

TELECOM ITALIA S P A
Form 20-F
May 27, 2005
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20-F

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

OR

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

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

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

Commission file number: 1-13882

Telecom Italia S.p.A.

(Exact name of Registrant as specified in its charter)

Italy

(Jurisdiction of incorporation or organization)

Piazza degli Affari 2, 20123 Milan, Italy

(Address of principal executive offices)

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

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

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

None

(Title of Class)

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

None

(Title of Class)

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

Not applicable

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No Not Applicable

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

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

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Introduction

INTRODUCTION

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

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

Beginning with the first quarter ended March 31, 2005, we will report our financial information and prepare our financial information and our financial statements in accordance with International Financial Reporting Standards (IFRS). See Item 3. Key Information 3.1 Risk Factors In 2005 we are obliged to adopt IFRS which will impact our financial results and results of operations as they differ in significant respects from Italian GAAP, and Item 5. Operating and Financial Review and Prospects 5.4 Critical Accounting Policies and 5.5 Adoption of International Accounting Standards .

Cautionary Statement for Purposes of the Safe Harbor Provisions of the United States Private Securities Litigation Reform Act of 1995. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. This Annual Report contains certain forward-looking statements, including, but not limited to, the discussion of the changing dynamics of the marketplace, including the continuing developments in competition in all aspects of our businesses from new competitors and from new and enhanced technologies, our outlook for growth in the telecommunications industry both within and outside of Italy, including our targets for the period 2005-2007 and our outlook regarding developments in the telecommunications industry, including certain trends we have identified particularly in our core Italian market, continuing regulatory measures regarding pricing and access for other local operators. Such statements include, but are not limited to, statements under the following headings: (i) Item 3. Key Information 3.1 Risk Factors, (ii) Item 4. Information on the Telecom Italia Group 4.1 Business 4.1.3 Significant Developments During 2004 and 4.1.8 Updated Targets and Strategy, (iii) Item 4. Information on the Telecom Italia Group 4.3 Regulation, (iv) Item 5. Operating and Financial Review and Prospects, (v) Item 8. Financial Information 8.3 Legal Proceedings and (vi) Item 11. Quantitative and Qualitative Disclosures About Market Risks, including statements regarding the likely effect of matters discussed therein. Actual results may differ materially from those projected or implied in the forward-looking statements. Such forward-looking information involves risks and uncertainties, which are outside our control, that could significantly affect expected results and are based on certain key assumptions.

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

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

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- the success of our customer loyalty and retention programs, particularly in the fixed line business, and the impact of such programs on our revenues;
- the impact of regulatory decisions and changes in the regulatory environment, including implementation of recently-adopted EU directives in Italy;
- the impact and consequences of the Merger and the TIM Acquisition (each as defined below);
- the impact of the economic recovery in Latin American and economic development generally on our international business and on our foreign investments and capital expenditures;
- the continuing impact of rapid or disruptive changes in technologies;
- the impact of political and economic developments in Italy and other countries in which we operate;
- the impact of fluctuations in currency exchange and interest rates;
- our ability to successfully implement our strategy over the 2005-2007 period;
- our ability to successfully achieve our debt reduction targets;
- our ability to successfully roll out our UMTS network and services and to realize the benefits of investment in our UMTS license and related capital expenditures;
- our ability to successfully implement our Internet and broadband strategy both in Italy and abroad;
- our ability to achieve the expected return on the significant investments and capital expenditures we have made and continue to make in Latin America;
- the amount and timing of any future impairment charges for our licenses, goodwill or other assets; and
- the impact of litigation or decreased mobile communications usage arising from actual or perceived health risks or other problems relating to mobile handsets or transmission masts.

The foregoing factors should not be construed as exhaustive. Due to such uncertainties and risks, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. We undertake no obligation to

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release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events. See Item 3. Key Information 3.1 Risk Factors and the related cautionary statement under Item 5. Operating and Financial Review and Prospects .

