PORTUGAL TELECOM SGPS SA
Form 20-F
June 30, 2005

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

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

OR

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

For the fiscal year ended December 31, 2004

OR

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

Commission file number 1-13758

PORTUGAL TELECOM, SGPS, S.A.

(Exact name of Registrant as specified in its charter)

Republic of Portugal
(Jurisdiction of incorporation or organization)

Av. Fontes Pereira de Melo, 40, 1069-300 Lisboa Codex, Portugal
(Address of principal executive offices)

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

Title of each class	Name of each exchange on which registered
American Depositary Shares, each representing one ordinary share, nominal value €1 per share	New York Stock Exchange
Ordinary shares, nominal value €1 each	New York Stock Exchange*

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

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

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

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

Ordinary shares, nominal value €1 per share	1,166,484,550
Class A shares, nominal value €1 per share	500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ý No o

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 o Item 18 ý

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CERTAIN DEFINED TERMS

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

PRESENTATION OF FINANCIAL INFORMATION

We publish our financial statements in Euro, the single European currency adopted by certain participating member countries of the European Union, including Portugal, as of January 1, 1999. Unless otherwise specified, references to "Euros," "EUR" or "€" are to the Euro. References herein to "U.S. dollars," "$" or "US$" are to United States dollars. References to "Escudos" or "PTE" are to Portuguese Escudos. References to "Real," "Reais" or "R$" are to Brazilian Reais. Certain Euro amounts have been translated into U.S. dollars at specified rates. Unless otherwise indicated, U.S. dollar equivalent information for amounts in Euro is based on the noon buying rate in the City of New York for cable transfers in Euros as certified for United States customs purposes by the Federal Reserve Bank of New York on June 22, 2005. For convenience and comparability, figures previously stated in Escudos have been converted to figures in Euros based on the fixed Escudo/Euro exchange rate of PTE 200.482 = €1.00. We are not representing that the Euro or US$ amounts shown herein could have been or could be converted into US$ or Euros, as the case may be, at any particular rate or at all. See "*Item 3 Key Information Exchange Rates*" for further information regarding the rates of exchange between Euros and U.S. dollars.

FORWARD-LOOKING STATEMENTS

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

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

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

- material adverse changes in economic conditions in Portugal or Brazil;
- exchange rate fluctuations in the Brazilian Real and the U.S. dollar;
- risks and uncertainties related to national and supranational regulation;
- increased competition resulting from the liberalization of the telecommunications sector in Portugal and Brazil;
- the success of our mobile operations in Brazil through our joint venture with Telefónica Móviles;
- the development and marketing of new products and services and market acceptance of such products and services; and
- the adverse determination of disputes under litigation.

PART I

ITEM 1 IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

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

ITEM 2 OFFER STATISTICS AND EXPECTED TIMETABLE

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

ITEM 3 KEY INFORMATION

Selected Consolidated Financial Data

The selected consolidated balance sheet data as of December 31, 2003 and 2004 and selected consolidated statement of income and cash flow data for each of the years ended December 31, 2002, 2003 and 2004 have been derived from our audited consolidated financial statements included herein. The selected consolidated balance sheet data as of December 31, 2000, 2001 and 2002 and selected consolidated statement of income and cash flow data for each of the years ended December 31, 2000 and 2001 have been derived from our audited consolidated financial statements not included herein.

We prepare our audited consolidated financial statements in accordance with Portuguese GAAP, which differs in certain significant respects from U.S. GAAP. See Notes 36, 37 and 38 to our audited consolidated financial statements for an explanation of the differences between Portuguese GAAP and U.S. GAAP. We have provided, in the information below, amounts in accordance with U.S. GAAP of operating revenues, operating income, net income, earnings per share, total assets, total liabilities and shareholders' equity for all periods and dates for which we have provided information.

