its offices, as well as conference-calls with investors and analysts on a regular basis.

The three roadshows that took place in Europe and the United States, particularly the roadshow that took place in February (after disclosure of the annual results), as well as the one that took place between the end of November and the beginning of December.

The quality of the investor relation activities was once again considered as a reference by the financial community at national and international levels. At international level, PT was distinguished at the IR Magazine Continental Europe Awards 2007 with two prizes:

- Best Investor Relations Officer (Small and Medium Cap)
- Best Investor Relations in Portugal.

At national level, PT was awarded three prizes at the Investor Relations Awards 2007 organised by Deloitte, Diário Económico and Semanário Económico. The prizes received were as follows:

- Best CEO in the Investor Relations area
- Report and Accounts, non-financial sector Honourable Mention
- Best Investor Relations Officer Honourable Mention.

8. COMPENSATION COMMITTEE

The Compensation Committee is elected by shareholders at the General Meeting and serves the purpose of defining the remuneration policy of PT corporate body members and determining the remunerations applicable taking into account the duties performed and the economic position of the Company.

For the completion of this task, the Compensation Committee continuously follows up and evaluates the directors' performance, by checking the extent to which the proposed targets have been achieved, and it meets whenever necessary.

The current composition of the Compensation Committee, appointed by the General Meeting of Shareholders on 22 June 2007, is as follows:

- Álvaro Pinto Correia, Chairman
- João de Mello Franco
- Francisco Esteves de Carvalho

The Member of the Compensation Committee João de Mello Franco is also a Non-Executive Director of PT.

The underlying factor of the proposal for and selection of the Compensation Committee members is the Company's intention of ensuring that a majority of the Compensation Committee members are independent from management, without prejudice to the required articulation of this Committee with the Board of Directors.

In this way, except for the abovementioned non-executive director, the Compensation Committee does not include any other member of the Board of Directors or any member who has any family relationship with members of the management body by way of marriage, kindred or affinity in a direct line and up to the third degree.

9. CHANGE OF CONTROL

PT, in its normal course of business, executed some agreements that may be amended or terminated in case of change of control of the company. Due to their importance, the following shall be highlighted:

- Shareholders' agreement executed on 16 April 1999 between the companies of Group Banque Marocaine du Commerce Extérieur, Holdco, S.A., Telefónica Intercontinental, SA and Portugal Telecom referring to the incorporation of Médi Telecom. Pursuant to the Agreement, in the case of a change of control in any party thereto, the remaining parties shall have a call option under which terms they may require that the shares held in Médi Telecom by the party affected by the change of control are sold to the other parties at its fair market value minus 10%. If such call option is executed by more than one party, the acquisition of the shares held by the party affected by the change of control shall be made pro-rata. In what concerns PT and for the purpose of this agreement, a change of control

shall mean an acquisition, by a direct or indirect competitor of the Group, of a controlling holding in PT.

- **Shareholders Agreement executed on 17 October 2002 between Telefónica and PT, whereby it was agreed that Telefónica Móviles shall have the right to sell all of Brasilcel's shares held by it to PT, which shall be obliged to buy such shares, if there is a change of control in PT or in any of its subsidiaries which directly or indirectly has an interest in Brasilcel. Likewise, PT shall have the right to sell all of Brasilcel's shares held by it to Telefónica, which shall be obliged to buy such shares, if there is a change of control in Telefónica or in any of its subsidiaries which directly or indirectly has an interest in Brasilcel.**

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- Credit Facility in the total amount of 900 million Euros and some loan agreements, in the total amount of 386 million euros, executed on 31 December 2006 with BEI, which grant the lender the right to require the payment of all amounts in debt in case of a change of control in PT.

CHAPTER 4.

EXERCISE OF VOTING RIGHTS AND SHAREHOLDER REPRESENTATION

1. GENERAL MEETING OF SHAREHOLDERS AND VOTING RIGHTS

The General Meeting of Shareholders, composed of shareholders with the right to vote, ordinarily meets once a year or whenever its call is requested to the Chairman of board of the General Meeting of Shareholders by the Board of Directors, by the Audit Committee or by Shareholders representing at least 5% of the share capital.

As at 31 December 2007, the board of the General Meeting of Shareholders of the Company was composed as follows:

- António Manuel da Rocha e Menezes Cordeiro (Chairman)
- Daniel Proença de Carvalho (Vice Chairman)
- Francisco Manuel Leal Barona (Secretary)

According to the Company's Bylaws, each 500 shares grant the right to one vote. Shareholders holding a lesser number of shares may group together and be represented by one of the group members, so as to jointly accumulate the number of shares necessary to exercise the right to vote.

Within the framework of American Depositary Receipts (ADR) or Global Depositary Receipts (GDR) programs having as their object Company shares, the holders of ADR or GDR are considered to be shareholders, while the entity on behalf of whom the shares are registered is considered to be a mere representative of theirs, provided they comply with the conditions provided for in the Bylaws for the exercise of such right. These conditions are communicated to the holders of the right to vote in each notice for the General Shareholders Meeting.

For confirmation of title to voting rights, the Bylaws require proof of the registry of the shares in a book-entry securities account no later than 5 business days prior to the respective meeting, and such shares should remain inscribed in the name of the shareholder until the General Meeting is closed.

A qualified majority of two thirds of the votes cast is required to resolve on the amendment of the Bylaws, at first or second call.

However, if shareholders holding at least half the share capital are present or represented at a General Meeting held on second call, the amendment to the Bylaws may be resolved by a majority of the votes cast.

At a General Meeting of Shareholders resolving on an amendment to the Bylaws, shareholders holding at least shares corresponding to a third of the share capital must be present or represented. The General Meeting may resolve on second call whatever the number of shareholders present or represented, but in this case it must observe the rules on required majorities as to votes cast at General Meetings as described above.

In any case, no resolutions on bylaws amendment matters may be approved against the majority of votes corresponding to class A shares.

Still in the context of the General Meeting, and subject to it, reference must be made to the existence of a Compensation Committee, which composition, powers and activity during the financial year of 2007 are described above.

2. VOTING BY CORRESPONDENCE AND BY ELECTRONIC MEANS

The Company bylaws provide that the voting by correspondence or by electronic means may encompass all matters contained in the notice, under the terms and conditions set forth therein, and voting exercised in this way shall be considered at the time of vote counting by adding the same to the voting rights exercised in the course of the General Meeting.

The Bylaws further provide that the terms and conditions for voting by correspondence or by electronic means shall be defined by the Chairman of the board of the General Meeting of Shareholders, in order to ensure their authenticity, regularity, security, reliability and confidentiality up to voting time.

In any case, vote authenticity shall be ensured before the Chairman of the board of the General Meeting of Shareholders by means of communication having apposed a certified signature according to the law in the case of corporations, or by means of communication accompanied by a simple copy of the identification document in the case of individuals. In order to guarantee vote confidentiality, the said communication shall be sent in a closed envelope that will only be considered at the time of vote counting.

On the other hand, votes cast by correspondence or electronic means are deemed as negative votes as to any resolution proposals submitted at a time subsequent to the time when the same were cast. The presence at a General Meeting of a shareholder having exercised his voting rights by correspondence or electronic means, or his representative, determines the revocation of the vote so cast.

Voting by correspondence

According to the procedures generally followed by PT, the voting by correspondence shall be performed as follows:

- The shareholders entitled to vote may, according to article 22 of the Portuguese Securities Code, exercise such vote by correspondence, provided that, by the time and date scheduled on the notice, a communication addressed to the Chairman of the board of the General Meeting be delivered to the latter, such communication to bear a signature certified by a notary (or, for individuals, a simple signature together with a copy of the relevant ID card), and to include the address to where voting bulletins and other documentation should be sent. In return, the voting bulletins and other relevant documentation will be sent to such shareholders, who shall send to the Chairman of the board of the General Meeting, in such a way as to be received by the time and date scheduled on the notice for the General Shareholders Meeting (a 5-business day term has been adopted so far, but, as from 2009, this term is expected to be reduced to 3 business days), a closed envelope containing the duly filled in voting bulletins.
- Without prejudice to the download of voting bulletins from the Internet according to the next paragraph, there are voting bulletins available to the shareholders at the offices of the Company, and the same may also be provided by hand delivery, by post or by electronic mail.
- Alternatively, shareholders may also download the voting bulletins from the Internet site www.telecom.pt, and send the same, addressed to the Chairman of the board of the General Meeting, duly filled in and in a closed envelope, in such a way as to be received, together with an envelope containing a copy of the ID card (or, for corporations, a document of signature certification as provided for in the applicable law), the declaration of the financial intermediary entrusted with the registration service of the relevant shares.
- In any case, shareholder votes may only be considered if the declaration of the financial intermediary entrusted with the registration of the relevant shares is received no later than 5 business days prior to the General Meeting.

Voting by Electronic Means

As an alternative to voting by correspondence, the holders of voting rights can choose to exercise their voting right by electronic means. However, the Chairman of the board of the General Meeting of Shareholders may subject voting by electronic means to the satisfaction of conditions as he establishes for safety and reliability thereof.