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Key Definitions

KEY DEFINITIONS

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

Telecom Italia	means the entity which resulted from the Merger.
Telecom Italia Group	means the Company and its consolidated subsidiaries.
Old Telecom Italia and Old Telecom Italia Group	means Telecom Italia and its consolidated subsidiaries as they existed immediately prior to the effective date of the Merger.
Olivetti	means Olivetti S.p.A., the holding company and controlling shareholder of Old Telecom Italia.
Olivetti Group	means Olivetti and its consolidated subsidiaries, including Old Telecom Italia.
Merger	means the merger of Old Telecom Italia into Olivetti, approved by the shareholders of Old Telecom Italia and Olivetti on May 24, 2003 and on May 26, 2003, respectively, which became effective on August 4, 2003.
Shares	means the ordinary shares, 0.55 par value each, of Telecom Italia.
Savings Shares	means the savings shares, 0.55 par value each, of Telecom Italia.
TIM	means Telecom Italia Mobile S.p.A. and following the spin-off of the domestic mobile assets which is part of the TIM Acquisition, TIM Italia S.p.A., the Telecom Italia Group's subsidiary operating in the mobile telecommunications business.
TIM Acquisition	means the acquisition by Telecom Italia of the ordinary shares and savings shares of TIM it does not already own through a cash tender offer completed on January 21, 2005 to be followed by a merger of TIM S.p.A. with and into Telecom Italia, expected to be completed by the end of June, 2005.
Telecom Italia Media	means the corporate name of the remaining part of Seat Pagine Gialle S.p.A. which resulted from the proportional spin-off of the directories and most of the directory assistance and business information business segments of SEAT into New SEAT. The spin-off became effective on August 1, 2003 and new SEAT was disposed of on August 8, 2003. Telecom Italia Media is the Telecom Italia Group's subsidiary operating the Internet & Media business.
EU	means the European Union.

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Item 2. Offer Statistics and Expected Timetable

Risk Factors

Item 3. Key Information

PART I

Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not Applicable

Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not Applicable

Item 3. KEY INFORMATION

3.1 RISK FACTORS

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

Strong domestic competition exists in all of the principal telecommunications business areas in Italy in which we operate, including, most significantly, our fixed-line and mobile voice telecommunications businesses. This competition may increase further due to the consolidation and globalization of the telecommunications industry in Europe and elsewhere. Consolidation is increasing rapidly and competition is expected to rise at all levels in the future. In addition, the use of the single European currency and the liberalization of the Italian telecommunication market has further intensified competition by facilitating international operators' entry into the Italian market and direct competition with our fixed line and mobile telephony businesses, particularly in the local and long-distance markets. As of December 31, 2004, there were a number of significant competitors offering fixed-line services and three other operators (besides TIM) offering mobile services in the Italian domestic market; the third mobile competitor (H3G) entered the market in 2003, offering third generation commercial services. Although we stopped the decline in our market share of voice traffic in our fixed line business during 2003 and maintained our market share in 2004, continuing pressures on prices due to competition and further erosion in market shares could adversely affect our results of operations. Continuing changes to the regulatory regime, including carrier preselection, number portability and local loop unbundling as well as the implementation of new EU telecommunications directives and the continuing entry of strong international operators in our markets are increasing competition for the services we provide, particularly in our fixed line business, which could also adversely affect our business.

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

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

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Item 3. Key Information

Risk Factors

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

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

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

The most significant objectives of the Industrial Plan were achieved, particularly the sale of non-core assets and debt reduction. We also took steps to strengthen our competitive position in our core Italian domestic market through the introduction of new products and tariff packages and our focus on lowering costs through the reduction of operating expenses and capital expenditures.