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

During 1998, we acquired voting control of Telesp Celular Participações S.A., or TCP, the controlling shareholder of Telesp Celular S.A., or Telesp Celular, a mobile telecommunications operator in the Brazilian state of São Paulo. During 1999 and 2000, we increased our economic interest in TCP to 13.92% and Telesp Celular became the wholly-owned operating subsidiary of TCP. In June 2000, we conducted a tender offer in Brazil for ordinary shares in TCP. As a result of the tender offer, we increased our economic interest in TCP to 29.92%. On November 7, 2000, TCP completed a capital increase in which we subscribed for additional shares in TCP, and, upon acquisition of such shares, our economic interest in TCP increased to 36.20%. In November 2000, after we exchanged with Telefónica our minority interest in Telesp Fixa (the wireline operator in the Brazilian state of São Paulo controlled by Telefónica) for an additional interest in TCP, we increased our economic interest in TCP further to 41.23%, our voting interest to 85.06% and our ownership of TCP's preferred shares to 17.7%. TCP completed a rights offering in September 2002, in which we subscribed to a total of 247,224 million common shares and 326,831 million preferred shares, thereby increasing our economic interest in TCP to 65.12%, our voting interest to 93.7% and our ownership of TCP's preferred shares to 49.8%. In October 2002, in connection with our agreements with Telefónica Móviles, S.A., or Telefónica Móviles (Telefónica's mobile telecommunications subsidiary), for the formation of Brasilcel (the 50/50 joint venture with Telefónica Móviles for mobile operations in Brazil), which operates under the brand name Vivo as of April 2003 and is referred to as Vivo elsewhere in this Form 20-F, we sold a 14.68% stake in TCP to Telefónica Móviles. On December 27, 2002, we transferred the rest of our interest in TCP to Vivo. We now hold, jointly with Telefónica Móviles, an indirect interest in TCP, as well as in the other Brazilian mobile telecommunications companies previously held directly by Telefónica Móviles. See "*Item 4 Information on the Company Our Businesses Brazilian Mobile Business*" and "*Item 4 Information on the Company Strategic Alliances Alliance with Telefónica*".

Our financial statements for 2000 and 2001 fully consolidate the results of TCP in accordance with Portuguese GAAP. As a result of the transfer of our interest in TCP to Vivo on December 27, 2002 and our acquisition of a 50% ownership interest in Vivo as of that date, our consolidated balance sheet data as of December 31, 2002, 2003 and 2004 proportionally consolidates 50% of Vivo's assets and liabilities. Our consolidated statement of income and cash flow data for the year ended December 31, 2002 includes the full consolidation of TCP's income and cash flows. Our consolidated statement of income and cash flow data for the years ended December 31, 2003 and 2004 proportionally consolidates 50% of Vivo's income and cash flows.

In February 2001, TCP acquired an 83% indirect economic interest in Global Telecom (corresponding to 49% of the voting rights), a mobile telecommunications company operating in the Brazilian states of Paraná and Santa Catarina. On December 27, 2002, TCP purchased the remaining 51% of the voting shares of the three holding companies that own Global Telecom and as a result holds a 100% indirect economic interest in Global Telecom. Our consolidated results of operations for the year ended December 31, 2002 presented below reflect the results of operations of Global Telecom based on the equity method of accounting. Global Telecom's assets and liabilities as of December 31, 2002, 2003 and 2004 are reflected in our consolidated balance sheet through our proportional consolidation of Vivo. Global Telecom's income and cash flows for the years ended December 31, 2003 and 2004 are reflected in our consolidated statement of income and cash flows through our proportional consolidation of Vivo's income and cash flows.

On April 25, 2003, TCP acquired a controlling interest in Tele Centro Oeste Participações, S.A., or TCO, a mobile telecommunications operator in the Midwestern and Northern regions of Brazil. As a result, TCO's assets and liabilities as of December 31, 2003 and 2004 are reflected in our consolidated balance sheets as of those dates through our proportional consolidation of Vivo. TCO's income and cash flows from May through December 2003 and for the year ended December 31, 2004 are reflected in our consolidated statement of income and cash flows for the years ended December 31, 2003 and 2004, respectively, through our proportional consolidation of Vivo's income and cash flows.

Information provided in U.S. dollars for the year ended December 31, 2004 has been calculated on the basis of the Euro/U.S. dollar exchange rate on June 22, 2005 of €0.8244 = US$1.00. See "*Presentation of Financial Information*" and " *Exchange Rates*".