Also according to a practice implemented in the company, shareholders may vote through the Internet site www.telecom.pt, according to the requirements established thereon, provided that, by the time and date scheduled on the notice for the General Meeting of Shareholders, they deliver to the Chairman of the board of the General Meeting a communication, prepared in accordance with the form made available on that same Internet site, to bear a signature certified by a notary (or, for individuals, a simple signature together with a copy of the relevant ID card), and to include the post mail address to where the keyword to be made available by the Company should be sent.

Such shareholders may exercise their voting rights during the period fixed on the notice for the General Shareholders Meeting. Only the votes of shareholders in respect of whom the declaration of the financial intermediary entrusted with the registration service of the relevant shares has been received during the period fixed on the notice for the General Shareholders Meeting may be taken into account.

3. SHAREHOLDER REPRESENTATION

Shareholders may participate directly in the General Meeting or appoint proxies to represent them, within the broadest terms foreseen in the Portuguese Companies Code. A signed letter addressed to the Chairman of the board of the General Meeting of Shareholders is a sufficient instrument of representation.

4. AVAILABILITY OF PREPARATORY INFORMATION

The proposals to be submitted by the Board of Directors to the General Meeting of Shareholders, as well as the reports that must be legally attached thereto and all other preparatory information data, are made available to shareholders at the company's registered office for a period of no less than 15 days prior to the meeting. The content of such documents is also disclosed on the Company's website, both in Portuguese and in English.

So as to facilitate access to such documents, especially by foreign shareholders, the Investor Relations Office will send the same by postal mail, fax or electronic mail, upon request.

In addition, the text of the notice for the General Meeting of Shareholders and of the proposals received by the board of the General Meeting of Shareholders will be available on the company's website sufficiently in advance.

The result of the resolutions of the General Shareholders Meeting is disclosed by the company on its website, as well as through its Investor Relations Office.

CHAPTER 5. CORPORATE RULES

1. CODES OF CONDUCT

Code of Ethics

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The PT Group's Code of Ethics applies to all employees in order to guarantee a set of common ethical standards for all the Group's companies. Its update and implementation are permanently monitored by the Governance Committee.

The goals, values and rules listed in the Code of Ethics incorporate the PT Group's culture, which should preside over the professional conduct of all those who work at its companies and imposes its disclosure with investors, customers, suppliers, regulatory authorities and competitors.

In order to pursue such goals and values, all employees and agents of the PT Group should guide their actions by the following rules as better expressed on the text of the Code of Ethics:

- Protection of shareholder rights and Interests;
- Safeguard of assets in the course of the company's business;
- Duty to undertake a loyal behaviour towards the PT Group, by promoting its prestige;
- Protection of confidentiality and professional secrecy as to any information obtained in carrying out business, including after termination of duties;
- Compliance with the liability limits assigned to each employee;

- Good governance, with zeal and transparency in the management of the PT Group companies;
- Duty to scrupulously comply with the applicable legal and regulatory rules;
- Duty to communicate conflicts of interest and refrain from exercise of functions that may put compliance with the PT Group employee duties in question;
- Duty not to accept or resort to unlawful offer or advantages;
- Transaction limitation as to securities issued by a PT Group company where an employee is in possession of sensitive or inside information;
- Duty to refrain from participating in transactions under conditions other than usual market conditions with entities having trade relations with the PT Group;
- Contribution to the creation of a good inter-person relationship within the PT Group;
- Duty to show high professionalism, respect, honesty, good faith and courtesy when dealing with the customer, by acting notably in such a way as to provide the customer with an efficient assistance and support service;
- Negotiation with suppliers always in observance of the good faith principle and duty to fully honour all commitments to suppliers;
- Observance of competition rules and promotion of a good relationship with competitors;
- Duty to cooperate with regulatory authorities;
- Observance of the principle of equal opportunities and appreciation of professional careers and merit;
- Advancement of safety and welfare at work;
- Rules of conduct as to press releases and advertising;
- Undertaking social responsibility with the communities where the PT Group's corporate businesses are carried out, in order to contribute to their progress and wellbeing.

The full text of the PT Group Code of Ethics is available for consultation on the Company's official website (www.telecom.pt) and may also be made available through the Investor Relations Office.

Code of Ethics for Financial Officers

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In 2004, the PT Group Board of Directors approved the Code of Ethics for Financial Officers, reinforcing the importance of the specific ethical rules applicable to all PT Group employees that are directly or indirectly involved in the preparation, analysis and disclosure of financial statements, press releases or any other information to be disclosed to the markets related to one of the entities that integrate the PT Group.

The Code of Ethics for Financial Officers reinforces the principles of honesty and responsibility and regulates aspects such as the reporting of conflicts of interest, competence and professionalism, professional secrecy, compliance with the laws applicable to the PT Group and the responsibility for disclosure of information. Its scope has been disclosed to all relevant employees by the annual signature of a compliance statement.

This Code is also available on the Company's website.

Internal Regulation on Transactions by the Group's Managers

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In 2006, the transactions by the PT Group's managers were subject to regulation through a Regulation on Transactions by the Group's Managers, which replaced the former Regulation on Transactions for the account of Senior Managers.

This Regulation was issued in line with the amendments implemented by Decree-Law no. 52/2006 of 15 March to the Portuguese Securities Code, notably aiming at extending the objective and subjective scope of the matters and definitions specified under applicable legal and regulatory rules in order to complete the system of rules on Corporate Governance and good conduct practices as already in force for PT and implement by PT in order to strengthen the market abuse prevention.

However, in the current year, the Company thought it should revise such document to adjust its rules to the new conditions and to make swifter the insertion of data in the database implemented by the Securities Market Commission for this purpose swifter, notably taking into

account that since the approval of such Regulation several facts occurred having an effect on the PT Group's structure, particularly the spin-off of its subsidiary PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, S.A. (currently, ZON Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, S.A.).

In this way, such amendment implements the form of compliance with the legal obligations of communication, by the PT Group managers, of the transactions carried out with their participation.

Transactions with Related Parties

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The Company has in force, since 2006, a Regulation on Transactions with Related Parties aimed at implementing a set of procedures towards ensuring a correct identification and disclosure of transactions with related parties, as well as defining the relevant concepts of transaction and related parties .

This Regulation pursues a double purpose: (1) permitting PT s financial statements to evidence, if and where applicable, the possibility of the Company financial position and results being affected by the existence of related parties and by transactions and pending balances for the same; and (2) safeguarding PT s interest in potential conflict of interest situations vis-à-vis the interests of persons or entities understood as having the possibility of influencing, either directly or indirectly, its management.

However, the Company thought it should reformulate some procedures regarding transactions with related parties, and new rules were approved by the Board of Directors on 31 January 2008.

Such rules provide for internal control procedures and mechanisms that ensure the proper identification and disclosure of transactions with related parties, involving a preliminary stage of definition, identification and transparency in the transaction decision-making process, to culminate in the disclosure of relevant transactions according to the Portuguese Securities Code rules and with the Securities Market Commission (CMVM) and United States Securities and Exchange Commission (SEC) regulations.

Sustainable Development and Social Responsibility Policy

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The corporate sustainability strategy in PT is integrated in a consistent and transverse way within the Group and lies on the development and monitoring of practices and procedures at three main levels: economic, environmental and social.

Social, corporate, economic and environmental responsibilities are levels that are intrinsic in this strategy that PT expects to progressively consolidate and renew in a systematic and transverse way as to the Group's business.

Within this framework, PT is the signatory of and actively participates in a number of international organisations connected to the advancement of the best practices leading to sustainable development. PT is a signatory of the sustainability principles of the United Nations Global Compact, the Social Responsibility charter of the Union Network International, the sustainability charter of ETNO – European Telecommunications Network Operators Association, and is a member of the Business Council for Sustainable Development of Portugal (WBCSD).

The sustainability report is published each year, simultaneously with the consolidated report and accounts, and it is prepared in accordance with the guidelines of the Global Reporting Initiative (GRI). The report is audited by an independent external entity. This document outlines the practices and economic, social and environmental references that allow the performance of the company to be highlighted in a tridimensional sustainability perspective, as well as the commitments undertaken by PT before its stakeholders.

This report is also published on the Company's website.

2. INTERNAL RISK CONTROL PROCEDURES

Internal risk control procedures were already specified in connection with the risk control system described under Chapter 3-2 above.

3. MEASURES THAT MAY INTERFERE WITH THE SUCCESS OF TAKEOVER BIDS

Measures existing in the Company that may interfere with the success of takeover bids are described hereinafter.

However, it is PT's understanding that its Bylaws do not contain any defensive clauses the effect of which is to automatically cause erosion in the company's assets in case of change or change in the composition of the management body, and that is not the case notably of the provisions that described below.

This notwithstanding, it was CMVM's understanding, in its Analysis on the Compliance with the Recommendation on the Governance of Listed Companies in 2006, that PT failed to comply with Recommendation no. 4, as already referred to in Chapter 0.

