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As filed with the Securities and Exchange Commission on June 27, 2002.

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2001

Commission File Number: 1-10749

Teléfonos de México, S.A. 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)

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)

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

American Depositary Shares, each representing 20 Series A Shares, without par value ("A Share ADSs")

Series A Shares, without par value ("A Shares")

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, 2001 was:

4,307 million	**AA Shares**
313 million	**A Shares**
8,545 million	**L Shares**

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

Yes __X__ **No** ____

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

Item 17 ____ **Item 18** __X__

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PART I

Item 3. Key Information

SELECTED FINANCIAL DATA

The selected consolidated financial data set forth below have been derived from our audited consolidated financial statements for each of the years in the five-year period ended December 31, 2001, which have been reported on by Mancera, S.C., a member of Ernst & Young Global, independent public accountants. The selected consolidated financial data should be read in conjunction with, and are qualified in their entirety by reference to, our consolidated financial statements and notes thereto included elsewhere in this Annual Report.

The consolidated financial statements included in this Annual Report have been restated to reflect as discontinued operations the businesses we spun off in September 2000 to América Móvil, S.A. de C.V.

Our consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Mexico, or Mexican GAAP, which differ in certain important 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 GAAP and U.S. GAAP, as they relate to us; a reconciliation to U.S. GAAP of operating income, net income and total stockholders' equity; and a condensed statement of cash flows under U.S. GAAP.

Pursuant to Mexican GAAP, in the consolidated financial statements and the selected consolidated financial data set forth below:

- nonmonetary assets (including plant, property and equipment) and stockholders' equity are restated for inflation and, in the case of imported telephone plant, as described below,

- gains and losses in purchasing power from holding monetary liabilities or assets are recognized in income, and

- all financial statements are restated in constant pesos as of December 31, 2001.

Since January 1, 1997, we have restated plant, property and equipment of non-Mexican origin based on the rate of inflation in the country of origin and the prevailing exchange rate at the balance sheet date; other fixed assets are restated based on the Mexican National Consumer Price Index. We have not reversed the effect of inflation accounting under Mexican GAAP in the reconciliation to U.S. GAAP of our net income and stockholders' equity, except with respect to the methodology for restatement of plant, property and equipment of non-Mexican origin. See Note 18 to the consolidated financial statements.

	Year ended December 31,				
	2001	**2000**	**1999**	**1998**	**1997**
	(in millions of constant pesos as of December 31, 2001, except per share data)				
Income Statement Data:					
Mexican GAAP:					
Gross operating revenues	P. 110,967	P. 106,557	P. 96,880	P. 91,368	P. 86,775
Operating costs and expenses	68,376	65,106	58,148	55,520	55,465
Operating income	42,591	41,451	38,732	35,848	31,310
Income from continuing operations	23,494	26,098	23,713	16,378	17,218
Income from discontinued operations(1)	—	1,538	4,870	4,577	2,257
Net income	23,494	27,636	28,583	20,955	19,475
Income per share from continuing operations—Basic(2)	1.735	1.779	1.571	1.036	1.024
Income per share from continuing operations—Diluted(2)	1.629	1.683	1.534	1.036	1.024
Net income per share—Basic(2)	1.735	1.884	1.894	1.326	1.159
Net income per share—Diluted(2)	1.629	1.784	1.852	1.326	1.159
Dividends per share(2)(3)	0.490	0.445	0.388	0.350	0.263
U.S. GAAP:					
Operating revenues	P. 110,967	P. 106,557	P. 96,880	P. 91,368	P. 86,775
Operating income	35,178	35,260	32,196	30,018	25,401
Income from continuing operations	20,225	24,154	22,592	15,980	16,363
Income from discontinued operations(1)	—	1,302	4,072	3,992	2,188
Net income	20,225	25,456	26,664	19,972	18,551
Income per share from continuing operations—Basic(2)	1.494	1.647	1.497	1.011	0.973
Income per share from continuing operations—Diluted(2)	1.399	1.557	1.461	1.011	0.973
Net income per share—Basic(2)	1.494	1.735	1.767	1.263	1.104
Net income per share—Diluted(2)	1.399	1.642	1.726	1.263	1.104
Dividends per share(2)(3)	0.490	0.445	0.388	0.350	0.263