In order to satisfy a series of business needs, prompted by the progressive convergence between fixed and mobile platforms, Telecom Italia decided to make the TIM Acquisition. The strategic and industrial objectives of the TIM Acquisition are to:

- simplify the chain of ownership of the group;
- unify management of the fixed and mobile businesses to improve business opportunities;
- realize significant synergies from the integrated management of fixed and mobile telecommunications in Italy and abroad; and
- optimize financial and cash flows within the Telecom Italia Group by managing our debt more efficiently, making better use of financial leverage and reducing our weighted average cost of capital.

In connection with the Merger and the TIM Acquisition, we confirmed the objectives and guidelines of the Industrial Plan and established certain targets for the 2005-2007 period, which include strict capital expenditures and cost controls and instituting other actions to ensure the reduction of the debt level we have as a result of the Merger and the TIM Acquisition. See Item 3. Key Information 3.1 Risk Factors As a result of the Merger and the TIM Acquisition we remain highly leveraged .

Factors beyond our control that could affect the implementation and achievement of the strategic objectives of the TIM Acquisition and reaching our targets for the period 2005-2007 include:

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

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

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

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

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

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

As a member of the EU, Italy is required to adapt its telecommunications regulatory framework to the legislative and regulatory framework established by the EU for the regulation of the European telecommunications market. The EU Commission approved a new electronic communications framework in March 2002 which has been effective in Italy since September 2003. Included within this new framework is the obligation on the part of the National Regulatory Authority to identify operators with significant market power based on a market analysis in eighteen separate retail and wholesale markets, in which it is considered necessary to intervene to protect free competition. The National Regulatory Authority is currently conducting its analysis. The new framework establishes criteria and procedures for identifying remedies applicable to operators with significant market power. The conclusion of this analysis and the implementation of these revised telecommunications regulations and possible future decisions relating thereto, which is expected to be completed before the second half of 2005, may change the regulatory environment in a manner adverse to us, particularly as they relate to new services which may not currently be part of the eighteen identified markets. Please see Item 4. Information on the Telecom Italia Group 4.3 Regulation in this report for more information on the regulatory requirements to which we are subject.

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

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

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

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

As a result of this change in strategy, in the 2002-2003 period we divested certain of our most significant European assets such as BDT (Bouygues Decaux Telecom), Autel (Mobilkom Austria), Telekom Austria,

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9Telecom group and Auna. Consistent with our strategy to focus our Latin American operations principally in Brazil, we recently disposed of Entel Chile (Chile) and intend to sell our interest in Corporacion Digitel (Venezuela) and we will continue to seek to divest certain international non-strategic assets. In April 2005, we entered into an agreement to sell our stake in TIM Hellas, our Greek mobile telecommunications operator. In addition, certain investments which were made during the 1999-2001 period declined significantly in value resulting in write-downs and asset impairments which materially adversely affected our results of operations in 2002, and to a lesser degree in 2003 and 2004. We will continue to target our international investments in Latin America, particularly mobile telecommunications in Brazil, European broadband and mobile telecommunications in selected markets. These investments will continue to require significant capital expenditures and there can be no assurance that we will be able to achieve a satisfactory return on our investments or that we will not suffer further losses and write-downs in markets where we have decided to focus our investments.

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

The telecommunications industry is in a period of rapid technological change. Many of the services we offer are technology-intensive and the development of new technologies may render such services non-competitive or reduce prices for such services. We make and will have to make substantial additional investments in new technologies to remain competitive. The new technologies we choose may not prove to be commercially successful. In addition, we may not receive the necessary licenses to provide services based on new technologies in Italy or abroad. Furthermore, our most significant competitors in the future may be new entrants to our markets who do not have the obligations to maintain an installed base of older equipment. As a result, we could lose customers, fail to attract new customers or incur substantial costs in order to maintain our customer base.