Limitation on the counting of the votes of a single shareholder

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According to article 13 of the company's bylaws, the votes cast by a single holder of ordinary shares, directly or through a representative, on his own behalf or as a representative of another shareholder, that exceed 10% of the total voting rights corresponding to the share capital, shall not be counted.

Class A Shares

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On the other hand, further to the ordinary shares, the share capital in PT is also represented by 500 Class A shares, which may be held only by the Portuguese State or another entity belonging to the public sector: Those shares grant special rights, pursuant to the terms set forth in article 14-2 and article 19-2 of the company's bylaws.

According to these provisions, the following matters may not be approved at a General Meeting of Shareholders against the majority of the votes corresponding to Class A shares:

- Authorization for the acquisition of ordinary shares representing more than 10% of the share

capital by shareholders that directly or indirectly perform, directly or not, activities competing with those of the companies within a control relationship with PT;

- Amendments to the bylaws and share capital increases, as well as the limitation or suppression of pre-emptive rights and the establishing of standards for share capital increases to be resolved by the Board of Directors;
- Issuance of bonds or other securities, establishing the issue value for these securities to be resolved by the Board of Directors and limitation or suppression of pre-emptive rights in the issuance of bonds convertible into shares, as well as establishing the standards for the issuance of such convertible bonds to be resolved by the Board of Directors;
- The passing of resolutions on the application of the financial year results, in the event of a dividend distribution to the shareholders in a percentage in excess 40% of distributable profits;
- Election of the board of the General Meeting of Shareholders, as well as of the Chairman of the Audit and the Chartered Accountant;
- Approval of the general goals and fundamental principles of the Company's policies;
- Definition of the general principles of the policy of shareholdings in companies, as well as, in the cases where those principles require prior authorization by the General Meeting of Shareholders, the passing of resolutions on such acquisitions and sales;
- Moving the Company's registered offices.

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

On the other hand, although this is not a special right of the owners of class A shares properly, it is convenient to stress that the Company's Bylaws determine that, among the members of the Executive Committee designated by the Board of Directors, at least one or two designated directors, according to the Executive Committee being composed of five or seven members, must be elected in accordance with the election rule that grants special rights to owners of class A shares.

Limitations on the transferability of shares, shareholders' agreements and limitations on the ownership of shares

There are no limitations on the transferability of shares, and the company has no knowledge of the existence of any shareholders' agreements.

Under the terms of the Bylaws, shareholders which are, either directly or indirectly, engaged in an activity which competes with an activity being performed by companies in a controlling relationship with PT may not hold more than 10% of the company's ordinary shares without the prior authorization of the General Shareholders Meeting.

APPENDIX

Functions performed by members of the management body in other companies

The functions performed by each of the directors in other companies are as follows:

- **MEMBERS OF THE EXECUTIVE COMMITTEE**

- **Henrique Granadeiro**

Functions in other PT Group companies:

Chairman of the Board of Directors of PT Centro Corporativo, S.A.

Chairman of the Board of Directors of PT Rede Fixa, SGPS, S.A.

Chairman of the Board of Directors of Fundação Portugal Telecom

Chairman of the Board of Directors of Africatel Holdings B.V.

Functions in other companies:

Non-executive Member of the Board of Directors of OPCA - Obras Públicas e Cimento Armado, S.A.

Member of the Board of Directors of Espírito Santo Resources

Member of the Strategic Council of Banco Finantia

Chairman of the Board of the Portuguese-Chinese Chamber of Commerce

Member of the General Council of COTEC Portugal Associação Empresarial para a Inovação

Non-executive Director of Fundação Eugénio de Almeida

Member of the Council of Founders of Fundação Casa da Música

- **Zeinal Bava**

Functions in other PT Group companies:

Chairman of the Board of Directors of TMN - Telecomunicações Móveis Nacionais, S.A.

Chairman of the Board of Directors of PT Comunicações, S.A.

Chairman of the Board of Directors of Portugal Telecom Inovação, S.A.

Chairman of the Board of Directors of PT.Com, Comunicações Interactivas, S.A.

Chairman of the Board of Directors of PT Prime Soluções Empresariais de Telecomunicações e Sistemas, S.A.

Chairman of the Board of Directors of PT Sistemas de Informação, S.A.

Chairman of the Board of Directors of PT PRO, Serviços Administrativos e de Gestão Partilhados, S.A.

Chairman of the Board of Directors of PT Portugal, SGPS, S.A.

Director of PT Rede Fixa, SGPS, S.A.

Director of PT Centro Corporativo, S.A.

Functions in other companies:

Not applicable

- **Rodrigo Costa***

Functions in other PT Group companies:

Chairman of the Board of Directors of PT Comunicações, S.A.

Chairman of the Board of Directors of PT Prime, S.A.

Chairman of the Board of Directors of PT Corporate Soluções Empresariais de Telecomunicações e Sistemas, S.A.

Non-executive Chairman of the Board of Directors of PT Sistemas de Informação, S.A.

Chairman of the Board of Directors of Portugal Telecom Inovação, S.A.

Director of PT Centro Corporativo, S.A.

Director of PT Portugal, SGPS, S.A.

Director of PT Rede Fixa, SGPS, S.A.

Chairman of the Board of Directors of PT.COM, Comunicações Interactivas, S.A.

Functions in other companies:

Member of the Consultive Council for the Technological Plan of Portugal

Member of the High Council for Foreign Investment

* Director Rodrigo Costa resigned from his office in the course of the 2007 financial year

• **Luís Pacheco de Melo**

Functions in other PT Group companies:

Director of PT PRO, Serviços Administrativos e de Gestão Partilhados, S.A.

Director of PT Prestações Mandatária de Aquisições de Gestão de Bens, S.A.

Non-Executive Director of Banco BEST, S.A.

Chairman of the Board of Directors of Previsão Sociedade Gestora de Fundos de Pensões, S.A.

Chairman of the Board of Directors of PT-ACS Associação de Cuidados de Saúde

Chairman of the Board of Directors of PT Imobiliária, S.A.

Director of PT Centro Corporativo, S.A.

Director of PT Rede Fixa, SGPS, S.A.

Member of the Board of Directors of Brasilcel

Director of Africatel Holdings B.V.

Functions in other companies:

Not applicable

- **João Pedro Baptista**

Functions in other PT Group companies:

Chairman of the Board of Directors of Portugal Telecom - Investimentos Internacionais Consultoria Internacional, S.A.

Chief Executive Officer of Africatel Holdings B.V.

Chairman of the Board of Directors of PT Móveis Serviços de Telecomunicações, SGPS, S.A.

Chairman of the Board of Directors of PT Acessos de Internet WI-FI, S.A.

Chairman of the Board of Directors of PT Ventures, SGPS, S.A.

Chief Counsellor of Portugal Telecom Brasil, S.A.

Vice-Chairman of the Board of Directors of Vivo Participações, S.A.

Vice-Chairman of Brasilcel

Chairman of the Board of Directors of Mobitel

Member of the Board of Directors of Universo Online UOL.

Chairman of the Board of Directors of Directel

Member of the Board of Directors of Unitel, SARL

Functions in other companies:

Not applicable

- **António Caria**

Functions in other PT Group companies:

Chairman of the Board of Directors of PT Compras - Serviços de Consultoria e Negociação, S.A.

Chairman of the Board of Directors of PT Contact - Telemarketing e Serviços de Informação. S.A.

Functions in other companies:

Chairman of the General Meeting of Members of APQ - Associação Portuguesa para a Qualidade

- **Rui Pedro Soares**

Functions in other PT Group companies:

Member of the Board of Directors of Portugal Telecom Imobiliária, S.A.

Functions in other companies:

Member of the Board of AIP - Associação Industrial Portuguesa

- **NON EXECUTIVE DIRECTORS**

- **António Viana Baptista***

Functions in other PT Group companies:

- Counsellor of Brasilcel N.V.

Functions in other companies:

Member of the Board of Directors, Delegate Commission and Executive Committee of Telefónica, S.A.

Chief Executive Officer of Telefónica Móviles España, S.A.L.

Chief Executive Officer of Telefónica de España, S.A.L.

Member of the Board of Directors of O2,PLC

Member of the Board of Directors of Telefónica Latinoamérica

* Director António Viana Baptista resigned from his office in the course of the 2008 financial year.

- **Fernando Abril-Martorrel***

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Chief Executive Officer (CEO) of Credit Suisse Spain

* Director Fernando Abril-Martorell resigned from his office in the course of the 2008 financial year.

- **Joaquim Goes**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Director of Banco Espirito Santo, S.A.

Director of BES-Vida, Companhia de Seguros, S.A.

Director of E.S. VENTURES, SCR, S.A.

Director of ESDATA Espirito Santo Data, SGPS, S.A.

- **Amílcar Morais Pires**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Director of Banco Espírito Santo, S.A.

Director of BES-Vida, Companhia de Seguros, S.A.

Director of Banco Espírito Santo de Investimento, S.A.

Chairman of the Board of Directors of Bank Espírito Santo (International) Limited

Director of ESAF - Espírito Santo Activos Financeiros, SGPS, S.A.

