TELEFONOS DE MEXICO S A B DE C V
Form 20-F
May 11, 2011
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As filed with the Securities and Exchange Commission on May 11, 2011.

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 or 15 (d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended: December 31, 2010

Commission File Number: 001-32741

Teléfonos de México, S.A.B. de C.V.

(Exact name of Registrant as specified in its charter)

Telephones of Mexico

(Translation of Registrant s name into English)

United Mexican States

(Jurisdiction of incorporation or organization)

Parque Vía 190, Colonia Cuauhtémoc, 06599 México, D.F., México

(Address of principal executive offices)

Anna Domínguez González

Teléfonos de México, S.A.B. de C.V.

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Colonia Cuauhtémoc

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Tel: (52) 55 52 22 17 74

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

SECURITIES 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 20 Series L Shares, without par value (L Share ADSs)	New York Stock Exchange
Series L Shares, without par value (L Shares)	New York Stock Exchange (for listing purposes only)
American Depositary Shares, each representing 20 Series A Shares, without par value (A Share ADSs)	The NASDAQ Capital Market
Series A Shares, without par value (A Share ADSs)	The NASDAQ Capital Market (for listing purposes only)
8.75% Senior Notes due 2016	New York Stock Exchange

SECURITIES 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

The number of outstanding shares of each class of capital or common stock as of December 31, 2010 was:

7,840 million	AA Shares
383 million	A Shares
9,935 million	L Shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

x Yes ¨ No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

¨ Yes x No

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.

x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). N/A

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

Large Accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

U.S. GAAP	¨	International Financial Reporting Standards as issued by the International Accounting Standards Board	¨	Other	x

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

¨ Item 17 x Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

¨ Yes x No

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FORWARD-LOOKING STATEMENTS

This annual report contains forward-looking statements. We may from time to time make forward-looking statements in our periodic reports to the SEC on Form 6-K, in our annual report to shareholders, in offering circulars and prospectuses, in press releases and other written materials and in oral statements made by our officers, directors or employees to analysts, investors, representatives of the media and others. Examples of such forward-looking statements include:

- projections of operating revenues, net income, net income per share, capital expenditures, indebtedness levels, dividends, capital structure or other financial items or ratios;
- statements of our acquisition or divestiture plans;
- statements about the impact of our acquisition of businesses;
- statements about our plans, objectives or goals, including those relating to competition, regulation and rates;
- statements about competition in the business sectors in which we operate;
- statements about our future financial performance or the economic performance of Mexico or other countries;
- statements about interest rates, currency exchange rates and foreign securities markets;
- statements about the availability and cost of external financing for our operations, which have been affected by the stress experienced by the global financial markets;
- statements about the renewal, revocation or expropriation of our concessions, decisions of regulatory and judicial authorities, and the future impact of regulations; and
- statements of assumptions underlying such statements.

Words such as believe, anticipate, plan, expect, intend, target, estimate, project, predict, forecast, guideline, should and intended to identify forward-looking statements but are not the exclusive means of identifying them.

Forward-looking statements involve inherent risks and uncertainties. We caution you that a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements. These factors, some of which are discussed under Item 3. Risk Factors beginning on page 6, include regulatory developments, economic and political conditions, which have been affected by the global economic crisis, competition, customer demand, government policies, inflation rates, exchange rates and technological changes. We caution you that the foregoing list of factors is not exclusive and that other risks and uncertainties may cause actual results to differ materially from those in forward-looking statements.

Forward-looking statements speak only as of the date they are made. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information or future events or for any other reason.

You should evaluate any statements made by us in light of these important factors.

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PART I

Item 1. Identity of Directors, Senior Management and Advisers

Not applicable.

Item 2. Offer Statistics and Expected Timetable

Not applicable.

Item 3. Key Information

SELECTED FINANCIAL DATA

The selected consolidated financial data set forth below have been derived from our consolidated financial statements for each of the five years in the period ended December 31, 2010, which have been audited by Mancera, S.C., a member practice of Ernst & Young Global, an independent registered public accounting firm. The selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, our audited consolidated financial statements and notes thereto included elsewhere in this annual report.

Beginning in 2012, Mexican issuers with securities listed on a Mexican securities exchange will be required to prepare financial statements in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). Issuers may voluntarily report using IFRS before the change in the reporting standards becomes mandatory. We will be presenting financial statements in accordance with IFRS for the fiscal year ending December 31, 2011, with an official IFRS adoption date as of January 1, 2011 and a transition date to IFRS of January 1, 2010.

Our consolidated financial statements have been prepared in accordance with Mexican Financial Reporting Standards, or Mexican FRS, which differ in certain respects from generally accepted accounting principles in the United States, or U.S. GAAP. Note 18 to our audited consolidated financial statements provides a description of the principal differences between Mexican FRS and U.S. GAAP, as they relate to us; a reconciliation to U.S. GAAP of net income and total stockholders equity; and condensed financial statements under U.S. GAAP.