	Year Ended December 31,					
	2004	2004	2003	2002	2001	2000
	US$	EUR	EUR	EUR	EUR	EUR
STATEMENT OF PROFIT AND LOSS DATA:						
Amounts in accordance with Portuguese GAAP						
Operating revenues:						
Services rendered	6,399.9	5,276.1	5,056.5	4,950.9	4,976.3	4,329.8
Sales of merchandise and products	748.4	617.0	583.5	492.0	613.5	684.7
Telephone directory	157.4	129.8	136.1	139.1	136.8	131.7
Total operating revenues	7,305.7	6,022.9	5,776.1	5,582.0	5,726.6	5,146.2
Operating costs and expenses:						
Wages and salaries	905.1	746.2	705.9	694.8	668.6	578.1
Post retirement benefits	168.0	138.5	222.9	183.2	140.7	103.4
Costs of telecommunications	669.9	552.2	587.1	622.9	715.1	470.7
Depreciation and amortization	1,161.3	957.3	954.0	962.8	956.2	1,021.5
Subsidies	(18.3)	(15.1)	(20.6)	(31.5)	(36.8)	(38.1)
Maintenance and repairs	145.0	119.6	126.5	129.2	120.1	105.7
Own work capitalized	(108.6)	(89.5)	(74.5)	(114.0)	(179.3)	(133.9)
Raw materials and consumables	83.0	68.4	74.0	97.2	139.1	97.3
Costs of products sold	721.3	594.7	550.2	462.7	619.8	658.0
Telephone directories	105.4	86.9	90.4	92.0	89.2	87.1
Marketing and publicity	228.9	188.7	141.9	108.8	142.0	157.5
Concession rent				16.3	12.7	20.8
Other general and administrative	1,305.1	1,075.9	966.5	925.6	998.9	848.9
Provision for doubtful receivables, inventories & other	208.3	171.7	130.8	132.8	130.7	188.6
Other net operating income	(81.6)	(67.3)	(90.0)	(45.3)	(45.3)	(51.9)
Taxes other than income taxes	152.8	126.0	97.1	77.8	87.1	95.7
Total operating costs and expenses	5,645.6	4,654.3	4,462.4	4,315.3	4,558.8	4,209.4
Operating income	1,660.1	1,368.6	1,313.7	1,266.7	1,167.8	936.8
Other expenses, net	399.7	329.5	249.5	520.9	1,086.0	419.6
Work force reduction program costs	207.2	170.8	314.1	53.7	183.9	252.7
Extraordinary items	106.0	87.4	52.8	38.6	258.6	(492.2)
Income before income taxes	947.1	780.8	697.3	653.5	(360.7)	756.7
Provision for income taxes	(217.3)	(179.1)	(377.9)	(337.1)	(174.6)	(258.6)
Consolidated net income before minority interests	729.9	601.7	319.5	316.4	(535.3)	498.1
Loss (income) applicable to minority interests	(123.2)	(101.6)	(79.2)	74.6	342.7	42.3
Consolidated net income	606.7	500.1	240.2	391.1	(192.6)	540.3
Operating income per ordinary share, A share and ADS(1)	1.42	1.17	1.05	1.01	0.93	0.78
Earnings per ordinary share, A share and ADS(1)	0.52	0.43	0.19	0.31	(0.15)	0.45
Cash dividends per ordinary share, A share and ADS(1)(2)(3)	0.42	0.35	0.22	0.16	0.10	
Share capital	1,414.9	1,166.5	1,254.3	1,254.3	1,254.3	1,201.8