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

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

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

Because we have made substantial international investments, primarily in U.S. dollars, and have significantly expanded our operations outside the euro zone, particularly in Latin America, movements in the exchange rates of the euro against other

currencies can adversely affect our revenues and operating results. A rise in the value of the euro relative to other currencies in certain countries in which we operate or have made investments will reduce the relative value of the revenues or assets of our operations in those countries and, therefore, may adversely affect our operating results or financial position. In addition, we have raised, and may raise in an increasing proportion in the future, financing in currencies other than the euro, principally the U.S. dollar. Accordingly, the value of those liabilities will be affected by fluctuations of the currencies of the countries in which we operate against the currency in which the financing is denominated. We generally enter into a number of forward currency transactions, swaps and options to manage foreign currency risk exposure with respect to our non-euro denominated liabilities. However, we can give no assurances that we will be successful in managing foreign currency risk exposure, taking into consideration that appropriate foreign currency swaps and options may not be available as needed on the relevant financial markets. In recent years reported results of our Latin American operations have been adversely affected by changes in local currencies against the euro. In particular, in 2004 the strengthening of the euro against the local currencies in Latin America adversely affected the revenues of the Mobile Business Unit by 150 million.

Our total gross financial debt at year end 2004 was 38,844 million (41,465 million at year end 2003). On January 28, 2005, in connection with the Cash Tender Offer for TIM ordinary and savings shares as part of the

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TIM Acquisition, we borrowed an additional 11.3 billion under a 12 billion Term Loan Facility, granted by a pool of Italian and international banks (0.7 billion of the Tranche A was partially cancelled at the time of drawdown). On February 11, 2005, the remaining 2.3 billion of Tranche A was repaid in advance and cancelled, leaving 9 billion outstanding under the Term Loan Facility. Interest on this debt is calculated by applying an average spread over Euribor of 0.55 basis points. As a result, our total interest payable will increase in 2005 compared to 2004 and our exposure of total debt subject to floating interest rates has increased as well.

We enter into derivative transactions to hedge our interest exposure and to diversify debt parameters in order to reduce debt cost and volatility within predefined target boundaries. However, we can give no assurance that fluctuations in interest rates will not adversely affect our results of operations.

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

Through TIM, we have acquired a third generation mobile telephone, or UMTS, license to commence operations of UMTS services in Italy. TIM committed to pay 2,417 million for its license, with 2,066 million paid in December 2000 and three installments of 117 million paid in November 2001, November 2002 and December 2003. The size of the market for UMTS products and services is unknown and may fall short of the industry's expectations. We cannot be certain that the demand for such services will justify the related costs. We have made investments, although required under our license, which may not be commercially desirable. In addition, there are a number of significant competitors in Italy offering these services including one competitor only offering third generation services, which competitor entered the market prior to our third generation services being available.

We have made significant investments, in accordance with the terms and conditions of our license, to create the infrastructure to offer UMTS services. TIM commenced offering UMTS services in Italy in the second half of 2004 and it is not yet possible to assess the response of the market. Given the substantial costs of upgrading our existing networks to support UMTS and the uncertainty regarding the commercial adoption of UMTS, we may not be able to recoup our investment according to our estimates, if at all.

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

In recent years, our consolidated revenues have grown or remained stable in large part because of the rapid growth in the mobile communications business which has offset flat or declining revenues in our Italian fixed line business. This growth has been driven largely by the rapid expansion of the mobile telecommunications market in Italy. However, as a result of this growth, the Italian market is approaching saturation levels, with penetration rates now around 109% (due to many subscribers having more than one line). TIM's domestic market share declined in 2004 from approximately 46% in the past two years to 42% at the end of 2004. As a result, revenue growth is no longer driven by the rapid subscriber growth which TIM experienced in the 1998-2001 period. Offsetting this decline has been growth in international markets, particularly Brazil, but these markets on the whole are not yet profitable.

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

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

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

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

In recent years the market for telecom stocks and credit ratings of market participants, as well as our ongoing review and refinement of our business plan, resulted in substantial impairment write-downs of our assets (in particular goodwill) which materially adversely affected our results of operations in 2001 and 2002. Although the negative impact of write-downs in 2003 and 2004 was much lower than 2001 and 2002, there can be no assurance that similar events in the future may not result in further substantial impairment write-downs from assets.