	December 31,				
	2001	**2000**	**1999**	**1998**	**1997**
	(in millions of constant pesos as of December 31, 2001)				
Balance Sheet Data:					
Mexican GAAP:					
Plant, property and equipment, net	P. 114,454	P. 111,205	P. 111,409	P. 129,154	P. 133,981
Total assets of continuing operations	156,911	163,789	155,384	166,039	170,868
Total assets of discontinued operations(1)	—	—	69,658	54,891	48,343
Total assets	156,911	163,789	225,042	220,930	219,211
Long-term debt	52,254	31,629	27,871	32,292	30,556
Total stockholders' equity(4)	50,762	51,626	139,118	135,304	133,708
U.S. GAAP:					
Total assets of continuing operations	P. 179,145	P. 183,365	P. 177,093	P. 181,718	P. 190,526
Total assets of discontinued operations(1)	—	—	70,366	55,674	49,021
Total assets	179,145	183,365	247,459	237,392	239,547
Long-term debt	52,254	31,629	27,871	32,292	30,556
Total stockholders' equity(4)	52,901	50,569	128,696	118,649	119,236

(1) The businesses we spun off to América Móvil in September 2000 are presented as discontinued operations.

(2) We have not presented net income or dividends on a per ADS basis. Each L Share ADS represents twenty L Shares and each A Share ADS represents twenty A Shares.

(3) Nominal amounts.

(4) The decrease in 2000 was due to the spin-off of América Móvil.

EXCHANGE RATES

Mexico has had a free market for foreign exchange since November 1991. Prior to December, 1994, Banco de México kept the peso-U.S. dollar exchange rate within a range prescribed by the Government through intervention in the foreign exchange market. In December 1994, the Government suspended intervention by Banco de México and allowed the peso to float freely against the U.S. dollar. The peso declined sharply in December 1994 and continued to fall under conditions of high volatility in 1995. In 1996 and most of 1997, the peso fell more slowly and was less volatile. In the last quarter of 1997 and for much of 1998, the foreign exchange markets were volatile as a result of financial crises in Asia and Russia and financial turmoil in countries including Brazil and Venezuela. The peso has been relatively stable since 1999, declining in 1999 and 2000, appreciating slightly in 2001 and declining in 2002 to date. There can be no assurance that the Government will maintain its current policies with regard to the peso or that the peso will not further depreciate or appreciate significantly in the future.

The following table sets forth, for the periods indicated, the high, low, average and period-end noon buying rate in New York City for cable transfers in pesos published by the Federal Reserve Bank of New York, expressed in pesos per U.S. dollar. The rates have not been restated in constant currency units.

Period	High	Low	Average(1)	Period End
1997	P. 7.72	P. 8.41	P. 7.97	P. 8.07
1998	8.04	10.63	9.24	9.90
1999	9.24	10.60	9.56	9.48
2000	9.18	10.09	9.47	9.62
2001	8.95	9.97	9.33	9.16
2001:				
December	P. 9.10	P. 9.25		
2002:				
January	P. 9.10	P. 9.25		
February	9.05	9.17		
March	9.00	9.11		
April	9.00	9.38		
May	9.41	9.71		

(1) Average of month-end rates.

On June 26, 2002 the noon buying rate was P.9.98 to U.S.$1.00.

We will pay any cash dividends in pesos, and exchange rate fluctuations will affect the U.S. dollar amounts received by holders of 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 have affected the U.S. dollar equivalent of the peso price of our shares on the Mexican Stock Exchange and, as a result, have also affected the market price of the ADSs.

RISK FACTORS

Risks Relating to Our Business Generally

Increasing Competition Could Adversely Affect Our Market Share, Revenues and Profitability

Our results of operations have been affected by the opening of the Mexican market for long distance services to competition beginning in August 1996 and the availability of interconnection to our network beginning January 1, 1997. Competing carriers have won a share of the long distance market, and prices have fallen steadily as real rates have fallen and customer discounts have increased. The effects of increased competition have been particularly severe in international long distance service, where our revenues declined from 1996 through 1998 and again in 2000 and 2001. We believe the decline in our international traffic volume has been adversely affected by an unauthorized practice referred to as "illegal bypass," which occurs when an incoming international call is routed into Mexico through private circuits or other channels and then handled as a domestic call. The practice is difficult to prevent and is likely to arise whenever there is a substantial price advantage to be gained by competing carriers. Increased competition may adversely affect our market share, revenues and profitability.