Amounts in accordance with U.S. GAAP						
Operating revenues	5,650.7	4,658.5	4,460.0	6,007.7	6,042.8	5,199.9
Operating income as restated(4)	1,019.0	840.7	723.1	383.2	696.1	395.8
Net income before change in accounting principles as restated(4)	618.5	509.9	145.5	1,315.3	208.1	66.8
Cumulative effect of a change in accounting principles SAB 101						(126.7)
Cumulative effect of a change in accounting principles SFAS 133					(57.5)	
Cumulative effect of a change in accounting principles SFAS 142				(1,038.9)		
Cumulative effect of a change in accounting principles SFAS 143			(7.4)			
Cumulative effect of a change in accounting principle subscriber acquisition costs	(29.3)	(24.2)				
Net income after change in accounting principles as restated(4)	589.2	485.7	138.2	276.4	150.6	(59.8)
Earnings per ordinary share, A share and ADS as restated(4)(5)	0.49	0.40	0.11	0.22	0.12	(0.05)
Diluted net income per share as restated(4)(6)	0.47	0.39	0.11	0.21	0.12	(0.05)

(1) Based on 1,201,750,000 ordinary and A shares issued in the year ended December 31, 2000, 1,254,285,000 ordinary and A shares issued in the years ended December 31, 2001, 2002 and 2003 and 1,166,485,050 ordinary and A shares issued in the year ended December 31, 2004.

(2) Dividends for the year ended December 31, 2000 were not paid.

(3) Cash dividends per ordinary share, A share and ADS for the years ended December 31, 2001, 2002, 2003 and 2004 in US$ were US$0.09, US$0.17, US$0.28 and US$0.42 respectively.

(4) Operating income and net income for the years ended December 31, 2000 and 2001 have been restated to include the effect of the reduction in the reported amortization expense for the translated carrying value of goodwill in Portugal Telecom's investment in TCP.

(5) Based on the weighted average number of shares as of the date given and taking into account the number of shares issued pursuant to capital increases and all treasury shares, there were 1,091,826,182 shares for the year ended December 31, 2000, 1,228,392,386 shares for the year ended December 31, 2001, 1,253,880,328 shares for the year ended December 31, 2002, 1,249,778,188 shares for the year ended December 31, 2003 and 1,210,976,939 shares for the year ended December 31, 2004.

(6) The weighted average number of shares is computed as a weighted average as of the date given and taking into account the number of shares from the exchangeable bonds issued on December 6, 2001, assuming conversion of the bonds into ordinary shares. For the years ended December 31, 2000, 2001, 2003 and 2004, the effects of the exchangeable bonds have been excluded from the calculation of diluted earnings per share since they would be antidilutive.

	December 31,					
	2004	**2004**	**2003**	**2002**	**2001**	**2000**
	US$	**EUR**	**EUR**	**EUR**	**EUR**	**EUR**
CASH FLOW DATA:						
Amounts in accordance with Portuguese GAAP						
Cash flows from operating activities	2,447.5	2,017.8	2,334.0	2,092.3	1,475.4	1,357.6
Cash flows from investing activities	757.5	(624.5)	(459.5)	(1,009.6)	(2,528.5)	(2,343.2)
Cash flows from financing activities	2,410.8	(1,987.5)	(1,654.1)	(486.1)	1,839.9	1,131.0

	December 31,					
	2004	**2004**	**2003**	**2002**	**2001**	**2000**
	US$	**EUR**	**EUR**	**EUR**	**EUR**	**EUR**
BALANCE SHEET DATA:						
Amounts in accordance with Portuguese GAAP						
Current assets	5,661.1	4,667.1	5,039.7	4,850.9	3,628.1	2,032.6
Investments, net	524.8	432.6	448.1	376.4	2,000.3	1,295.3
Fixed assets, net	4,928.2	4,062.9	4,268.0	4,575.8	5,491.3	5,446.2
Intangible assets post retirement benefits					761.9	495.0
Intangible assets other, net	3,897.2	3,212.9	3,150.1	2,968.7	4,934.4	3,878.8
Other non-current assets, net	713.3	588.0	652.0	954.3	820.3	68.3
Total assets	15,724.6	12,963.4	13,557.8	13,726.1	17,636.3	13,216.2
Current liabilities	4,589.0	3,783.1	3,354.5	2,958.0	3,240.0	3,154.2
Long-term debt	4,447.1	3,666.2	4,555.6	5,219.1	5,428.3	2,815.2
Accrued post retirement liability	1,540.4	1,269.9	1,256.0	1,061.5	1,810.0	1,488.0
Deferred income post retirement benefits					23.0	26.2
Other non-current liabilities	1,162.5	958.4	806.8	929.1	1,748.2	257.4
Total liabilities	11,738.9	9,677.6	9,973.0	10,167.6	12,249.5	7,741.0
Net assets	3,985.7	3,285.8	3,584.8	3,558.5	5,386.7	5,475.2
Minority interests	704.8	581.0	644.0	447.2	1,220.0	1,113.1
Total shareholders' equity	3,280.9	2,704.8	2,940.8	3,111.3	4,166.8	4,362.1
Number of ordinary shares	1,166.5	1,166.5	1,254.3	1,254.3	1,254.3	1,201.7
Share Capital(1)	1,414.9	1,166.5	1,254.3	1,254.3	1,254.3	1,201.7
Amounts in accordance with U.S. GAAP						
Total assets as restated(2)	14,391.9	11,864.7	11,764.3	12,554.2	16,747.8	14,534.6
Total liabilities as restated(2)	12,089.9	9,967.0	9,562.1	10,167.9	11,902.5	9,019.4
Total shareholders' equity as restated(2)	1,987.5	1,638.5	1,999.0	2,343.7	3,736.5	4,191.8