Effect of Inflation Accounting

Due to the adoption of Mexican FRS B-10, effective January 1, 2008, we ceased to recognize the effects of inflation on our financial information. Through December 31, 2007, under Mexican Accounting Bulletin B-10, inflation accounting had extensive effects on the presentation of our financial statements. In our financial information, inflation adjustments for periods prior to 2008 have not been removed from stockholders equity and the re-expressed amounts for non-monetary assets and liabilities at December 31, 2007 became the accounting basis for those assets and liabilities beginning on January 1, 2008 and for subsequent periods, as required by Mexican FRS. Financial statements for periods prior to 2008 are presented in constant pesos as of December 31, 2007. See Item 5. *Operating and Financial Review and Prospects Effect of Inflation Accounting*.

In December 2007, we transferred our Latin American and yellow pages directory businesses to a new, separate entity, Telmex Internacional, S.A.B. de C.V. or Telmex Internacional, in an *escisión*, or split-up. See *Item 4. Information on the Company History*. The businesses we transferred to Telmex Internacional are presented as discontinued operations for dates and periods prior to the effective date of the *Escisión*, which was December 26, 2007 under Mexican FRS and June 10, 2008 under U.S. GAAP.

	Year ended December 31,				
	2010(2)	2009(2)	2008(2)	2007	2006
	(2010, 2009 and 2008 in millions of pesos, previous years in millions of constant pesos as of December 31, 2007, except share and per share data)				
Income Statement Data:					
Mexican FRS:					
Operating revenues	P. 113,563	P. 119,100	P. 124,105	P. 130,768	P. 129,755
Operating costs and expenses	85,146	84,736	84,362	86,884	83,491
Operating income	28,417	34,364	39,743	43,884	46,264
Financing cost, net	4,756	4,314	9,233	3,349	3,770
Income from continuing operations, net of income tax	15,371	20,469	20,177	28,889	27,701
Income from discontinued operations, net of income tax				7,166	2,615
Net income	15,371	20,469	20,177	36,055	30,316
Earnings per share(1)	0.85	1.11	1.07	1.80	1.41
Earnings per share from continuing operations	0.85	1.11	1.07	1.46	1.32
Earnings per share from discontinued operations				0.34	0.09
Dividends paid per share (nominal)(1)	0.490	0.845	0.413	0.440	0.403
Weighted average number of shares outstanding (millions)	18,189	18,383	18,906	19,766	20,948
U.S. GAAP:					
Operating revenues	P. 113,563	P. 119,100	P. 124,105	P. 130,768	P. 129,755
Operating costs and expenses	86,618	87,128	85,749	89,983	87,676
Operating income	26,945	31,972	38,356	40,785	42,079
Income from continuing operations, net of income tax	14,981	19,818	19,782	28,985	27,087
Income from discontinued operations, net of income tax			2,173	6,848	1,081
Net income	14,981	19,818	21,955	35,833	28,168
Earnings per share(1)	0.82	1.08	1.16	1.79	1.37
Earnings per share from continuing operations	0.82	1.08	1.05	1.47	1.29
Earnings per share from discontinued operations			0.11	0.32	0.08
Dividends paid per share (nominal)(1)	0.490	0.845	0.413	0.440	0.403

(See footnotes on following page)

	December 31, 2010[2]	2009[2]	2008[2]	2007	2006
	(2010, 2009 and 2008 in millions of pesos, previous years in millions of constant pesos as of December 31, 2007, except share and per share data and ratios)				
Balance Sheet Data:					
Mexican FRS:					
Plant, property and equipment, net[3]	P. 99,421	P. 106,048	P. 115,534	P. 122,396	P. 126,758
Total assets from continuing operations	157,754	178,397	187,125	172,826	188,182
Total assets from discontinued operations					107,366
Total assets	157,754	178,397	187,125	172,826	295,548
Short-term debt and current portion of long-term debt	11,952	19,769	22,883	12,282	9,041
Long-term debt	62,569	83,105	84,172	79,180	81,376
Total stockholders equity	44,224	38,321	39,371	42,159	121,321
Capital stock	9,009	9,020	9,139	9,403	28,011
Number of outstanding shares (millions)					
Series AA	7,840	8,115	8,115	8,115	8,115
Series A	383	395	407	430	446
Series L	9,935	9,682	10,033	10,815	11,642
U.S. GAAP:					
Plant, property and equipment, net[3]	P. 100,903	P. 108,196	P. 118,345	P. 126,572	P. 132,360
Total assets from continuing operations	145,352	167,494	177,033	163,263	183,815
Total assets from discontinued operations				132,191	87,807
Total assets	145,352	167,494	177,033	295,454	271,622
Short-term debt and current portion of long-term debt	11,952	19,769	22,883	12,282	9,041
Long-term debt	62,569	83,105	84,172	79,180	81,376
Total stockholders equity	10,447	7,465	11,309	122,414	103,195
Capital stock	9,009	9,020	9,139	27,231	28,011
Other Data:					
Mexican FRS:					
Ratio of earnings to fixed charges[4]	5.1	5.7	4.9	7.1	6.7
U.S. GAAP:					
Ratio of earnings to fixed charges[5]	5.1	5.6	4.9	7.0	6.7