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

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

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

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

Any of the above factors may adversely affect the successful implementation of our strategy, our business and results of operations.

As a result of the Merger and the TIM Acquisition we remain highly leveraged.

Under Italian GAAP, our gross financial debt was 38,844 million at December 31, 2004 compared with 41,465 million at December 31, 2003, and our total net financial debt was 29,525 million as of December 31, 2004 compared with 33,346 million at December 31, 2003. See Item 3. Key Information 3.3 Selected Financial and Statistical Information Note 9 which reconciles our net financial debt to our gross financial debt.

At December 31, 2004, our gross and net financial debt did not include debt incurred for the TIM Acquisition. As a result of the total outlay borne by Telecom Italia for the purchase of TIM shares tendered and accepted in the Public Tender Offer, we have incurred additional debt of 9 billion and, after taking into account certain cash payments (2.5 billion for the Public Tender offers and 2.3 billion used to repay a portion of the Term Loan Facility), net financial debt would have increased by 13.8 billion. As a result of the tender offer and related transactions, our pro forma gross financial debt and pro forma net financial debt at December 31, 2004 would have been 47.8 billion and 43.3 billion, respectively. Under IFRS net financial debt would increase a further 3.3 billion. We are targeting reducing our net financial debt through:

- significant cash flow generation by our core businesses, and
- net proceeds from disposals used to reduce outstanding debt.

There can be no assurance that factors beyond our control, including but not limited to deterioration in general economic conditions, will not significantly affect our ability to generate cash to reduce debt or to refinance existing debt through further borrowing.

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

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

Table of Contents**Item 3. Key Information****Risk Factors*****Actual or perceived health risks or other problems relating to mobile handsets or transmission masts could lead to litigation or decreased mobile communications usage.***

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

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

In 2005 we are obliged to adopt IFRS which will impact our financial results and results of operations as they differ in significant respects from Italian GAAP.

Until 2004, we prepared our consolidated financial statements in accordance with Italian GAAP. In June 2002, the Council of Ministers and the Parliament of the EU adopted new regulations requiring all listed EU companies, including us, to apply IFRS (previously known as International Accounting Standards or IAS) in preparing their consolidated financial statements from January 1, 2005. Because our consolidated financial statements prepared in accordance with IFRS will differ from our consolidated financial statements prepared in accordance with Italian GAAP, the methods used by the financial community to assess our financial performance and value our publicly-traded securities could be affected.

Please see Item 5. Operating and Financial Review and Prospects 5.5 Adoption of International Accounting Standards for a more complete description of the impact of IFRS reporting on our consolidated financial statements.

Risks associated with Telecom Italia's ownership chain.

Although, as a result of the Merger, no shareholder controlled Telecom Italia, because of the *voto di lista* system for the election of directors, currently 15 out of 21 of our directors (of whom, however, 11 are considered independent) were elected from a slate of candidates proposed by Olimpia, which is currently the largest shareholder in Telecom Italia. As a result of a series of transactions entered into by Olimpia, as of the date hereof, Olimpia holds 21.4% of the Telecom Italia shares. Upon completion of the merger in connection with the TIM Acquisition, and based on the exchange ratio established for the merger of TIM into Telecom Italia, it is estimated that Olimpia's stake in Telecom Italia will be diluted back to approximately 18% on completion of the merger of TIM into Telecom Italia. See Item 7. Major Shareholders and Related-Party Transactions 7.1 Major Shareholders 7.1.1 The Olimpia Shareholders Agreements.