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Director of Espírito Santo PLC (Dublin)

Director of Banco Espírito Santo Oriente, S.A.

Chairman of the Board of Directors of BIC International Bank, Ltd (BIBL)

Director of BES Finance Limited

- **Armando Vara***

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Director of Caixa Geral de Depósitos

Chairman of the Board of Directors of IMOCAIXA, S.A.

Chairman of the Board of Directors of SOGRUPO, GI (ACE-Grupo CGD)

Director of Caixa Participações, SGPS, S.A.

Chairman of the Board of Directors of CAIXATEC Tecnologias de Comunicação, S.A.

* Director Armando Vara resigned from his office in the course of the 2008 financial year.

- **Jorge Tomé**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Chief Executive Officer of Caixa Banco de Investimento, S.A.

Chairman of the Board of Directors of Trem II Aluguer de Material Circulante

Director of Sociedade Gestora de Fundos de Investimento Mobiliários CaixaGeste

- **Nuno de Almeida e Vasconcellos**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Chairman of the Board of Directors of Ongoing Strategy Investments, SGPS, S.A.

Chairman of the Board of Directors of Insight Strategic Investments, SGPS, S.A.

Non-executive Director of Heidrick & Struggles

Member of the Board of of Automóvel Clube de Portugal

- **Rafael Luís Mora Funes**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Director of Ongoing Strategy Investments

Member of the Compensation Committee of Impresa

Member of the Compensation Committee of Banco Privado Português

Member of the Supervisory Board of the Business School of INDEG-ISCTE

Member of the Board of Automóvel Clube de Portugal

- **João Mello Franco**

Functions in other PT Group companies:

Vice-Chairman of the board of the General Meeting of Shareholders of PT Pro, Serviços Administrativos e de Gestão Partilhados, S.A.

Functions in other companies:

Chairman of the board of the General Meeting of Shareholders of SIRESP, S.A.

- **Thomaz Paes de Vasconcellos**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Managing Partner of TPV Consultoria e Gestão, Lda.

- **José Xavier de Basto**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Not applicable

- **Franquelim Alves**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Not applicable

- **Gerald McGowan**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Not applicable

- **Francisco Pereira Soares**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Chairman of the Environment Committee of CEEP - European Centre of Enterprises with Public Participation and of Enterprises of General Economic Interest (Centro Europeu de Empresas com Participação Pública e de Interesse Económico Geral, Brussels)

Director of Gadsa Arquivo e Depósito, S.A.

- **Fernando Soares Carneiro**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Member of the Board of Directors and Executive Committee of REN, SGPS, S.A.

- **Luís de Azevedo Coutinho**

Functions in other PT Group companies:

Not applicable

Functions in other companies:

Not applicable

Professional qualifications and professional activities performed during the last 5 years

- **Members of the Executive Committee**

Henrique Granadeiro

Portuguese, 64 years old.

Elected for the first time in 2003. Former term of office ended on 31 December 2005 and was re-elected in 2006 | Chairman of the Board of Directors of PT Multimédia Serviços de Telecomunicações e Multimédia, SGPS, S.A., from 2006 to 2007 | Executive Member of the Board of Directors of PT Multimédia Serviços de Telecomunicações e Multimédia, SGPS, S.A., from 2002 to 2006 | Non-executive Member of the Board of Directors of PT Multimédia Serviços de Telecomunicações e Multimédia, SGPS, S.A., in 2001 | Chairman of the Board of Directors of Cabo TV Madeirense, S.A. | Chief Executive Officer of Lusomundo Media, SGPS, S.A., from 2002 to 2004 | Chief Executive Officer of Diário de Notícias from 2002 to 2004 | Chief Executive Officer of Jornal de Notícias from 2002 to 2004 | Chief Executive Officer of TSF from 2002 to 2004 | Chief Executive Officer of Jornal do Fundão from 2002 to 2004 | Chief Executive Officer of Açoreana Ocidental from 2002 to 2004 | Chief Executive Officer of DN da Madeira from 2002 to 2004 | Chairman of the Board of Directors of Aleluia - Cerâmica Comércio e Indústria S.A. from 2001 to 2004 | Member of the Board of Directors of Parfil SGPS S.A. from 2001 to 2004 | Member of the Board of Directors of Controljornal SGPS S.A. from 1990 to 2001 | Member of the Board of Directors of Sojornal - Sociedade Jornalística e Editorial S.A from 1990 to 2001 | President of Fundação Eugénio de Almeida from 1989 to 1992 | President of IFADAP - Instituto Financeiro de Apoio ao Desenvolvimento da Agricultura e Pescas from 1987 to 1990 | Managing Director of Fundação Eugénio de Almeida from 1981 to 1987 | Member of the Board of Directors of M.N. Tiago, Construções S.A. during 1981 | Member of the Board of Directors of Standard Eléctrica during 1981 | Portuguese Ambassador to the O.E.C.D. from 1979 to 1981 and Head of the Civil House of the President of the Republic of Portugal from 1976 to 1979. He has a degree in Corporate Organization and Business Administration by the Instituto Universitário de Évora (Sociology Department).

Zeinal Bava

Portuguese, 42 years old.

Elected for the first time in 2000. Former term of office ended on 31 December 2005 and was re-elected in 2006 | Chief Executive Officer of PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, S.A., from May 2003 to September 2007 | Chairman of the Board of Directors of TV Cabo Portugal, S.A., from March 2004 to September 2007 | Chief Executive Officer of TMN Telecomunicações Móveis Nacionais, S.A., from December 2005 to May 2006 | Chairman of the Board of Directors of Previsão - Sociedade Gestora de Fundos de Pensões, S.A., from March 2003 to October 2007 | Chairman of the Board of Directors of PT Prestações Mandatária de Aquisições de Gestão de Bens, S.A., from March 2004 to 2006 | Chairman of the Board of Directors of PT Conteúdos Actividade de Televisão e de Produção de Conteúdos, S.A., until September 2007 | Chairman of the Board of Directors of Lusomundo Cinemas, S.A., until September 2007 | Chairman of the Board of Directors of PT Televisão por Cabo, SGPS, S.A., until September 2007 | Member of the Board of Directors of Brasilcel NV from December 2002 to October 2007 | Member of the Board of Directors of Portugal Telecom Investimentos Internacionais, S.A., from April 2004 to April 2006 | Vice-CEO of the Board of Directors of PT Comunicações, S.A., from January 2004 to December 2005 | Member of the Board of Directors of PT Corporate - Soluções Empresariais de Telecomunicações e Sistemas, S.A. from June 2003 to April 2006 | Member of the Board of Directors of PT Sistemas de Informação, S.A., from May 2004 to April 2006 | Member of the Board of Directors of Portugal Telecom Brasil, S.A., from July 2002 to March 2004 | Member of the Board of Directors of Páginas Amarelas, S.A., from January 2004 to May 2005 | Member of the Board of Directors of PT Compras - Serviços de Consultoria e Negociação, S.A., from May 2003 to 2005 | Member of the Board of Directors of BEST - Banco Electrónico de Serviço Total, S.A., from May 2001 to October 2004 | Member of the Board of Directors of Telesp Celular Participações S.A. from April 2001 to December 2003 | Member of the Board of Directors of CRT Celular Participações S.A. from 2003 to 2005 | Member of the Board of Directors of Tele Sudeste Participações, S.A., from 2003 to 2005 | Member of the Board of Directors of Tele Leste Participações, S.A., from 2003 to 2005 | Member of the Board of Directors of Tele Centro Oeste Celular Participações, S.A., from 2003 to 2005 | Vice-President of PT Ventures, SGPS, S.A., from 2000 to 2002 | Merrill Lynch Executive and Relationship Manager for Portugal Telecom, from 1998 to 1999 | Deutsche Morgan Grenfell Executive and Relationship Manager for Portugal Telecom, from 1996 to 1998 | Warburg Dillon Read Executive Manager, from 1989 to 1996. He has a degree in Electronic and Electrotechnical Engineering by the University College, London.

*Rodrigo Costa**

Portuguese, 47 years old.

Elected for the first time in 2005. Term of office ended on 31 de December 2005 and was re-elected in 2006 | Chief Executive Officer of PT Comunicações, S.A., since December 2005 | Member of the Consultive Council for the Technological Plan of Portugal since 2005 | Member of the High Council for Foreign Investment since 2004 | Corporate Vice-President of OEM Microsoft Corporation from 2002 to 2005 | General Manager of Microsoft Brasil from 2001 to 2002 | Member of the Consultive Council of Instituto Superior de Comunicação Empresarial, Human and Social Science College, from 1998 to 2000 | Member of the Board of the Fórum dos Empresários para a Educação from 1997 to 2001 | Manager and Vice-President of the Portuguese-American Chamber of Commerce from 1996 to 2001 | General Manager of Microsoft Portugal from 1990 to 2001 | Partner, Marketing Manager, Distribution Manager and General Assistant Manager of Prológica, S.A. from 1987 to 1990 | General Manager and Founding Partner of Intério S.A. in 1986 | Planning and Control Consultant to Duphar Portugal from 1984 to 1989 | Consultant to the Board of Viagens Abreu from 1983 to 1990 | Director, Partner, Programmer and Systems Analyst of Nogueira Informática, S.A./Groupi, Lda., from 1979 to 1985. He has training in the fields of Information Systems, Finance and Planning, Management, Strategic Marketing, Social Organisation and Human Resources.