(1) We have not presented net income or dividends on a per ADS basis. Each L Share ADS represents 20 L Shares, and each A Share ADS represents 20 A Shares. At a regular meeting held on December 1, 2009, the stockholders agreed to declare an extraordinary cash dividend of P.0.40 per outstanding share, paid in a single payment on December 17, 2009.

(2) Note 1 to our audited consolidated financial statements describes accounting pronouncements under Mexican FRS that became effective on January 1, 2008, which were applied on a prospective basis. As a result, the financial statements of prior years, which are presented for comparative purposes, have not been modified and may not be comparable to our financial statements for 2008 through 2010.

(3) The caption of inventories for operation of the telephone plant, net has been reclassified as part of the caption plant, property and equipment, net.

(4) Earnings for this purpose consist of earnings from continuing operations before provision for income tax and equity interest in net income of affiliates, plus fixed charges during the period. Fixed charges for this purpose consist of interest expense during the period. Fixed charges do not take into account gain or loss from monetary position or exchange gain or loss attributable to our indebtedness.

(5) Earnings for this purpose consist of earnings from continuing operations before provision for income tax and equity interest in net income of affiliates, plus fixed charges and depreciation of capitalized interest and minus interest capitalized during the period. Fixed charges for this purpose consist of interest expense plus interest capitalized during the period. Fixed charges do not take into account gain or loss from monetary position or exchange gain or loss attributable to our indebtedness.

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EXCHANGE RATES

The following table sets forth, for the periods indicated, the high, low, average and period-end exchange rate expressed in pesos per U.S. dollar.

Period	High	Low	Average(1)	Period End
2006	P. 10.43	P. 11.46	P. 10.90	P. 10.80
2007	10.67	11.27	10.84	10.92
2008	9.92	13.94	11.21	13.83
2009	12.63	15.41	13.58	13.06
2010	12.16	13.19	12.67	12.38
2010:				
November	12.21	12.57	12.34	12.45
December	12.33	12.47	12.39	12.38
2011:				
January	12.04	12.25	12.13	12.15
February	11.97	12.18	12.06	12.11
March	11.92	12.11	12.00	11.92
April	11.52	11.86	11.71	11.52

Sources: The U.S. Federal Reserve Bank of New York and the U.S. Federal Reserve Board.

(1) Average of month-end rates, where applicable.

On May 6, 2011, the exchange rate was P.11.58 to U.S.$1.00, according to the U.S. Federal Reserve Board.

We pay cash dividends in pesos, and exchange rate fluctuations affect the U.S. dollar amounts received by holders of our American Depositary Shares, or ADSs, on conversion by the depositary of cash dividends on the shares represented by such ADSs. Fluctuations in the exchange rate between the peso and the U.S. dollar affect the U.S. dollar equivalent of the peso price of our shares on the Mexican Stock Exchange (*Bolsa Mexicana de Valores, S.A.B. de C.V.*) and, as a result, can also affect the market price of the ADSs.

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RISK FACTORS

Risks Relating to Our Business Generally

Competition and shifting usage patterns are adversely affecting our revenues and profitability

Our revenues and our profitability continue to be adversely affected by increasing competition and by changes in how customers use telecommunications services. Our fixed-line network services face increasing competition from other technologies including wireless telephone service, wireless data service, cable television providers that offer telephone service, Voice over Internet Protocol (VoIP) service and others and the substitution of fixed-line telephony by these technologies. This process has adversely affected our traffic volume and our results of operations and will likely continue to do so in the future.

In addition to competition from other technologies, we also have numerous competitors in local service and in long-distance services. Governmental authorities in Mexico continue to grant new licenses and concessions to new market entrants, which results in increased competition.

The Mexican authorities have also adopted regulations to permit cable television providers to provide voice-transmission services to local fixed-line telecommunications operators and data and broadband Internet access services to the Mexican public. As of December 31, 2010, 32 cable television providers, through more than 300 concessions, have been authorized to provide local fixed-line voice-transmission service in various cities in Mexico. Regulations have also been adopted to allow other local telephone service providers to provide paid television and audio services, but to date we have been unable to obtain authorization to do so.

The effects of competition on our business are highly uncertain and depend on a variety of factors, including economic conditions, regulatory developments, the behavior of our customers and competitors and the effectiveness of measures we take in response to competition. Our ability to compete successfully depends on customer service, marketing and our ability to anticipate and respond to various competitive factors affecting the telecommunications industry, including new services and technologies, changes in consumer preferences, demographic trends, economic conditions and the commercial strategies of our competitors. If we are unable to respond to competition and compensate for declining prices by adding new customers, increasing usage and offering new services, our revenues and profitability could decline.