Competition in local service, principally from wireless service providers, has been developing since 1999. In December 2001, there were 21.8 million cellular lines in service compared with 13.8 million fixed lines in service. At present, there are 14 competitive fixed-line local operators, primarily in Mexico City and other large cities. Other operators that are currently long distance operators (Avantel and Alestra) and cellular operators with PCS and fixed wireless frequencies also provide local service. We cannot yet predict the long-term effects of local service competition on our results of operations.

The effects of increased competition on our business are highly uncertain and will depend on a variety of factors, including Mexican economic conditions, regulatory developments including the lowering of interconnection fees, the behavior of our customers and competitors and the effectiveness of measures we take.

Dominant Carrier Regulations and Other Regulatory Developments Could Hurt Our Business by Limiting Our Ability to Pursue Competitive and Profitable Strategies

Our business is subject to extensive regulation, and it can be adversely affected by changes in law, regulation or regulatory policy. In particular, the Mexican Competition Commission has determined that we are a dominant provider of certain telecommunications services, and Mexican law provides for the regulatory authorities to impose additional regulations on a dominant provider. In September 2000, the Mexican Federal Telecommunications Commission *(Comisión Federal de Telecomunicaciones,* or "Cofetel") adopted regulations that apply specifically to us as a dominant carrier. In May 2001, a Mexican court held that the determination that we are a dominant carrier was procedurally defective, but the Mexican Competition Commission addressed the defect and issued a second resolution with the same findings later in May 2001. In May 2002, a federal court nullified several resolutions issued by the Competition Commission and Cofetel, including the September 2000 resolution adopting the dominant carrier regulations. We believe that if dominant carrier regulations are eventually implemented, the new substantive rules and the related regulatory procedures will reduce our flexibility to adopt competitive tariff policies.

Our financial performance may be affected by changes in interconnection fees we charge to other carriers and our ability to collect interconnection fees from competing carriers. Cofetel oversees the negotiation and establishment of interconnection fees and imposes the fees where negotiations fail. Interconnection fees have been the subject of controversy and litigation. For example, the interconnection fees we charged to competing long distance carriers were reduced by action of Cofetel in October 2000. Actions of Mexican regulatory authorities in these or other areas could require us to adopt fees or other practices that differ from those we would otherwise adopt.

The United States has initiated World Trade Organization (WTO) dispute settlement with Mexico regarding alleged illegal barriers to competition in the Mexican telecommunications market. The United States claims that Mexico has not complied with its WTO commitments because it has failed to ensure that (i) we provide international termination to U.S. telecommunications carriers at "cost-based" and "reasonable" rates and (ii) U.S. companies can route their calls into and out of Mexico over leased lines. While we believe that the U.S. claims are politically motivated and incorrect, an adverse decision by the panel could lead to trade sanctions against Mexico and could prompt changes in regulation affecting our business.

In October 2001, the Mexican Congress announced the beginning of a process to reform the *Ley Federal de Telecomunicaciones* (the Federal Telecommunications Law). We cannot predict whether or when such amendments may be implemented and, if implemented, their effect on our business.

The Spin-off of América Móvil in 2000 Substantially Changed Our Business

In September 2000, we spun off our Mexican mobile telecommunications business and most of our investments outside Mexico to América Móvil. We are now a substantially less diversified telecommunications company than we were before the spin-off. The businesses that we will continue to operate, which consist primarily of Mexican fixed line telecommunications, including Internet and data businesses, may have lesser prospects for future growth than those we spun off. Because we are no longer engaged in wireless telecommunications, our business may be adversely affected by the development and commercial success of providers of wireless and other new technologies, including América Móvil. The spin-off left us with substantially more debt and less cash and marketable securities than before.