* Director Rodrigo Costa resigned from his office in the course of the 2007 financial year.

Luís Pacheco de Melo

Portuguese, 41 years old.

Elected for the first time in 2006 | Executive Director of PT Multimédia - Serviços de Telecomunicações e Multimedia, SGPS, S.A., from June 2002 to April 2006 | Director of Cabo TV Madeirense, S.A., from April 2004 to September 2006 | Chairman of the Board of Directors of Cabo TV Açoreana, S.A., from December 2004 to October 2007 | Director of TV Cabo Portugal S.A., from 2002 to 2006 | Director of Lusomundo Audiovisuais S.A. from 2002 to 2006 | Director of Lusomundo Cinemas S.A. from 2002 to 2006 | Director of Lusomundo Sociedade de Investimentos Imobiliários, SGPS, S.A., from March 2006 to March 2007 | Director of Lusomundo Imobiliária 2, S.A., from March 2006 to March 2007 | Director of PT Conteúdos S.A. from 2002 to 2006 | Director of PT Televisão por Cabo, SGPS, S.A., from 2002 to 2006 | Director of Sport TV from June 2002 to November 2005 | Director of Lusomundo Espanha S.L. from February 2003 to

April 2006 | Central Manager and invited member of the Executive Committee of BES Investimento from 1998 to 2002 | Associate and Director of UBS Warburg from 1994 to 1998. He has a degree in Civil Engineering by the Instituto Superior Técnico with an MBA by IESE Barcelona.

João Pedro Baptista

Portuguese, 49 years old.

Elected for the first time in 2006 | Member of the Audit Committee of the Victoria and Albert Museum in London, since 2005 | Leader of the global telecommunications team in the United Kingdom and partner of Booz Allen Hamilton, from 2005 to 2006 | Global leader for the group of technology, information and entertainment industries of March & McLennan Companies Inc., from 2004 to 2005 | Member of the Executive Committee and partner of Mercer Management Consulting from 1997 to 2005 | Globally responsible person of the technology, information and entertainment group, from 2000 to 2005 | Co-leader for the United Kingdom, from January 2001 to 2005. He has a degree in Mechanical Engineering and a post-graduation studies diploma in Energy by the Federal Polytechnical School of Lausanne, Switzerland, and an MBA by the Stanford Graduate School of Business, Stanford, CA, USA.

António Caria

Portuguese, 55 years old.

Elected for the first time in 2006 | Executive Director of TV Cabo Portugal from 2002 to 2006 | Non-executive Director of Cabo TV Açoreana, S.A. from 2004 to September 2007 | Chairman of the Board of Directors and Managing Director of TV Cabo Tejo from 1998 to 2002 | Managing Director of TV Cabo Lisboa from 2000 to 2002 | Chairman of the Board of Directors of TV Cabo Sado from 1996 to 1998 | Non-executive Director of INESC from 1997 to 2006 | Member of the Board of Fundação CulturSintra from 1999 to 2006 | Member of Associação Empresarial de Setúbal (AERSET) from 1996 to 1998 | Executive Director of Portugal Telecom, S.A., from 1995 to 1996 | Regional Manager in Santarém and Setúbal of Telecom Portugal from 1990 to 1995 | National representative in International Telecommunications Standards Organisations (CEPT and CCITT) from 1983 to 1990 | Engaged to CTT Telecomunicações on 1978, specialising in Automatical, Analogical and Digital Switching, he was responsible for the National Switching Technical Planning at the Engineering Division from 1983 to 1987, and responsible for the first technical-commercial department from 1987 to 1989 | Trainee Engineer at RARET, EDP, and at the technical and professional teaching, Ministry of Education, from

1975 to 1978 | He was granted the title of Specialist in Telecommunications by Ordem dos Engenheiros in 2002 | Commendator of Ordem de Mérito de Pedro Álvares Cabral since 2006. He has a degree in Electrotechnical, Electronic and Telecommunications Engineering by the Instituto Superior Técnico | Post-Graduation in Business Administration by the ISCTE (1988) and by Universidade Nova de Lisboa (1994).

Rui Pedro Soares

Portuguese. 35 years old.

Elected for the first time in 2006 | Executive Director of PT Compras - Serviços de Consultoria e Negociação, S.A., from 2005 to 2006 | Consultant to the Board of Directors of PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, S.A., in the fields of Business Intelligence, Service Quality Evaluation, Security and Real Estate Management, from 2001 to 2004 | Executive in Business Intelligence and Competitive Analysis at Banco Cetelem, Banque Nationale de Paris/Paribas Group, from 2000 to 2001 | Assistant of the Socialist Group at the European Parliament from 1998 to 2000. He has a degree in Marketing Management by IPAM - Instituto Português de Administração de Marketing.

- **Non-Executive Directors**

*António Viana Baptista**

Portuguese, 50 years old.

Elected for the first time in 2000. Former term of office ended on 31 de December 2005 and he was re-elected in 2006 | Member of the Board of Directors of Telesp Celular Participações, S.A., Tele Leste Celular Participações, S.A., Tele Sudeste Celular Participações, S.A., Tele Centro Oeste Participações, S.A. and Celular CRT Participações, S.A. from 2003 to 2006 | Member of the Board of Directors of Telefónica de Argentina, S.A. from 2003 to 2006 | Chairman of the Board of Directors and Chief Executive Officer of Telefónica Móviles España, S.A., from 2002 to 2006 | Member of the Board of Directors of Telefónica International, S.A., from 1998 to 2002 | Director of Latinoamérica, from 1998 to 2002 | Member of the Board of Directors of Telesp, S.A., from 2001 to 2006 | Director of Emergia Holding N.V. since 2000 | Member of the Sponsorship of Fundación Telefónica since 1999 | Member of the Board of Directors of Telefónica Datacorp, SAU, since 1998 | Member of the Board of Directors of Telefónica Perú Holding since 1998 | Member of the Board of Directors of CTC Chile since 1998 | Member of the Board of Directors of

Telefónica Internacional, S.A., from 1998 to 2002 | Member of the Board of Directors of BPI from 1991 to 1996 | Principal Partner of McKinsey & Company from 1985 to 1991 (Madrid/Lisboa Offices). He has a degree in Economy by Universidade Católica de Lisboa, a post-graduation in European Economy by Universidade Católica Portuguesa, and an MBA by INSEAD, Fontainebleau.

* Director António Viana Baptista resigned from his office in the course of the 2008 financial year.

*Fernando Abril-Martorell**

Spanish, 45 years old.

Elected for the first time in 2001. Former term of office ended on 31 de December 2005 and he was re-elected in 2006 | Managing Director and Chief Executive Officer of Credit Suisse Spain. Started working at Credit Suisse in August 2005 | Member of the Board of Directors of Telecomunicações de São Paulo - Telesp from 2001 to 2003 | Chief Operating Officer of Telefónica S.A. from 2000 to 2003 | Chief Executive Officer of Telefónica Publicidad e Información from 1999 to 2000 | Chief Financial Officer of Telefónica, S.A. from 1997 to 1999 | Corporate Finance General Manager of Telefónica Publicidad e Información from 1997 to 1999 | Manager of the Treasury Department of JP Morgan from 1987 to 1997. He has a Law Degree and a graduation in Business Management and Administration by the ICADE (Madrid).

* Director Fernando Abril-Martorell resigned from his office in the course of the 2008 financial year.

Joaquim de Goes

Portuguese, 41 years old.

Elected for the first time in 2000. Former term of office ended on 31 de December 2005 and he was re-elected in 2006 | Member of the Board of Directors of PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, S.A., from August 2002 to September 2007 | Member of the Board of Directors of BEST - Banco Electrónico de Serviço Total, S.A., from May 2001 to July 2007 | Manager of the Strategic Marketing Department of Banco Espírito Santo, S.A., from 1995 to 1999 | Manager of the Strategic Department of CIMPOR - Cimentos de Portugal, S.A., from 1994 to 1995 | Senior Consultant of Roland Berger & Partner from 1992 to 1993 | Consultant of Roland Berger & Partner from 1989 to 1992. He has a degree in Business Administration and

Management | Specialization in Marketing and Finance, by Universidade Católica Portuguesa | MBA by INSEAD, Fontainebleau.

Amílcar de Moraes Pires

Portuguese, 46 years old.