Regulatory developments could hurt our business by limiting our ability to pursue competitive and profitable strategies

Our business is subject to extensive government regulation, and it can be adversely affected by changes in law, regulation or regulatory policy that limit our ability to modify our business strategy. In particular, the regulatory developments described below could adversely affect us.

> Beginning 2007, the Competition Commission (*Comisión Federal de Competencia*) began eight industry-wide investigations into market power and monopolistic practices in certain segments of the Mexican telecommunications market. In four of these investigations, final resolutions have concluded that we and our subsidiary, Teléfonos del Noroeste, S.A. de C.V. or Telnor, have substantial power in the relevant markets investigated. Based on these final resolutions, the Mexican Federal Telecommunications Commission (*Comisión Federal de Telecomunicaciones*, or Cofetel) could impose specific tariff requirements or other special regulations such as additional requirements regarding disclosure of information or quality of service. We have filed petitions for constitutional protection (*amparo*) to challenge these

resolutions, all of which are pending. Of the four remaining cases relating to monopolistic practices, two remain under investigation and in the other two the Competition Commission has issued a notice of probable fault *(Oficio de Probable Responsabildad)*, to which we have objected. Findings adverse to us in any of the Competition Commission proceedings may lead to the imposition of additional regulations, prohibitions or monetary penalties, which in turn could have an adverse effect on our business and results of operations.

In February 2009, Cofetel published a Fundamental Technical Plan of Interconnection and Inter-Operability, or the Fundamental Technical Plan, which requires operators with the greatest number of access points to provide other operators with access to our network on an unbundled basis that disaggregates the prices for different service elements. We believe this may result in pricing network access at rates below the recovery cost for our infrastructure investments and may have a negative impact on us and the Mexican telecommunications sector in general. In October 2009, Cofetel issued two resolutions determining that we and Telnor are operators with the largest number of access points in our respective concession coverage areas. We have filed petitions for constitutional protection (*amparo*) against the Fundamental Technical Plan and these resolutions, which are pending.

In November 2005, Cofetel issued guidelines for making changes to local service areas, including the consolidation of such local service areas. We are challenging the legality of the underlying guidelines in the Mexican courts. If the guidelines are upheld and new resolutions to consolidate our local service areas are implemented, we believe this consolidation would have an adverse impact on our revenues from long-distance service.

On April 12, 2011, Cofetel published in the *Official Gazette*, guidelines for developing cost models to be used to settle disputes regarding interconnection rates between public telecommunication networks providers. We believe that these guidelines could have an adverse impact on our revenues from interconnection services and on our operating results.

Adverse global economic conditions and, in particular, the slowdown of the U.S. and Mexican economies, could have a negative impact on our operating results and financial condition

Our business is influenced by general economic conditions worldwide and in Mexico. Further deterioration in the economic environment could have an adverse effect on demand for some of our products and services. The Mexican economy is influenced by the U.S. economy, so a deterioration in economic conditions or delayed recovery of the U.S. economy may hinder a recovery in Mexico. In difficult economic conditions our customers may seek to reduce discretionary spending. Under these conditions our business customers may delay purchasing decisions, delay full implementation of service offerings or reduce their use of services. Adverse economic conditions may also lead to an increase in the number of our residential and business customers that are unable to pay for services. If these events were to occur, it could have a material adverse effect on our business and results of operations.

The ongoing uncertainty in global financial markets could adversely affect our financing costs and exposure to our customers and counterparties

The recent instability in the global financial markets and ongoing uncertainty affecting these markets have resulted in extreme volatility in the credit, equity and fixed income markets. This volatility has limited many companies access to funding. If access to credit tightens further and borrowing costs rise, our costs could be adversely affected. Difficult financial markets may also adversely affect some of our customers, including other telecommunications carriers that pay us for interconnection and other services. In addition, we enter into derivative transactions with large financial institutions to support our treasury operations, including contracts to hedge our exposure to interest rates and foreign exchange, and we could be adversely affected by severe financial difficulties faced by our counterparties.

Our industry is subject to rapid technological changes, which could adversely affect our ability to compete

The telecommunications industry is subject to rapid technological change. Our future success depends, in part, on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge and that existing products and technologies will further develop. These new products and technologies may reduce the prices we can charge for our services or they may be superior to, and render obsolete, the products and services we offer and the technologies we use. They may consequently reduce the revenues generated by our products and services or require investment in new technology. As a result, our most significant competitors in the future may be new entrants to our markets that would not be burdened by an installed base of older equipment.