In addition, Marco Tronchetti Provera and Carlo Orazio Buora, respectively Executive Chairman and Managing Director of Telecom Italia, are also, respectively, Chairman and Managing Director of Pirelli & C. S.p.A., which currently owns a 57.66% stake in Olimpia. Mr. Tronchetti Provera is Chairman of Olimpia and Mr. Buora is a member of Olimpia's board of directors. See Item 6. Directors, Senior Management and Employees 6.1 Directors 6.1.1 Biographical Data .

Although Olimpia does not and will not own a controlling interest in Telecom Italia voting shares, Olimpia retains significant power as a result of its proposal of a majority of the present Telecom Italia Board members who were elected in May 2004. As a result, Olimpia may be able to influence certain corporate actions and may exert a significant influence on all matters to be decided by a vote of shareholders. In principle, the interests of Olimpia in deciding these matters could be different from the interests of Telecom Italia's other ordinary shareholders and it is possible that certain decisions could be taken that may be influenced by the needs of Olimpia.

Olimpia is in effect a holding company and the sole full operating company in which it holds shares is Telecom Italia. Therefore, if Olimpia were unable to obtain additional funding from new or existing shareholders or from other sources, Olimpia would be entirely dependent on dividends paid on its Telecom Italia shares for its funding needs, including to reimburse its existing debt. Under such circumstances, among the Telecom Italia corporate decisions that could be influenced by the needs of Olimpia would be the level of dividends payable by Telecom Italia to its shareholders.

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Risk Factors

Telecom Italia's financial position is not directly related to Olimpia and as such Telecom Italia does not have any obligations with respect to such debt since they are separate legal entities. Notwithstanding the foregoing, since certain rating agencies view Olimpia's and Telecom Italia's financial position together, such a view could affect our debt ratings, which may adversely affect Telecom Italia's financial flexibility and its cost of capital.

Although no shareholder controls Telecom Italia and thus is in a position to prevent a takeover of Telecom Italia, the Italian State, through the Treasury, is in a position to exert certain powers with respect to Telecom Italia through the exercise of the special powers included in Telecom Italia's Bylaws pursuant to compulsory legal provisions: specifically, the so-called Golden Share still provides for the Italian State's authority to approve or disapprove of the acquisition of material interests in our share capital (which is defined as 3% of the voting share capital). Currently, the exercise of special powers by the Italian State with respect to privatized companies (including Telecom Italia) is governed by ad hoc rules and the special powers themselves are undergoing further changes, but it is possible that the Italian State's Golden Share could make a merger with or takeover of Telecom Italia more difficult or discourage certain bidders from making an offer. See Item 7. Major Shareholders and Related-Party Transactions 7.1 Major Shareholders 7.1.3 Continuing Relationship with the Italian Treasury .

Table of Contents**Item 3. Key Information****Exchange Rates****3.2 EXCHANGE RATES**

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

For convenience only (except where noted otherwise), certain euro figures have been translated into dollars at the rate (the **Euro/Dollar Exchange Rate**) of 1.00= U.S.\$ 1.3538, using the noon buying rate in The City of New York for cable transfers in foreign currencies as announced by the Federal Reserve Bank of New York for customs purposes (the **Noon Buying Rate**) on December 31, 2004.

These translations should not be construed as a representation that the euro amounts actually represent such dollar amounts or have been or could be converted into dollars at the rate indicated.

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

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

The following table sets forth for the years 2000 to 2004 and for the beginning of 2005 certain information regarding the Noon Buying Rate for Dollars expressed in U.S.\$ per 1.00.

Calendar Period	High	Low	Average(1)	At Period End
2000	1.0335	0.8270	0.9207	0.9388
2001	0.9535	0.8425	0.8909	0.8901
2002	1.0485	0.8594	0.9495	1.0485
2003	1.2597	1.0361	1.1411	1.2597
2004	1.3625	1.1801	1.2438	1.3538
2005 (through May 23, 2005)	1.3476	1.2630	1.3039	1.2630
Monthly Amounts				
December 2004	1.3625	1.1801	1.2438	1.3538
January 2005	1.3476	1.2954	1.3123	1.3049

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February 2005	1.3274	1.2773	1.3013	1.3274
March 2005	1.3465	1.2877	1.3185	1.2969
April 2005	1.3093	1.2819	1.2943	1.2919
May 2005 (through May 23, 2005)	1.2936	1.2553	1.2751	1.2575

(1) Average of the rates for the last business day of each month in the relevant period except for May 2005 for which the date used is May 23, 2005.