Risks Relating to Our Controlling Shareholder and Capital Structure

We Are Controlled by One Shareholder

A majority of the voting shares of our company (66.6% as of April 30, 2002) is indirectly controlled by Carso Global Telecom, S.A. de C.V., which is controlled by Carlos Slim Helú and members of his immediate family. Carso Global Telecom 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.

The Protections Afforded to Minority Shareholders in Mexico Are Different from Those in the United States

Under Mexican law, the protections afforded to minority shareholders are different from those in the United States. In particular, the law concerning fiduciary duties of directors is not well developed, there is no procedure for class actions or shareholder derivative actions, and there are different procedural requirements for bringing shareholder lawsuits. As a result, in practice it may be more difficult for minority shareholders of Telmex to enforce their rights against us or our directors or controlling shareholder than it would be for shareholders of a U.S. company.

We Engage in Transactions with Affiliates That May Create the Potential for Conflicts of Interest

We engage in transactions with certain subsidiaries of Grupo Carso, S.A. de C.V. and Grupo Financiero Inbursa, S.A., which are under common control with Carso Global Telecom. Transactions with subsidiaries of Grupo Carso include the purchase of goods, services and insurance. We also engage in transactions with América Móvil, which is controlled by América Telecom, S.A. de C.V. América Telecom, like Carso Global Telecom, is controlled by Carlos Slim Helú and members of his immediate family. Transactions with América Móvil include certain agreements implementing the spin-off and providing for transitional services, as well as ongoing commercial relationships. We also make investments jointly with our affiliates as well as sell our investments to our affiliates. Investment transactions with our affiliates include an investment in Prodigy Communications Corporation, or Prodigy (which we sold to an affiliate of SBC International in November 2001), an investment in The Telvista Company and the sale of our subsidiary Kb/Tel. Our transactions with affiliates may create the potential for conflicts of interest.

Holders of L Shares and L Share ADSs Have Limited Voting Rights, and Holders of ADSs May Vote Only Through the Depositary

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 Mexican National Banking and Securities Commission 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 Depositary

Under Mexican law, a shareholder is required to deposit its shares with a Mexican custodian in order to attend a shareholders' meeting. A holder of ADSs will not be able to meet this requirement, and accordingly is not entitled to attend shareholders' meetings. A holder of ADSs is entitled to instruct the depositary as to how to vote the shares represented by ADSs, in accordance with procedures provided for in the deposit agreements, but a holder of ADSs will not be able to vote its shares directly at a shareholders' meeting or to appoint a proxy to do so.

You May Not Be Entitled to Participate in Future Preemptive Rights Offerings

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. 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 depositary to sell preemptive rights and distribute the proceeds from such sales to ADS holders.

Our Bylaws Restrict Transfers of Shares in Some Circumstances

Our bylaws provide that any acquisition or transfer 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 or transfer more than 10% of our capital stock, you will not be able to do so without the approval of the Board of Directors.

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 it may have, including any rights under the U.S. securities laws, with respect to its investment in Telmex. If you invoke such governmental protection in violation of this agreement, your shares could be forfeited to the Mexican government.

Our Bylaws May Only Be Enforced in Mexico

Our bylaws provide that legal actions relating to the execution, interpretation or performance of the bylaws may be brought only in Mexican courts. As a result, it may be difficult for non-Mexican shareholders to enforce their shareholder rights pursuant to the bylaws.

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 their assets 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.

Risks Relating to Developments in Mexico and Other Emerging Market Countries

Economic and Political Developments in Mexico May Adversely Affect Our Business

Our principal business operations and assets are located in Mexico. As a result, our business may be significantly affected by the general condition of the Mexican economy, by devaluation of the peso, by inflation and high interest rates in Mexico, or by political developments in Mexico.

Mexico Has Experienced Adverse Economic Conditions

Mexico experienced a severe economic crisis following the devaluation of the peso in December 1994. In recent years, economic crises in Asia, Russia, Brazil and other emerging markets have adversely affected the Mexican economy and could do so again. In 2000, Mexico's gross domestic product, or GDP, growth was 6.9%, and inflation was 8.9%. In 2001, GDP decreased 0.3%, as a result of the U.S. recession, while inflation declined to 4.4%. The Mexican government has estimated that GDP growth in 2002 is expected to be 1.7% and inflation is expected to be 4.5%. This estimate may not prove to be accurate. Economic conditions in Mexico are heavily influenced by conditions in the United States. If the U.S. economy does not recover, Mexican economic growth will be adversely affected.