Developments in the telecommunications sector may result in substantial write-downs of the carrying value of certain of our assets

We review the value of our long-lived assets, where the circumstances require, to assess whether those carrying values can be supported by the future cash flows expected to be derived from those assets. In addition, whenever we consider that our fixed assets, intangible assets or goodwill may be impaired due to changes in the economic, regulatory or business environment, we consider the necessity of performing certain valuation tests, which may result in impairment charges. The recognition of impairments of long-lived tangible and intangible assets could result in a non-cash charge on our income statement, which could adversely affect our results of operations.

A network failure could cause delays or interruptions of service, which could cause us to lose customers and revenues

We will need to continue to provide our users with reliable service over our network. Some of the risks to our network and infrastructure include physical damage to our network, natural disasters such as hurricanes, earthquakes, floods and storms, among others, and other disruptions beyond our control. Although we carry casualty insurance against loss and we have implemented redundancy in our network and installed backup technologies, disruptions may cause interruptions in service or reduced capacity for customers, either of which could cause us to lose customers and revenues or incur additional expenses.

We are exposed to currency and interest rate risk on our debt, and we have entered into derivatives contracts to limit these risks

A substantial part of our indebtedness is denominated in U.S. dollars, and we have relatively limited assets and revenues denominated in U.S. dollars. As of December 31, 2010, our U.S. dollar-denominated indebtedness amounted to P.40,853 million. In addition, a substantial part of our indebtedness bears interest at variable rates. As a result, we are exposed to risks from changing currency exchange rates and interest rates.

To offset these risks, we enter into derivative financial instruments with large financial institutions to minimize the impact of fluctuations in exchange rates and variable interest rates on our indebtedness. We have not entered into derivative financial instruments for any other purposes, although we may do so in the future. The types of derivative instruments we have typically entered into in recent periods include cross-currency swaps (in which we generally pay peso amounts based on peso interest rates and receive U.S. dollar amounts based on dollar interest rates), interest-rate swaps (in which we generally pay

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amounts based on fixed interest rates and receive amounts based on variable interest rates) and forward exchange contracts (in which we generally agree to use pesos to purchase U.S. dollars at a future date).

Our derivative financial instruments do not provide complete protection against the exchange rate or interest-rate risk of our indebtedness. We may determine that the risks are acceptable or that the protection available through derivative financial instruments in the market is insufficient or too costly. These determinations depend on many factors, including market conditions, the specific risks in question, and our expectations concerning future market developments. We review and change our derivatives positions regularly, and our hedging policies change from time to time.

When the financial markets are volatile, as they have been in recent periods, our results of operations may be substantially affected by variations in exchange rates and, to a lesser degree, interest rates. These effects include foreign exchange gain and loss on assets and liabilities denominated in U.S. dollars, fair value gain and loss on derivative financial instruments, and changes in interest income and interest expense. These effects can be much more volatile than our operating performance or our operating cash flows.

We attempt to match the cash flows on our derivative financial instruments with the cash flows on our indebtedness. The net effects on our reported results in any period are difficult to predict and depend on market conditions and on the specifics of our derivatives positions. For example, in 2010 the peso appreciated against the U.S. dollar by 5.4%. As a result, in 2010, we recognized a net exchange gain on our U.S. dollar denominated debt and a net fair value loss on currency derivatives. In 2010, we also recognized lower interest expense due to a lower average level of debt.

Our derivative financial instruments are also subject to the risk that counterparties will default or seek bankruptcy protection. The instability and uncertainty in the financial markets has made it more difficult to assess the risk of counterparties to derivatives contracts. Moreover, in light of the greater volatility in the global securities and exchange markets, there may be fewer financial entities available with which we could continue entering into derivative financial instruments to protect against currency and interest rate risks.

Substantially all our business is in Mexico, so we are affected by adverse economic or political conditions in Mexico

Substantially all of our business operations and assets are located in Mexico. Our financial performance may be affected by general economic, political and social conditions in Mexico. In the past, Mexico has experienced both prolonged periods of weak economic conditions and deterioration in economic conditions that have had a negative impact on our company. Mexico has also experienced high levels of inflation and high domestic interest rates in the past, which significantly lowered the purchasing power of consumers and businesses. Mexico began to enter a recession in the fourth quarter of 2008, during which GDP fell by approximately 1.6%. GDP fell by an additional 6.5% in 2009. By 2010, GDP rose by 5.5%. If the Mexican economy experiences a downturn or if inflation and interest rates increase significantly, our business, financial condition and results of operations could suffer material adverse consequences because, among other things, demand for telecommunications services may decrease and consumers may find it difficult to pay for the services we offer.

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Our corporate restructuring may affect our stock price

On April 4, 2011, we announced that at the extraordinary meeting held on that date, our shareholders approved a corporate restructuring which contemplates the creation of a subsidiary company that will provide telecommunications and interconnection services in rural areas where our fixed telephony competitors have not invested. The subsidiary company will be named Telmex Social. This may affect our stock price. The restructuring is subject to the authorization and confirmation of the applicable governmental authorities as well as the authorizations required under the Mexican companies law.