The shares and savings shares of Old Telecom Italia and the shares of Olivetti have traded on *Mercato Telematico Azionario* (Telematico), managed by Borsa Italiana S.p.A. (Borsa Italiana) in euro since January 4, 1999. Fluctuations in the exchange rate between the euro and the U.S. dollar will affect the U.S. dollar equivalent of the euro price of the Shares and the Savings Shares and the price of the American Depositary Shares (ADSs) and the Savings Share American Depositary Shares (Savings Share ADSs), on the New York Stock Exchange (NYSE). Cash dividends were paid by Old Telecom Italia and Olivetti in lire until 2001 (Olivetti paid no dividend in 2001) and in euro starting from 2002 (Olivetti paid no dividend in 2002). Exchange rate fluctuations will affect the U.S. dollar amounts received by owners of ADSs and Savings Share ADSs upon conversion by the Depositary of cash dividends paid in euro on the underlying Shares and Savings Shares. See Item 10. Additional Information 10.5 Description of American Depositary Receipts .

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

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Item 3. Key Information

Selected Financial And Statistical Information

3.3 SELECTED FINANCIAL AND STATISTICAL INFORMATION

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

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

- the Telecom Italia Group's selected financial data as of and for each of the years ended December 31, 2003 and 2004 have been extracted or derived from the consolidated financial statements of the Telecom Italia Group prepared in accordance with Italian GAAP and which have been audited by Reconta Ernst & Young S.p.A. independent auditor; and
- the Telecom Italia Group's selected financial data as of and for each of the years ended December 31, 2002, 2001 and 2000 have been extracted or derived (other than the 2000 pro forma data) from the Olivetti Group's consolidated financial statements prepared in accordance with Italian GAAP and which have been audited by the following independent auditors: Reconta Ernst & Young S.p.A. (for the years ended December 31, 2002 and 2001) and PricewaterhouseCoopers S.p.A. (for the year ended December 31, 2000).

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

Table of Contents**Item 3. Key Information****Selected Financial And Statistical Information**

	Year ended December 31,						
	2000		2001(1)	2002(1)	2003(1)	2004(1)	2004
2000(1)	pro forma (Unaudited) (1)(2)						
	(millions of Euro, except per share amounts)						(millions of U.S. dollars, except per share amounts)(3)
Statement of Operations Data in accordance with Italian GAAP:							
Operating revenues	30,116	28,374	32,016	31,408	30,850	31,237	42,289
Other income	483	459	476	504	345	315	426
Total revenues	30,599	28,833	32,492	31,912	31,195	31,552	42,715
Cost of materials	3,058	2,931	2,640	2,315	2,081	2,414	3,268
Salaries and social security contributions	5,245	4,965	4,919	4,737	4,303	4,045	5,476
Depreciation and amortization(4)	6,946	6,509	7,612	7,227	6,779	6,646	8,997
Other external charges	11,136	10,476	12,687	12,188	11,934	12,014	16,265
Changes in inventories	(318)	(296)	92	62	114	(25)	(34)
Capitalized internal construction costs	(912)	(831)	(583)	(675)	(805)	(742)	(1,005)
Total operating expenses(4)	25,155	23,754	27,367	25,854	24,406	24,352	32,967
Operating income(4)	5,444	5,079	5,125	6,058	6,789	7,200	9,748
Financial income	1,202	1,162	1,446	1,569	992	1,381	1,870
Financial expense(4)	(3,857)	(3,648)	(6,559)	(4,647)	(3,256)	(3,215)	(4,353)
<i>Of which write-downs and equity in affiliated and other companies, net</i>	<i>(1,037)</i>	<i>(1,025)</i>	<i>(1,771)</i>	<i>(487)</i>	<i>(91)</i>	<i>(30)</i>	<i>(42)</i>
Other income and (expense), net	135	165	(3,109)	(5,496)	(1,083)	(410)	(555)
Income (loss) before income taxes and minority interests	2,924	2,758	(3,097)	(2,516)	3,442	4,956	6,710
Income taxes	(1,923)	(1,813)	(579)	2,210	(1,014)	(3,054)	(4,135)
Net income (loss) before minority interests	1,001	945	(3,676)	(306)	2,428	1,902	2,575
Minority interests	(1,941)	(1,885)	586	(467)	(1,236)	(1,121)	(1,518)
Net income (loss)	(940)	(940)	(3,090)	(773)	1,192	781	1,057
Net income (loss) per Share(5)	(0.20)	(0.20)	(0.36)	(0.09)	0.07	0.04	0.054
Dividends per Share	0.0350	0.0350			0.1041	0.1093(6)	0.1480
Dividends per Savings Share					0.1151	0.1203(6)	0.1629