Elected for the first time in 2006. Engaged to Banco Espírito Santo, Finance Department, in 1986 | Appointed Sub-Manager and Head of the Financial Markets and Securities Department in 1989 | Member of the Board of Directors of Soginpar, Sociedade de Gestão de Fundos de Investimento Mobiliário, S.A. from July 1991 to February 1992 | Assistant Manager of the Financial Markets and Securities Department and Member of the Board of Directors of ESER, Soc^a until 1995 | Coordinating Manager of the Finance, Markets and Studies Departments and person responsible for the management of the treasury department of BES | Advisor of the Board of Directors of Banco Espírito Santo, S.A., in July 2000 | General Manager of Banco Espírito Santo, S.A. in March 2003 | Director of Banco Espírito Santo, S.A. since March 2004. He has a degree in Economy Sciences by Universidade Católica Portuguesa.

*Armando Vara**

Portuguese, 53 years old.

Elected for the first time in 2006 | Coordinating Manager of Caixa Geral de Depósitos | Assistant-Minister of the Prime Minister of the XIV Portuguese Government from October 1999 to September 2000 | Minister for Youth and Sports of the XIV Portuguese Government from September 2000 to December 2000. He has a degree in International Relations by Universidade Independente | Post-graduation in Business Administration by the ISCTE - Instituto Superior Ciências do Trabalho e da Empresa.

* Director Armando Vara resigned from his office in the course of the 2008 financial year.

Jorge Tomé

Portuguese, 53 years old.

He was appointed for the first time in 2002. Former term of office ended on 31 de December 2005 and he was re-elected in 2006 | Non-Executive Director of Caixa Gestão de Patrimónios from 2001 to 2005 | Non-Executive Director of BANIF Imobiliária, S.A., from April to June 2001 | Non-Executive Director of BANIF IMO - Sociedade Gestora de Fundos de Investimento Imobiliário from June 2000 to June 2001 | Director of Sociedade Gestora de Fundos de Pensões, S.A.

Açor Pensões, S.A. (currently Banif Açor Pensões), from October 1999 to July 2001 | Executive Member of the Boards of Directors of the following Insurance Companies: O Trabalho and O Trabalho Vida, from May 2000 to July 2001 | Executive Director of Companhia de Seguros Açoreana since December 1996 | Partner of Coopers & Lybrand in Portugal from June 1995 to November 1996 | Manager of Banco Pinto & Sotto Mayor, S.A. with the coordination of the French Branch and Sottomayor Bank of Canada from February to May 1995 | Director of Banco Pinto & Sotto Mayor from March 1994 to January 1995 | Executive Director of SULPEDIP, S.A. (currently PME Investimentos, S.A.), from June 1989 to March 1994 | Technical Officer at the Securities Directorate of Banco Pinto & Sotto Mayor in 1985 | Securities sub-manager and Manager of Banco Pinto & Sotto Mayor from 1986 to 1989 | Director of CPG Sociedade Gestora de Fundos de Investimento FIPOR | Business Analysis and Industrial and Tourism Projects Technical Officer, engaged in April 1983 | Technical Officer of Coopers & Lybrand Lda., engaged in February 1980 | Economist at the IAPMEI (Instituto de Apoio às Pequenas e Médias Empresas e ao Investimento), engaged in 1979. He has a degree in Business Organization and Administration by the ISCTE and an Applied Economy master by the Faculdade de Economia, Universidade Nova de Lisboa.

Nuno de Almeida e Vasconcellos

Portuguese, 43 years old.

Elected for the first time in 2006 | From 1995 to 2006, Managing Partner in Portugal for consulting field of Heidrick & Struggles | Member of the Board of Directors of several companies | Member of the Compensation Committee of a banking entity. He has a degree in Business Administration by the Curry College, Boston.

Rafael Luís Mora Funes

Spanish, 42 years old.

Elected for the first time in 2007 | Director of Ongoing Strategy Investments | Member of the Compensation Committee of Impresa | Member of the Compensation Committee of Banco Privado Português | Member of the Supervisory Board of the Business School of INDEG - ISCTE | Member of the Board of Automóvel Clube de Portugal | He has a degree in Economics and Management by the University of Malaga.

João de Mello Franco

Portuguese, 61 years old.

Elected for the first time in 1997. Former term of office ended on 31 de December 2005 and he was re-elected in 2006 | Member of the Board of Directors of José de Mello Participações, SGPS, S.A., from 2002 to 2006 | Vice-Chairman of the Board of Directors of José de Mello Imobiliária from 2001 a 2004 | Chairman of the Board of Directors of José de Mello Residências e Serviços from 2001 a 2004 | Chairman of the Board of Directors of Imópolis (SGFII) from 2001 a 2004 | Chairman of the Board of Directors of Engimais from 2001 a 2004 | Member of the Board of Directors of International Shipowners Reinsurance Co from 1998 a 2005 | Member of the Senior Council of PT from 1996 to 1997 | Chairman of the Board of Directors of Soponata - Sociedade Portuguesa de Navios Tanques, S.A., from 1997 to 2001 | Chief Executive Officer and Vice-Chairman of the Board of Directors of LISNAVE from 1995 to 1997 | Chairman of the Board of Directors of Marconi from 1994 to 1995 | Chairman of the Board of Directors of Guiné Telecom from 1994 to 1995 | Chairman of the Board of Directors of Companhia Santomense de Telecomunicações from 1994 to 1995 | Member of Board of Directors of CN - Comunicações Nacionais, S.A., from 1993 to 1995 | Chairman of the Board of Directors of Associação Portuguesa para o Desenvolvimento das Comunicações from 1993 to 1995 | Chairman of the Board of Directors of TMN - Telecomunicações Móveis Nacionais, S.A. from 1991 to 1994 | Chairman of the Board of Directors of TLP - Telefones de Lisboa e Porto S.A. from 1989 to 1994 |

Manager of TDC - Tecnologia das Comunicações, Lda. from 1986 to 1989. He has a degree in Mechanical Engineering by the Instituto Superior Técnico | Scholarship by Junta de Energia Nuclear for a specialization in Nuclear Power Plant Mechanical Technology | Additional Training in Strategic Management and High Business Management (PADE).

Thomaz Paes de Vasconcellos

Portuguese, 50 years old.

Elected for the first time in 2003. Term of office ended on 31 December 2005 and he was re-elected in 2006 | General Manager and Member of the Board of Directors of Vendal, ALD, Sfac, Unirent from 1988 to 1998 | Senior Manager of Arthur Andersen & Co., from 1980 to 1987 | Controller of Hubbard Group from 1987 to 1988 | Chartered Accountant no. 561 since 1985, he has been a member and/or the Chartered Accountant of several Supervisory Boards | Managing Partner of TPV Consultoria e Gestão, Lda, since 1999 | He has a degree in Business Management and Administration by Universidade Católica Portuguesa since 1980.

José Xavier de Basto

Portuguese, 69 years old.

Elected for the first time in 2007 | Member of Centro de Estudos da Câmara dos Técnicos Oficiais de Contas (CTOC) | Tax consultant | Retired lecturer at the Faculty of Economics of Coimbra University | He has a Law degree by Coimbra University (1960). Complementary Course in Political Economic Sciences (1961).

Franquelim Alves

Portuguese. 53 years old.

Elected for the first time in 2006 | Director of Cinveste Group between 2006 and 2007 | Chairman of the Board of Directors and Chief Executive Officer of IGCP - Instituto de Gestão do Crédito Público, from 2004 to 2006 | Assistant Secretary of State to the Minister of Economy from 2003 to 2004 | Chairman of the Board of Directors of SIMAB - Sociedade Instaladora de Mercados Abastecedores, S.A. from 2002 to 2003 | Financial Director of Lusomundo Group, from 2000 to 2002 | Director of Lusomundo, SGPS S.A., Lusomundo Net, Diário de Notícias, Lusomundo Media, SGPS S.A. and Lusomundo Audiovisuais, SGPS, S.A., from 2000 to 2002 | Director of PT Multimédia - Serviços de Telecomunicações e Multimédia, SGPS, S.A., from 2000 to 2002 | He has a degree in Economics by the ISE - Instituto Superior de Economia. MBA in Finance by

Universidade Católica. Wharton School Advanced Management Program, University of Pennsylvania.

Gerald S. McGowan

American, 61 years old.

Elected for the first time in 2003. Term of office ended on 31 de December 2005 and he was re-elected in 2006 | Member of the Board of Directors of the Virginia Center for Innovative Technology from 2004 to 2007 | United States Ambassador to Portugal from 1998 to 2001 | Member of the Board of Directors of the Overseas Private Investment Corporation (OPIC) from 1996 to 1997 | Member of the Board of Directors of the Virginia Port Authority from 2002 to 2003 | Member of the Board of Directors of Cellular Telecommunications Industry Association from 1992 to 1994. He has a Law degree by Georgetown University Law Center (J.D. 1974) and Georgetown University (B.S.B.A. 1968)

Francisco Pereira Soares

Portuguese, 58 years old.

Elected for the first time in 2006 | Economic Consultant at the Civil House of the President of the Republic of Portugal, from 2001 to 2006 | Chairman of the Executive Committee of API Capital, Sociedade de Capital de Risco, S.A., from January 2003 to October 2004 | Chairman of the Board of Directors of API Capital, Sociedade de Capital de Risco, S.A., from May 2004 to January 2005 | Director of NAER - Novo Aeroporto, S.A. from 2001 to 2002. He has an Economics degree by ISCEF (Universidade Técnica de Lisboa), 1972 | Master of Science in Management by Arthur D. Little Management Education Institute, Cambridge Massachusetts, EUA (1979) | Master in Public Administration by Harvard University, John F. Kennedy School of Government, Cambridge Massachusetts, USA (1981).