Risks Relating to Our Controlling Shareholder and Capital Structure

We are controlled by one shareholder

A majority of the voting shares of our company (74.1% as of February 24, 2011) is owned by América Móvil, S.A.B. de C.V., or América Móvil, indirectly through Carso Global Telecom, S.A.B. de C.V., or Carso Global Telecom. América Móvil has the effective power to designate a majority of the members of our Board of Directors and to determine the outcome of other actions requiring a vote of the shareholders, except in very limited cases that require a vote of the holders of L Shares. América Móvil may be deemed to be controlled by Carlos Slim Helú and members of his immediate family, who, taken together, own a majority of the common stock of América Móvil.

The protections afforded to minority shareholders in Mexico are different from those in the United States

Our bylaws provide that any dispute between us and our shareholders will be governed by Mexican law and that legal actions relating to the execution, interpretation or performance of the bylaws may be brought only in Mexican courts. Under Mexican law, the protections afforded to minority shareholders are different from those in the United States. In particular, the case law concerning fiduciary duties of directors is not well developed, there is no procedure for class actions, there are different procedural requirements for bringing shareholder lawsuits and there are different discovery rules. As a result, it may be more difficult in practice for minority shareholders of Telmex to enforce their rights against us, our directors or our controlling shareholder than it would be for shareholders of a U.S. company.

We engage in transactions with related parties that may create the potential for conflicts of interest

We engage in transactions with entities that, like us, are controlled, directly or indirectly, by Carlos Slim Helú and members of his immediate family. These entities include (a) América Móvil and its subsidiaries, (b) Grupo Carso, S.A.B. de C.V., or Grupo Carso, and its subsidiaries and (c) Grupo Financiero Inbursa, S.A.B. de C.V., or Grupo Financiero Inbursa, and its subsidiaries. Our transactions with América Móvil include interconnection between our respective networks and the completion of international traffic in each other s countries of operation, América Móvil s printing and distribution of our directories and América Móvil s access to our customer database and our billing and collection system in connection with its directories business. In addition, we recently entered into loan agreements with América Móvil. Transactions with Grupo Carso include the purchase of network construction services and materials, and transactions with Grupo Financiero Inbursa include financial services and insurance. We also have agreements with AT&T International that provide for the completion of calls in our respective countries of operation.

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Our transactions with related parties may create the potential for conflicts of interest.

Holders of L Shares and L Share ADSs have limited voting rights

Our bylaws provide that holders of L Shares are not permitted to vote except on such limited matters as the transformation or merger of Telmex or the cancellation of registration of the L Shares with the National Securities Registry (*Registro Nacional de Valores*), managed by the Mexican National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*), or any stock exchange on which they are listed. If you hold L Shares or L Share ADSs, you will not be able to vote on most matters, including the declaration of dividends that are subject to a shareholder vote in accordance with our bylaws.

Holders of ADSs are not entitled to attend shareholders meetings, and they may only vote through the ADS depositary

Under Mexican law, a shareholder is required to deposit its shares with a custodian in order to attend a shareholders meeting. As long as a shareholder holds shares in ADS form, the shareholder will not be able to satisfy this requirement. There can be no assurance that holders of ADSs will receive notice of shareholders meetings from our ADS depositary in sufficient time to enable such holders to return voting instructions to the ADS depositary in a timely manner. In the event that instructions are not received with respect to any shares underlying ADSs, the ADS depositary will, subject to certain limitations, grant a proxy to a person designated by us. In the event that this proxy is not granted, the ADS depositary will vote these shares in the same manner as the majority of the shares of each class for which voting instructions are received.

You may not be entitled to preemptive rights

Under Mexican law, if we issue new shares for cash as part of a capital increase, we generally must grant our shareholders the right to purchase a sufficient number of shares to maintain their existing ownership percentage in Telmex. Rights to purchase shares in these circumstances are known as preemptive rights. Preemptive rights do not arise upon the sale of newly issued shares in a public offering or the resale of shares of capital stock previously repurchased by us.

We may not legally be permitted to allow holders of ADSs or holders of L Shares or A Shares in the United States to exercise any preemptive rights in any future capital increase unless we file a registration statement with the U.S. Securities and Exchange Commission, or SEC, with respect to that future issuance of shares. At the time of any future capital increase, we will evaluate the costs and potential liabilities associated with filing a registration statement with the SEC and any other factors that we consider important to determine whether we will file such a registration statement. We cannot assure you that we will file a registration statement with the SEC to allow holders of ADSs or U.S. holders of L Shares or A Shares to participate in a preemptive rights offering. As a result, the equity interest of such holders in Telmex may be diluted proportionately. In addition, under current Mexican law, it is not practicable for the ADS depositary to sell preemptive rights and distribute the proceeds from such sales to ADS holders.