(1) As of the dates indicated, Portugal Telecom did not have any redeemable preferred stock.

(2) Assets, liabilities and shareholders' equity as of December 31, 2001 and 2000 have been restated to include the effect of translation of goodwill in TCP and the minimum pension liability adjustment.

Exchange Rates

Euro

Effective January 1, 1999, Portugal joined ten other member countries of the European Union in adopting the Euro as the common currency. During the transition period between January 1, 1999 and December 31, 2001, the Escudo remained legal tender in Portugal as a denomination of the Euro, and public and private parties paid for goods and services in Portugal using either the Euro or the Escudo. On January 1, 2002, the Euro entered into cash circulation, and from January 1, 2002 through February 28, 2002, both the Euro and the Escudo were in circulation in Portugal. From March 1, 2002, the Euro became the sole circulating currency in Portugal.

For the years ended December 31, 2002, 2003 and 2004 the majority of our revenues, assets and expenses were denominated in Euro, although a significant portion of our assets and liabilities are denominated in Brazilian Reais. We have published our audited consolidated financial statements in Euro and our shares trade in Euro on the Euronext Lisbon Stock Exchange. Our financial results could be affected by exchange rate fluctuations in the Brazilian Real. See "*Item 5 Operating and Financial Review and Prospects Exchange Rate Exposure to the Brazilian Real*".

Our future dividends, when paid in cash, will be denominated in Euros. As a result, exchange rate fluctuations have affected and will affect the U.S. dollar amounts received by holders of ADSs on conversion of such dividends by The Bank of New York as the ADS depositary. The Bank of New York converts dividends it receives in foreign currency into U.S. dollars upon receipt, by sale or such other manner as it has determined, and distributes such U.S. dollars to holders of ADSs, net of The Bank of New York's expenses of conversion, any applicable taxes and other governmental charges. Exchange rate fluctuations may also affect the U.S. dollar price of the ADSs on the New York Stock Exchange.

The following tables show, for the period and dates indicated, certain information regarding the U.S. dollar/Euro exchange rate. The information is based on the noon buying rate in the City of New York for cable transfers in Euro as certified for United States customs purposes by the Federal Reserve Bank of New York. On June 22, 2005, the Euro/U.S. dollar exchange rate was €0.8244 per US$1.00.

Year ended December 31,	Average Rate(1)
	(EUR per US$1.00)
2000	1.0873
2001	1.1217
2002	1.0561
2003	0.8786
2004	0.8022

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

Period	High	Low
	(EUR per US$1.00)	
December 31, 2004	0.7400	0.7317
January 31, 2005	0.7707	0.7658
February 28, 2005	0.7557	0.7530
March 31, 2005	0.7745	0.7681
April 30, 2005	0.7763	0.7704
May 31, 2005	0.8123	0.8008

None of the 25 member countries of the European Union has imposed any exchange controls on the Euro.