Fernando Soares Carneiro

Portuguese, 58 years old.

Elected for the first time in 2006 | Between 2003 and 2006, economy adviser at the Portuguese Embassy in London and representative of Portugal in the International Organizations of Base Products | Between 2002 and 2003, consultant | Chairman of the Board of Directors of Somincor - Sociedade Mineira de Neves-Corvo, S.A., from 1998 to 2002 | Chairman of the Board of Directors of EDM - Empresa de Desenvolvimento Mineiro, S.A., from 1998 to 2002 | Director of the International Copper Association, from 1998 to 2002 | Director of the European Bank for

Reconstruction and Development from 1993 to 1998 | Director of the World Bank Group from 1989 to 1993 | He has a degree in Mining Engineering by the Instituto Superior Técnico, Universidade Técnica de Lisboa.

Luís de Azevedo Coutinho

Portuguese, 47 years old.

Elected for the first time in 2006 | Invited Assistant Professor at the Economics College, Universidade Nova de Lisboa | Member of the Audit Committee of PT, SGPS, S.A., between 2006 and 2007 | Director and Member of the Audit Committee of EDP - Energias de Portugal S.A., from May 2003 to 2006 | Manager of AMEC - Associação Música, Educação e Cultura, from 2003 to 2005 | Consultant at the Municipality of Lisbon (Câmara Municipal de Lisboa), from 2002 to 2003 | Director of Valora - Serviços de Apoio à Emissão Monetária, S.A., from 1999 to 2002 | Consultant to the Board of Abrantina Group from 2000 to 2007 | Director of the Abrantina Group between 1991 and 1999 | Consultant at the Bank of Portugal, Fundação Calouste Gulbenkian and IPE | He has a degree in Business Management and Administration by Universidade Católica. MBA by Universidade Nova de Lisboa.

On 12 February 2008, José María Alvarez-Pallete López, Santiago Fernández Valbuena and Francisco Manuel Bandeira were co-opted onto the Board of Directors to complete the 2006-2008 term of office.

Glossary

| | |
|------------------------------------|--|
| ADR | American Depositary Receipt. Depositary certificate listed and traded on the New York Stock Exchange in representation of a foreign share. 1 PT ADR = 1 PT share. |
| ADSL | Asymmetric Digital Subscriber Line. Technology that allows high volume data transmission (broadband) over traditional phone lines. |
| ARPU | Average Revenue per User. Monthly average service revenues per average number of users in the period. |
| Capex | Capital expenditure. Investments in tangible and intangible assets. |
| Cash flow | The difference between cash inflows and cash outflows for a specific period. |
| CCPU | Cash Cost Per User. CCPU = monthly average operating costs minus provisions, depreciation and amortisation and sales of equipment per average number of users in the period. |
| CDMA | Code Division Multiple Access. Wireless interface technology for mobile networks based on spectral spreading of the radio signal and channel division by code domain. |
| CRM | Customer Relationship Management. |
| Curtailement costs | Work force reduction programme costs. |
| EBITDA | EBITDA = income from operations + depreciation and amortisation. |
| EBITDA margin | EBITDA Margin= EBITDA / operating revenues. |
| Euronext or Euronext Lisbon | The domestic stock market upon which PT shares are listed and traded. |
| Free cash flow | Free cash flow = operating cash flow +/- acquisitions/sales of financial investments +/- net interest paid payments related with PRB income taxes paid +/- dividends paid/received +/- other cash movements. |
| GAAP | Generally Accepted Accounting Principles. |
| Gearing ratio | Gearing ratio = net debt / (net debt + equity). |
| Goodwill | Goodwill is the excess amount that results if an acquisition cost is higher than the book value of the acquired company. |
| GSM | Global System for Mobile. Internationally standardised digital radio network that allows both voice and data transmission. |
| HDTV | High Definition Television. Transmission of the television signal with a higher resolution than the traditional formats. |
| IAS/IFRS | International Accounting Standards/International Financial Reporting Standards. The new international accountancy standards introduced as of 1 January 2005. |
| Income from operations | Income from operations = income before financials and taxes + workforce reduction costs + losses (gains) on disposal of fixed assets + net other costs. |

| | |
|----------------------------|--|
| IP | Internet Protocol. Standard that specifies the exact format of packets of data as they are transmitted through an Internet network. |
| IPTV | Internet Protocol Television. Digital television service available over a fixed telephony line, through a broadband connection. |
| ISDN | Integrated Services Digital Network. Digital telecommunications network that allows simultaneous voice and data transmission over an access line. |
| ISP | Internet Service Provider. Company that provides access to the Internet. |
| MMS | Multimedia Message Service. Technology allowing for data such as text, tunes, pictures, photos and brief video sequences to be transmitted via mobile phone. |
| MOU | Minutes of Usage. Monthly average of outgoing and incoming traffic in minutes per average number of users in the period. |
| NYSE | New York Stock Exchange. |
| Operating cash flow | Operating cash flow = EBITDA - capex +/- change in working capital +/- non-cash provisions. |
| Pay to basic ratio | Pay to basic ratio = total premium subscriptions per number of Pay TV customers. |
| PRB | Post Retirement Benefits Costs. |
| PSTN | Public Switched Telephone Network. Traditional telephone system that runs through copper lines. |
| SARC | Subscriber Acquisition and Retention Cost. $SARC = (70\% \text{ of marketing and publicity costs} + \text{commissions} + \text{subsidies}) / (\text{gross additions} + \text{upgrades})$. |
| SEC | US Securities and Exchange Commission. The US regulator for capital markets. |
| SMS | Short Message Service. Short text messages service for mobile handsets, allowing customers to send and receive alphanumerical messages. |
| Triple-play Offer | Integrated offer of voice, television and Internet services. |
| VoD | Video-on-demand. System that allows users to select and watch videos. |
| 3G | 3Generation. Third generation is a generic term, covering several technologies for mobile networks (UMTS, W-CDMA and EDGE), that integrate mobile multimedia services and allows a higher data transmission rates than GSM technology. |

Board of Directors

Chairman and CEO

Henrique Granadeiro

Deputy CEO

Zeinal Bava

Executive officers

Luís Pacheco de Melo

João Pedro Baptista

António Caria

Rui Pedro Soares

Non-executive officers

Santiago Fernández Valbuena

José María Álvarez-Pallete López

Joaquim Goes

Amílcar de Moraes Pires

Francisco Marques Bandeira

Jorge Tomé

Nuno de Almeida e Vasconcellos

Rafael Mora Funes

João de Mello Franco

Thomaz Paes de Vasconcellos

José Xavier de Basto

Franquelim Alves

Gerald McGowan

Francisco Pereira Soares

Fernando Soares Carneiro

Luís de Azevedo Coutinho

Key figures

Financial data by business segment

Euro million

| | Wireline | | TMN | | Vivo | | Other | |
|----------------------------|----------|---------|---------|---------|---------|---------|-------|--------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Operating revenues | 1,962.4 | 2,071.8 | 1,542.9 | 1,502.4 | 2,463.0 | 2,104.7 | 180.1 | 86.4 |
| EBITDA | 1,008.8 | 1,072.9 | 679.0 | 658.7 | 595.0 | 496.2 | 73.9 | 9.2 |
| EBITDA margin (%) | 51.4 | 51.8 | 44.0 | 43.8 | 24.2 | 23.6 | n.m. | n.m. |
| Capex | 292.1 | 238.5 | 198.0 | 188.6 | 359.9 | 386.8 | 64.4 | 53.8 |
| EBITDA minus Capex | 716.7 | 834.3 | 481.0 | 470.1 | 235.1 | 109.4 | 9.5 | (44.6) |
| Capex as % of revenues (%) | 14.9 | 11.5 | 12.8 | 12.6 | 14.6 | 18.4 | n.m. | n.m. |

Consolidated financial data

Euro million

| | 2007 | 2006 | y.o.y |
|------------------------------------|----------|----------|---------|
| Operating revenues | 6,148.4 | 5,765.3 | 6.6% |
| EBITDA | 2,356.7 | 2,237.0 | 5.3% |
| Income from operations | 1,233.6 | 1,106.3 | 11.5% |
| Net income | 741.9 | 866.8 | (14.4)% |
| Total assets | 13,122.2 | 14,171.2 | (7.4)% |
| Net debt | 4,381.8 | 3,756.6 | 16.6% |
| Total shareholders' equity | 2,081.8 | 3,106.0 | (33.0)% |
| Share capital | 30.8 | 395.1 | (92.2)% |
| Gearing (%) | 67.8 | 54.7 | 13.1pp |
| EBITDA margin (%) | 38.3 | 38.8 | (0.5pp) |
| Net debt / EBITDA (x) | 1.9 | 1.7 | 0.2x |
| Adjusted net debt / EBITDA (x) (1) | 2.3 | 2.3 | 0.0x |
| EBITDA / net interest (x) | 11.9 | 10.2 | 1.8x |
| Capex | 899.3 | 867.7 | 3.6% |
| Capex as % of revenues (%) | 14.6 | 15.1 | (0.4pp) |
| EBITDA minus Capex | 1,457.4 | 1,369.3 | 6.4% |
| Total group employees | 28,638 | 30,682 | (6.7)% |
| Domestic market | 10,338 | 11,336 | (8.8)% |
| International market | 18,300 | 19,346 | (5.4)% |

(1) Net debt plus after-tax unfunded post retirement benefit obligations divided by EBITDA excluding PRB.