Our bylaws restrict the acquisition of shares in some circumstances

Our bylaws provide that any acquisition of more than 10% of our capital stock by any person or group of persons acting together requires the approval of our Board of Directors. If you wish to acquire more than 10% of our capital stock, you will not be able to do so without the approval of our Board of Directors.

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Our bylaws restrict the ability of non-Mexican shareholders to invoke the protection of their governments with respect to their rights as shareholders

As required by Mexican law, our bylaws provide that non-Mexican shareholders shall be considered as Mexicans in respect of their ownership interests in Telmex and shall be deemed to have agreed not to invoke the protection of their governments in certain circumstances. Under this provision, a non-Mexican shareholder is deemed to have agreed not to invoke the protection of his own government by asking such government to interpose a diplomatic claim against the Mexican government with respect to the shareholder s rights as a shareholder, but is not deemed to have waived any other rights he may have, including any rights under the U.S. securities laws, with respect to his investment in Telmex. If you invoke such governmental protection in violation of this agreement, your shares could be forfeited to the Mexican government.

It may be difficult to enforce civil liabilities against us or our directors, officers and controlling persons

Telmex is organized under the laws of Mexico, and most of our directors, officers and controlling persons reside outside the United States. In addition, all or a substantial portion of our assets and the assets of our directors, officers and controlling persons are located in Mexico. As a result, it may be difficult for investors to effect service of process within the United States on such persons or to enforce judgments against them, including in any action based on civil liabilities under the U.S. federal securities laws. There is doubt as to the enforceability against such persons in Mexico, whether in original actions or in actions to enforce judgments of U.S. courts, of liabilities based solely on the U.S. federal securities laws.

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Item 4. Information on the Company

GENERAL

Overview

We own and operate a fixed-line telecommunications system in Mexico, where we are the only nationwide provider of fixed-line telephony services. We also provide other telecommunications and telecommunications-related services such as corporate networks, Internet access services, information network management, telephone and computer equipment sales, and interconnection services to other carriers.

We have developed a multi-service network in which 94.7% of our lines have the capacity to provide simultaneous transmission of voice and data through a broadband connection. Our network capability allowed us to increase the number of customers of our broadband Internet access service by 12.8% in 2010 to 7.4 million. At the same time, we are extending our voice and Internet access services to remote areas.

In 2010, we continued our efforts to grow voice and data service revenues by offering multiple-service products. In addition, we have made investments to increase our service offerings and to update the telecommunications platform in rural areas where we are the sole telecommunications carrier. We plan to continue expanding our multiple-service offerings in the future and to take advantage of technological advances in order to provide our customers with packages that combine voice, data and eventually video.

We intend to provide paid television and audio services and to expand our multi-service products to include triple play packages, which would include telephone, Internet access and paid television services in a single subscription. However, we have not been able to obtain the regulatory authorization we need to offer television and audio services. A Convergence Agreement (*Acuerdo de Convergencia*), issued in October 2006 by the Communication Ministry, established the requirements that market participants must meet to foster full convergence of telephone, Internet and television services in Mexico. Even though we believe we have met all the requirements, we still do not have authorization to offer television and audio services, and we believe that this situation is negatively affecting the technological development of our country.

Substantially all of our operations are now conducted in Mexico. Our strategy is to increase the value of our lines by capitalizing on our extensive and modern infrastructure and our technical capabilities to provide high-quality services to our customers across Mexico, pursuing growth in the broadband and data businesses, introducing and promoting packaged service offerings combining broadband with voice services at attractive prices, and maintaining our focus on customer service. In Mexico s major population centers, data is a source of growth, and we are well positioned to deliver Internet access and meet the demands of the growing data market. We plan to continue selling computer equipment at our Telmex stores and increase the Internet penetration rate in Mexico.

We are a Mexican corporation headquartered in Mexico City, Mexico. Our legal name is Teléfonos de México, S.A.B. de C.V., and we frequently refer to ourselves commercially as Telmex. Our principal executive offices are located at Parque Vía 190, Colonia Cuauhtémoc, 06599 México, D.F., México. Our telephone number at this location is (52) 55 5222 1774. Our website can be accessed at www.telmex.com.

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In this annual report, we, us or our refers to Teléfonos de México, S.A.B. de C.V. and, where the context requires, its consolidated subsidiaries.

History

We were formed in 1947 under private foreign ownership to acquire the Mexican telephone business of a wholly owned subsidiary of the LM Ericsson group of Sweden. In 1950, we acquired the Mexican telephone business of a wholly owned subsidiary of the International Telephone and Telegraph Company, which operated the only other national telephone network in Mexico at that time. In 1972, the Mexican federal government acquired the majority of our capital stock. In December 1990, the Mexican government sold shares representing voting control of our company. The Mexican government sold the balance of its shares in a series of transactions beginning in May 1991.