Brazilian Real

Although the majority of our revenues, assets and expenses are denominated in Euros, most of the revenues, assets and expenses from our Brazilian investments are denominated in Brazilian Reais. Consequently, exchange rate fluctuations between the Euro and the Brazilian Real affect our revenues.

There are two principal legal foreign exchange markets in Brazil: the commercial rate exchange market and the floating rate exchange market. Most trade and financial foreign-exchange transactions are carried out on the commercial rate exchange market. These transactions include the purchase or sale of shares or payment of dividends or interest with respect to shares. Foreign currencies may only be purchased through a Brazilian bank authorized to operate in these markets. In both markets, rates are freely negotiated but may be influenced by Central Bank intervention. In 1999, the Central Bank placed the commercial rate exchange market and the floating rate exchange market under identical operational limits, which led to a convergence in the pricing and liquidity of both markets. Since February 1, 1999, the floating market rate has been the same as the commercial market rate, and the system relying on the foreign exchange rate band has been eliminated. However, there is no guarantee that these rates will continue to be the same in the future. Despite the convergence in pricing and liquidity of both markets, each market continues to be regulated separately.

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

The following tables show, for the periods and date indicated, certain information regarding the Real/U.S. dollar exchange rate. On June 22, 2005, the Real/U.S. dollar exchange rate was R$2.3760 per US$1.00. The information is based on the noon buying rate in the City of New York for cable transfers in Brazilian Reais as certified for United States customs purposes by the Federal Reserve Bank of New York.

Year ended December 31,	**Average Rate(1)**
	(R$ per US$1.00)
2000	1.8333
2001	2.3507
2002	2.9886
2003	3.0565
2004	2.9175

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

Period	**High**	**Low**
	(R$ per US$1.00)	
December 31, 2004	2.6563	2.6520
January 31, 2005	2.6495	2.6085
February 28, 2005	2.6185	2.5831
March 31, 2005	2.6883	2.6520
April 30, 2005	2.5538	2.5235
May 31, 2005	2.4230	2.3650

Escudo

As of January 1, 2002, we ceased to use the Escudo. For the years ended December 31, 2001, 2002, 2003 and 2004 the majority of our revenues, assets and expenses were denominated in Euros. As

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a result, revenues, assets and expenses for years prior to 2001 have been translated from Escudos into Euros. All figures previously stated in Escudos have been converted to figures in Euro based on the fixed Escudo/Euro exchange rate, established on January 1, 1999, of PTE 200.482 per €1.00 or approximately €0.005 per PTE 1.00. See " *Euro*".

Risk Factors

The Portuguese Government Holds All of Our A Shares Which Afford It Special Approval Rights

All of our A shares are held by the Portuguese government. Under our articles of association, as the holder of all of our A shares, the Portuguese government may veto a number of actions of our shareholders, including the following:

- election of one-third of the directors, including the chairman of the board of directors;
- authorization of a dividend in excess of 40% of our distributable net income in any year;
- capital increases and other amendments to our articles of association;
- issuance of bonds and other securities;
- authorization for a shareholder that is engaged in an activity in competition with us to hold more than 10% of our ordinary shares;
- altering our general objectives, strategy or policies; and
- defining our investment policies, including the authorization of acquisitions and disposals.

An ADS Holder May Face Disadvantages Compared to an Ordinary Shareholder When Attempting to Exercise Voting Rights

Holders of our ADSs may instruct the depositary to vote the ordinary shares underlying the ADSs. For the depositary to follow the voting instructions, it must receive them on or before the date specified in our voting materials. The depositary must try, as far as practical, subject to Portuguese law and our articles of association, to vote the ordinary shares as instructed. In most cases, if the ADS holder does not give instructions to the depositary, it may vote the ordinary shares in favor of proposals supported by Portugal Telecom's board of directors, or, when practicable and permitted, give a discretionary proxy to a person designated by us. We cannot be certain that ADS holders will receive voting materials in time to ensure that they can instruct the depositary to vote the underlying ordinary shares. Also, the depositary is not responsible for failing to carry out voting instructions or for the manner of carrying out voting instructions. This means that ADS holders may not be able to exercise their right to vote and there may