Operating figures

Customer base (000)

| | 2007 | 2006 | y.o.y |
|-------------------------|-------------|-------------|--------------|
| Wireline | 4,176 | 4,404 | (5.2)% |
| Mobile | 39,745 | 34,757 | 14.4% |
| Broadband (ADSL retail) | 652 | 685 | (4.9)% |

Wireline

| | 2007 | 2006 | y.o.y |
|---------------------------------|--------|--------|---------|
| Main accesses (000) | 4,176 | 4,404 | (5.2)% |
| Retail accesses | 3,682 | 4,001 | (8.0)% |
| PSTN/ISDN | 3,010 | 3,317 | (9.2)% |
| Traffic-generating lines | 2,772 | 2,909 | (4.7)% |
| Carrier pre-selection | 238 | 408 | (41.7)% |
| ADSL retail (1) | 652 | 685 | (4.9)% |
| TV subscribers | 21 | 0 | n.m. |
| Wholesale accesses | 494 | 403 | 22.6% |
| Unbundled local loops | 291 | 196 | 48.7% |
| Wholesale line rental | 140 | 142 | (1.4)% |
| ADSL wholesale | 62 | 65 | (3.5)% |
| Net additions (000) | (227) | (74) | n.m. |
| Retail accesses | (319) | (353) | (9.8)% |
| PSTN/ISDN | (306) | (453) | (32.3)% |
| Traffic-generating lines | (136) | (285) | (52.2)% |
| Carrier pre-selection | (170) | (168) | 1.4% |
| ADSL retail | (33) | 100 | n.m. |
| TV subscribers | 21 | 0 | n.m. |
| Wholesale accesses | 91 | 279 | (67.4)% |
| Unbundled local loops | 95 | 124 | (22.9)% |
| Wholesale line rental | (2) | 142 | n.m. |
| ADSL wholesale | (2) | 13 | n.m. |
| Pricing plans (000) | 4,304 | 2,827 | 52.2% |
| ARPU (Euro) | 30.4 | 30.1 | 1.1% |
| Voice | 24.5 | 25.0 | (2.2)% |
| Data and other | 5.9 | 5.0 | 17.5% |
| Total traffic (million minutes) | 12,502 | 13,442 | (7.0)% |
| Retail traffic | 5,217 | 5,575 | (6.4)% |
| Wholesale traffic | 7,285 | 7,867 | (7.4)% |
| Retail MOU (minutes / month) | 159 | 158 | 0.6% |
| Employees | 6,354 | 7,181 | (11.5)% |
| Fixed lines per employee | 657 | 613 | 7.2% |

(1) Includes a database cleanup (related with inactive prepaid broadband customers) of 103 thousand.

Domestic mobile _ TMN (1)

| | 2007 | 2006 | y.o.y |
|-----------------------------------|-------|-------|---------|
| Customers (000) | 6,261 | 5,704 | n.m. |
| Net additions (000) | 558 | 391 | n.m. |
| MOU (minutes) | 121 | 120 | n.m. |
| ARPU (Euro) | 19.8 | 21.0 | (5.7)% |
| Customer | 15.8 | 16.6 | (4.5)% |
| Interconnection | 3.5 | 3.8 | (7.5)% |
| Roamers | 0.5 | 0.6 | (24.9)% |
| ARPM (Euro cents) | 16.4 | 17.5 | (6.0)% |
| Data as % of service revenues (%) | 16.0 | 13.3 | 2.8pp |
| SARC (Euro) | 46.9 | 55.1 | (14.9)% |
| Employees | 1,144 | 1,140 | 0.4% |

(1) Includes MVNO subscribers.

Brazilian mobile _ Vivo

| | 2007 | 2006 | y.o.y |
|-----------------------------------|--------|--------|---------|
| Customers (000) | 33,484 | 29,053 | n.m. |
| Net additions (000) | 4,430 | (752) | n.m. |
| MOU (minutes) | 77 | 74 | n.m. |
| ARPU (R\$) | 30.4 | 27.1 | n.m. |
| Customer | 17.3 | 15.7 | n.m. |
| Interconnection | 13.1 | 11.5 | n.m. |
| Data as % of service revenues (%) | 7.9 | 6.8 | 1.1pp |
| SARC (R\$) | 109.7 | 130.7 | (16.1)% |
| Employees | 5,600 | 5,896 | (5.0)% |

Additional information to shareholders

Listing

PT shares are listed on the Euronext Stock Exchange (symbol: PTC.LS) and the New York Stock Exchange, as ADRs-American Depository Receipts (symbol: PT). One ADR represents one ordinary share.

The company's share capital, as at 31 December 2007, comprised 1,025,800,000 shares with a par value of 3 cents each, with 1,025,799,500 shares listed on the Euronext and the New York Stock Exchange. There were 48,731,494 ADRs registered on the same date, representing 4.8% of PT's total share capital.

Stock Market Data

| | 2007 | 2006 |
|--|---------------|---------------|
| As at 31 December | | |
| Share capital (Euro) | 30,774,000 | 395,099,775 |
| Number of shares | 1,025,800,000 | 1,128,856,500 |
| Price (Euro) (1) | 8.93 | 8.22 |
| Market capitalisation (Euro million) | 9,160 | 11,108 |
| Gross dividend per share (Euro) (2) | 0.575 | 0.475 |
| Dividend yield | 6.4% | 5.8% |
| Net income (Euro million) | 742 | 867 |
| Pay-out ratio | 79.5% | 61.9% |
| Price / transactions | | |
| High (Euro) (1) | 9.60 | 8.60 |
| Low (Euro) (1) | 8.02 | 6.76 |
| Volume (million of shares) | 1,343 | 1,220 |
| Traded Value (Euro million) | 13,343 | 12,207 |
| % of total traded volume (Euronext Lisbon) | 14% | 23% |
| Performance | | |
| Portugal Telecom (1) | 8.6% | 15.1% |
| PSI-20 | 16.3% | 29.9% |
| DJ Stoxx Telecom Europe | 14.6% | 16.9% |

(1) Prices adjusted by the spin-off of PT Multimédia. (2) Subject to Shareholder's approval at the AGM to be held on 28 March 2008.

Financial timetable 2008

28 February

Full year results 2007

28 March

Annual General Shareholders Meeting
Form 20-F filing with the SEC

8 May

First quarter results 2008

7 August

First half results 2008

13 November

First nine months results 2008

Contacts

Investor relations

Nuno Prego

Investor Relations Director

Portugal Telecom

Avenida Fontes Pereira de Melo, 40

1069 - 300 Lisboa, Portugal

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Fax: +351 21 500 0800

E-mail: nuno.prego@telecom.pt

Shareholders, investors, analysts and other interested parties should send their requests for information and clarifications (annual and half year reports, Form 20-F, press releases, etc).

Depository bank

The Bank of New York

ADR Division

101 Barclay Street, 22nd Floor

New York, NY 10286, USA

Tel: +1 212 815 2367

Fax: +1 212 571 3050

Holders of ADRs may also request additional information directly from PT's depository bank for ADRs in New York.

Website

All publications and communications, in addition to information on the company's products, services and business are also available at **www.telecom.pt**

Registered office

Portugal Telecom, SGPS, SA

Avenida Fontes Pereira de Melo, 40

1069-300 Lisboa, Portugal

Tel: +351 21 500 2000

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: April 18, 2008

PORTUGAL TELECOM, SGPS, S.A.

By: **/s/ Nuno Prego**
Nuno Prego
Investor Relations Director

FORWARD-LOOKING STATEMENTS

This document may contain forward-looking statements. These statements are statements that are not historical facts, and are based on management's current view and estimates of future economic circumstances, industry conditions, company performance and financial results. The words anticipates, believes, estimates, expects, plans and similar expressions, as they relate to the company, are intended to identify forward-looking statements. Statements regarding the declaration or payment of dividends, the implementation of principal operating and financing strategies and capital expenditure plans, the direction of future operations and the factors or trends affecting financial condition, liquidity or results of operations are examples of forward-looking statements. Such statements reflect the current views of management and are subject to a number of risks and uncertainties. There is no guarantee that the expected events, trends or results will actually occur. The statements are based on many assumptions and factors, including general economic and market conditions, industry conditions, and operating factors. Any changes in such assumptions or factors could cause actual results to differ materially from current expectations.