In September 2000, we transferred our Mexican wireless business and our foreign operations at the time to América Móvil in an *escisión*, or split-up. Beginning in 2004, we expanded our operations outside Mexico through a series of acquisitions in Brazil, Argentina, Chile, Colombia, Peru, Ecuador and the United States. In December 2007, we transferred our Latin American and yellow pages directory businesses to a new, separate entity, Telmex Internacional, in a second *escisión*, or split-up (the *Escisión*). In an *escisión*, an existing company is divided, creating a new company to which specified assets and liabilities are allocated. The shares of the new company are issued to the shareholders of the existing company, pro rata to their share ownership in the existing company. This procedure differs from the procedure by which a spin-off is typically conducted in the United States, where a parent company distributes to its shareholders shares of a subsidiary.

The *Escisión* was approved by our shareholders on December 21, 2007. The establishment of Telmex Internacional became effective on December 26, 2007. As of the effective date of the *Escisión*, each holder of Telmex shares became the owner of an equal number of Telmex Internacional shares of the corresponding class, and each Telmex ADS represented an equal number of Telmex and Telmex Internacional shares. On June 10, 2008, the shares and ADSs of Telmex Internacional began trading separately from our shares and ADSs on the Mexican Stock Exchange and the New York Stock Exchange.

In May 2010, América Móvil launched two separate but concurrent public exchange offers to acquire the outstanding capital stock of Carso Global Telecom and Telmex Internacional. At that time, Carso Global Telecom was the direct holder of 59.4% of the outstanding capital stock of Telmex. In June 2010, América Móvil completed its first public exchange offer. Through this offer, América Móvil directly acquired 99.4% of the outstanding capital stock of Carso Global Telecom and indirectly acquired 59.1% of the outstanding capital stock of Telmex. In November 2010, América Móvil launched a second public exchange offer, which was completed in December 2010, and increased América Móvil´s indirect ownership of the outstanding capital stock of Telmex to 59.5%. América Móvil may be deemed to be controlled by Carlos Slim Helú and members of his immediate family.

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On April 4, 2011, we announced that at the extraordinary meeting held on that date, our shareholders approved a corporate restructuring which contemplates the creation of a subsidiary company that will provide telecommunications and interconnection services in rural areas where our fixed telephony competitors have not invested. The subsidiary company will be named Telmex Social.

Telmex Social will provide services mainly in rural areas. A substantial number of Mexican migrant workers hail from these rural areas and make telephone calls to these places. These areas have high call termination volumes from the United States, where negotiated interconnection rates have declined 95% since 1990. These interconnection rates are lower than those charged in many other countries, particularly taking into account that most of these areas are remote and sparsely populated.

Considering that these regions experience significant economic and social disadvantages, we expect that this restructuring will promote access to telecommunications services by demonstrating the importance of both investing in the expansion and modernization of these services and encouraging the growth of digital culture. This should improve the quality of life of rural inhabitants and integrate rural communities into Mexico s socio-economic development.

Telmex Social s network infrastructure could be complemented with investments from other telecommunications operators and, if the Mexican federal government approves, with investments and support for providing access to voice, data, and video from both the Mexican federal government and decentralized public sector companies.

The interconnection rates to be determined by Telmex Social will be the same for all telecommunications operators, including Telmex.

We estimate that Telmex Social will serve approximately 1.5 million lines, with a density of 14.8 inhabitants per line, located in 10,453 communities which are not being served by competitors. The local service areas of Telmex Social comprise approximately 40% of the country where there are more than 22 million inhabitants.

The restructuring is subject, if needed, to the approval of the Communications Ministry, as well as the authorization and confirmation of the rest of the corresponding authorities and government entities.

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Significant Subsidiaries and Investees

The following table sets forth our significant subsidiaries and affiliated companies accounted for using the equity method at December 31, 2010:

Name of Company	Jurisdiction of establishment	Percentage of ownership and voting interest	Description
Subsidiaries			
Integración de Servicios TMX, S.A. de C.V.	Mexico	100%	Intermediate holding company.
Alquiladora de Casas, S.A. de C.V.	Mexico	100%	Real estate company owning our facilities.
Compañía de Teléfonos y Bienes Raíces, S.A. de C.V.	Mexico	100%	Real estate company owning our facilities.
Consorcio Red Uno, S.A. de C.V.	Mexico	100%	Supplier of telecommunications network integration services and information systems.
Teléfonos del Noroeste, S.A. de C.V.	Mexico	100%	Fixed-line public network concessionaire for the state of Baja California Norte and the San Luis Rio Colorado region of the state of Sonora.
Uninet, S.A. de C.V.	Mexico	100%	Provider of corporate networks and Internet access services to Telmex and corporate customers.
Telmex USA, L.L.C.	Delaware	100%	Authorized long-distance service re-seller, provider of prepaid telephone cards and payment collection services for lines in Mexico (installation and monthly rental), and authorized by the FCC to provide facility-based long-distance services, data transmission and cross-border data transit services.
Affiliated companies			