If the Mexican economy falls into a recession 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.

Depreciation or Fluctuation of the Peso Relative to the U.S. Dollar Could Adversely Affect Our Financial Condition and Results of Operations

Primarily because of our U.S. dollar-denominated indebtedness, we are affected by fluctuations in the value of the peso against the U.S. dollar. In 2001, the peso appreciated against the U.S. dollar by 4.8% at year-end, and the average value of the peso against the U.S. dollar during 2001 was 1.7% higher than in 2000. In 2000, the peso depreciated slightly against the U.S. dollar at year-end, but the average value of the peso against the U.S. dollar during 2000 was 1.0% higher than in 1999. In 1999, the peso appreciated against the U.S. dollar at year end by approximately 3.5%, but the average value of the peso against the U.S. dollar during 1999 was 3.6% lower than in 1998. Any future depreciation or devaluation of the peso may result in further net foreign exchange losses.

Severe devaluation or depreciation of the peso may also result in disruption of the international foreign exchange markets and may limit our ability to transfer or to convert pesos into U.S. dollars and other currencies for the purpose of making timely payments of interest and principal on our indebtedness. While the Mexican government does not currently restrict, and for many years has not restricted, the right or ability of Mexican or foreign persons or entities to convert pesos into U.S. dollars or to transfer other currencies out of Mexico, the government could institute restrictive exchange rate policies in the future. Currency fluctuations will probably continue to affect our financial income and expense and our revenues from international settlements.

High Levels of Inflation and High Interest Rates in Mexico Could Adversely Affect Our Financial Condition and Results of Operations

Mexico has experienced high levels of inflation and high domestic interest rates. The annual rate of inflation, as measured by changes in the National Consumer Price Index, was 4.4% for 2001. Inflation for the first quarter of 2002 was 1.4%. If inflation in Mexico does not remain within the government's projections, we might not be able to raise our rates to keep pace with inflation, and more generally the adverse effects of high inflation on the Mexican economy might result in lower demand or lower growth in demand for telecommunications services. Interest rates on 28-day Mexican treasury bills, or *Cetes*, averaged 11.3% during 2001. On May 29, 2002, the 28-day *Cetes* rate was 6.98%. High interest rates in Mexico could adversely affect our financing costs.

Political Events in Mexico Could Affect Mexican Economic Policy and Our Operations

The national elections held in July 2000 ended 71 years of rule by the Institutional Revolutionary Party ("PRI") with the election of president Vicente Fox, a member of the National Action Party ("PAN"), and resulted in the increased representation of opposition parties in the Mexican Congress and in mayoral and gubernatorial positions. Neither the PRI nor the PAN currently has a majority in the Congress or Senate. Although there have not yet been any material adverse repercussions resulting from this political change, multiparty rule is still relatively new in Mexico and could result in economic or political conditions that could materially and adversely affect our operations. The lack of a majority party in the legislature and the lack of alignment between the legislature and the President could result in deadlock and prevent the timely implementation of economic reforms, which in turn could have a material adverse effect on the Mexican economy and on our business.

Developments in Other Emerging Market Countries May Adversely Affect Our Business or the Market Price of Our Securities

The market value of securities of Mexican companies is, to varying degrees, affected by economic and market conditions in other emerging market countries. Although economic conditions in such countries may differ significantly from economic conditions in Mexico, investors' reactions to developments in any of these other countries may have an adverse effect on the market value of securities of Mexican issuers. In late October 1997, prices of both Mexican debt securities and Mexican equity securities dropped substantially, precipitated by a sharp drop in value of Asian markets. Similarly, in the second half of 1998, prices of Mexican securities were adversely affected by the economic crises in Russia and in Brazil. The current economic crisis in Argentina could adversely affect the Mexican economy and the value of Mexican securities. If Argentina's economic environment does not improve, the Mexican economy could experience slower growth than in recent years. There can be no assurance that the market value of our securities would not be adversely affected by events elsewhere, especially in emerging market countries.