Amounts in accordance with U.S. GAAP:

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Total revenues	29,201	29,191	29,467	30,593	41,417
Operating income	3,538	7,181	8,034	7,006	9,485
Net income (loss) before minority interests, discontinued operations and cumulative effect of accounting changes	(2,994)	6,341	3,190	2,801	3,792
Minority interests	18	(3,016)	(1,523)	(1,205)	(1,631)
Net income (loss) from discontinued operations	(1,050)	(1,369)	195	(55)	(74)
Cumulative effect of accounting changes, net of tax	20		(21)		
Net income (loss)	(4,006)	1,956	1,841	1,541	2,086
Net income (loss) per Share before discontinued operations and cumulative effect of accounting changes Basic	(0.87)	0.82	0.18	0.10	0.14
Net income (loss) per Share before discontinued operations and cumulative effect of accounting changes Diluted	(0.87)	0.82	0.18	0.10	0.14
Net income (loss) per Share from discontinued operations Basic	(0.31)	(0.34)	0.02	(0.01)	(0.01)
Net income (loss) per Share from discontinued operations Diluted	(0.31)	(0.34)	0.02	(0.01)	(0.01)
Net income (loss) per Share from cumulative effect of accounting changes Basic	0.01	0.00	(0.01)	(0.00)	(0.00)
Net income (loss) per Share from cumulative effect of accounting changes Diluted	0.01	0.00	(0.01)	(0.00)	(0.00)
Net income (loss) per Share Basic(7)	(1.17)	0.48	0.20	0.09	0.12
Net income (loss) per Share Diluted(7)	(1.17)	0.48	0.20	0.09	0.12

Table of Contents**Item 3. Key Information****Selected Financial And Statistical Information**

	As of December 31,						
	2000						
	2000(1)	pro forma (Unaudited) (1)(2)	2001(1)	2002(1)	2003(1)	2004(1)	2004
	(millions of Euro)						(millions of U.S. dollars)(3)
Balance Sheet Data in accordance with Italian GAAP:							
Total current assets(4)	21,097	20,957	23,417	22,597	22,429	21,980	29,757
Tangible assets, net	23,776	21,072	22,097	19,449	18,324	17,717	23,985
Intangible assets, net(4)	39,528	39,062	39,045	34,412	33,853	32,874	44,505
Total assets	95,360	91,832	94,227	83,384	80,501	76,609	103,713
Short-term debt	16,927	16,536	9,072	6,827	10,613	2,027	2,744
Total current liabilities	30,179	29,207	22,984	20,385	23,373	14,650	19,833
Long-term debt	27,485	25,950	37,747	33,804			