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, institutional investors, representatives of the media and others. Examples of such forward-looking statements include:

- projections of operating revenues, net income (loss), net income (loss) per share, capital expenditures, dividends, capital structure or other financial items or ratios,

- statements of our plans, objectives or goals, including those relating to competition, regulation and rates,

- statements about our future economic performance or that of Mexico or other countries, and

- statements of assumptions underlying such statements.

Words such as “believe,” “anticipate,” “plan,” “expect,” “intend,” “target,” “estimate,” “project,” “predict,” “forecast,” “guideline,” “should” and similar expressions are 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 “Risk Factors” beginning on page 4, include economic and political conditions and government policies in Mexico or elsewhere, inflation rates, exchange rates, regulatory developments, technological improvements, customer demand and competition. 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. You should not expect that, just because we have made a forward-looking statement, we will update it in light of new information or new developments.

Item 4. Information on the Company

TELMEX

We own and operate the largest telecommunications system in Mexico. We are the only nationwide provider of fixed-line telephony services and the leading provider of fixed local and long distance telephone services as well as Internet access in Mexico. We also provide other telecommunications and telecommunications-related services such as directory services, data transmission, Internet connectivity, paging service and interconnection services to other carriers.

At March 31, 2002, we had 13.6 million local fixed lines in service, up 9.9% over March 31, 2001. In long distance services, we estimate that in 2001 our share of traffic was 68% for domestic long distance and 59% for international long distance.

Of our consolidated revenues in 2001, 47.2% was attributable to local service, 34.2% was attributable to long distance service and 13.3% was attributable to interconnection. Included in long distance revenues are revenues from data transmission services, which represented 10.3% of total revenues. Other services, including yellow pages and equipment sales, accounted for 5.3% of consolidated revenues.

History

We were formed in 1947 under private foreign ownership to acquire the Mexican telephone business of a wholly-owned subsidiary of the L.M. 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 government sold shares representing voting control of our company. The government sold the balance of its shares in a series of transactions beginning in May 1991.

In September 2000, we spun off our Mexican wireless business and, with limited exceptions, our international operations into América Móvil, a new Mexican corporation. The spin-off was conducted by means of the procedure under Mexican corporate law called *escisión*. The spin-off was completed on February 7, 2001, when shares and ADSs of América Móvil started trading separately from our shares and ADSs on the Mexican Stock Exchange, the New York Stock Exchange and NASDAQ.

In the years since our privatization, we have evolved from a state-owned commodity business to a fully integrated private-sector service provider. Consumption of telephone services has grown rapidly as we modernized our equipment, rebuilt our external infrastructure, optimized our network architecture, digitalized our local and long distance switches and built a fully redundant nationwide fiber optic network. We have expanded both the volume and scope of our services, to reach 25,638 communities and provide a range of services from the most essential voice communications to products where voice, data and video converge.

Business Strategy

We operate primarily in the Mexican markets for wireline voice telecommunications, Internet and data businesses. We expect that these markets will see continuing growth in demand, increasingly intense competition and growing diversification of service offerings, particularly if the Mexican economy recovers. We expect that any decline in our market share as a result of increasing competition will be at least partly offset by the overall growth in the market. We think our strengths under these conditions include the following:

- our strong competitive position in the Mexican markets for fixed voice telephony and Internet and data businesses, with nationwide coverage, the largest market share and strong brand recognition;

- our ability to offer integrated telecommunications solutions throughout Mexico;

- the size and technological sophistication of our network infrastructure, which includes Mexico's largest fiber optic network;

- our strong financial position and stable cashflows; and

- our deep and experienced management team, which benefits from the strength of our leading shareholders Carso Global Telecom and SBC International, Inc.

We intend to maintain our leadership in traditional wireline voice telecommunications and to take advantage of the potential for growth in data transmission and Internet-related businesses in Mexico. To this end, our business strategy highlights the following:

- We are focusing on improving customer service by anticipating and fulfilling customer needs in distinctive sectors, including large corporations, medium-sized businesses, entrepreneurs and home-based businesses. To address the needs of our business clients, we have developed improved billing systems tailored to particular categories of customers and we are reducing delivery times for new services.

- For our residential clients, we have tailored our products and services to meet customer needs. We implemented the "Prodigy Plus" program to provide personal computers together with introductory Internet access. In 2001, we introduced bandwidth expansions as part of our Prodigy line, including Prodigy Turbo (ISDN) and Prodigy Infinitum (ADSL). We have emphasized enhanced digital services such as caller ID, call waiting, three-way calling, call forwarding and voice mail. For our lower income customers, we provide extensive prepaid offerings, including the launch of the "Multifon" prepaid card in 2001 and "Multifon Home" (*Multifon Hogar*) prepaid service in 2002.

- While building on our core voice communications business with its strong penetration and brand recognition, we are promoting our ability to provide integrated value-added services, including data transmission, advanced data services, hosting of data processing functions, e-commerce support, customer premises equipment and tailored business solutions for particular industries.

- We are continuing to expand our nationwide fiber optic network, which currently extends over 70,000 kilometers, including full redundancy, and links areas with 99% of Mexico's population.

- In equal partnership with Microsoft, we developed the T1MSN portal, one of Mexico's most frequently visited Internet sites in 2000. In September 2001, T1MSN acquired Yupi, a popular Spanish-language portal.

- We are implementing a transition in network design toward what we call the next generation network, or NGN. During the transition, we intend to gradually integrate our separate service infrastructures and management systems under a common infrastructure with multi-service nodes that have the capacity to provide voice, data, Internet and video services. The NGN will allow us to improve flexibility in offering services and increase efficiency in network management.

Significant Subsidiaries

The following table sets forth our significant subsidiaries at December 31, 2001:

Name of Company	Jurisdiction of Establishment	Percentage Owned	Description
Compañía de Teléfonos y Bienes Raíces, S.A. de C.V.	Mexico	100.0	Real estate company owning our facilities
Alquiladora de Casas, S.A. de C.V.	Mexico	100.0	Real estate company owning our facilities
Teléfonos del Noroeste, S.A. de C.V., or Telnor	Mexico	100.0	Fixed-line network concessionaire for two states in northwestern Mexico
Anuncios en Directorios, S.A. de C.V.	Mexico	100.0	Producer of yellow pages directories
Uninet, S.A. de C.V.	Mexico	100.0	Provider of Internet access to Telmex and commercial customers
Consorcio Red Uno, S.A. de C.V.	Mexico	100.0	Supplier of telecommunications network integration services and information systems
Telmex USA, L.L.C.	Delaware	100.0	Authorized reseller of domestic and international long distance services in the United States
T1MSN Corporation	Delaware	50.0	Joint venture with Microsoft to establish an Internet portal for the Spanish-speaking Americas

Overview

The following table gives selected data on the size and usage of our network, excluding the wireless operations that were spun-off to América Móvil in September 2000:

	December 31,				
	2001	**2000**	**1999**	**1998**	**1997**
Lines in service (thousands)	13,372	12,069	10,878	9,927	9,254
Internet access accounts (thousands)	913	634	403	146	34
Data transmission line equivalents (thousands)	1,574	997	507	371	224
Percentage of lines connected to digital exchanges	100.0	100.0	99.6	97.7	90.1
Lines in service per employee	272.8	247.4	222.7	202.4	187.2
Domestic long distance call minutes for the year (millions)	14,251	12,309	10,419	9,077	8,232
International long distance call minutes for the year (millions)(1)	4,404	5,521	4,192	3,286	3,768

(1) Includes incoming and outgoing traffic.

In 2000, the Mexican government recognized our technological strength by awarding us the National Technology Award for outstanding use and management of technological resources as well as for improvement in products, services and processes to benefit customers. In 2002, Forbes magazine named us the best telecommunications company in the world for 2001 in its annual review of the financial and growth performance of companies with sales or market capitalization of at least U.S.$5 billion.

Local Service

There were 13.4 million local fixed lines in service at December 31, 2001. Lines in service grew 10.8% in 2001, reflecting 1,917 thousand new lines and 615 thousand disconnections. Growth in lines can be affected by economic conditions. For example, in 1996, the economic crisis in Mexico adversely affected growth in lines, with 475 thousand new lines and 450 thousand disconnections.

In November 2000, we finished implementing the modernized Mexican numbering plan adopted by Cofetel, which provides more local numbers and accommodates the introduction of competition in local services. Since then we have consolidated certain local service areas under a consolidation plan agreed with Cofetel, increasing the size of the local area for customers in certain regions and reducing the number of local service areas from approximately 2,200 to approximately 406 by June 2002.

Our network is 100% digital, with all of our lines connected to digital exchanges. During 2001, customers made increasing use of digital services, such as caller ID, call waiting, three-way calling, call forwarding and voice mail. The number of lines with digital services in use at year-end 2001 was 3.2 million, an increase of 55.5% from 2000. At December 31, 2001, 24.0% of lines had at least one digital service.

We provide local telephone service to 25,638 communities throughout Mexico. Lines in service are concentrated in large urban areas. Of all lines in service, 37.8% are in the Mexico City, Monterrey and Guadalajara areas, and 26.0% are in the Mexico City area alone. We provide service to 14,748 rural communities, exceeding our obligations under the Concession to extend services to rural areas.

Our charges for fixed-line local telephone service comprise (a) installation charges, (b) monthly line rental charges, (c) monthly measured service charges, and (d) charges for other services, such as the transfer of a line to another address and reconnection. Residential customers pay a fixed charge per local call in excess of a monthly allowance of 100 local calls, and commercial customers pay for every local call at the same fixed rate per call. During 2001, approximately 51.5% of residential customers made fewer than 100 local calls per month. The Concession permits, but does not require, us to base our charges on the duration of each call, with a monthly allowance of free calls or call minutes for residential customers. We currently do not charge by duration of invoiced calls in any region, but may do so in the future.

We offer pre-paid local and long distance service through our "Ladatel" and "Multifon" calling cards. Multifon cards may be used with Ladatel public phones, Ladafon home-installed phones and with invoiced fixed-line phones. Beginning with the March 2002 launch of "*Multifon Hogar*" (Multifon Home), we offer prepaid local and long distance service from home telephones. This service, aimed at low-income customers and customers with delinquent accounts, offers an alternative to monthly invoices for fixed-line phones.

In November 2001, we announced that we would not increase rates during 2002. In March 2001, we increased our monthly rental charges for residential customers by 6.5% and monthly measured service charges for all customers by 6.4%. On October 1, 2000, we increased our local service rates by 6.1%, with the exception of commercial installation fees. During 1999, we increased all our local service rates by 4.1% on March 10 and 4.1% on July 1, with the exception of commercial installation charges. Rate increases are described in this paragraph in nominal terms, without taking account of inflation.

We hold frequency concessions acquired at auctions in October 1997 and 1998. We use the frequencies primarily for long distance transmission and to provide fixed-wireless services where the local loop is not available.

Long Distance Service

We are the leading provider of domestic and international long distance telecommunications services in Mexico. Our domestic long distance transmission network consists of more than 70,000 kilometers of optical fiber connecting Mexico's major cities, and includes secondary branches and an additional transmission ring around Mexico City designed to mitigate network congestion. International long distance traffic with the United States, Canada, Central America and other countries is carried by a combination of the fiber optic network, microwave transmission, satellite systems and submarine cable. See "—Network."

Our charges for domestic long distance service are based on call duration and the type of service, e.g., direct-dial or operator-assisted. Charges for international long distance calls are based on type of service, call duration and the region of the world called. We do not expect to increase our nominal rates for domestic and international long distance service in 2002. Our nominal rates for domestic and international long distance service remained unchanged in 2000 and 2001. Basic rates increased by 14.2% in nominal terms in March 1999 for traffic to the United States and Canada.

We offer a variety of long distance discount plans that reduce the effective rates paid by our customers based on volume, time of use or other factors. For domestic long distance service, beginning in 2000, high volume corporate clients pay P.1.00 per minute, which represents a discount of up to 61.2% from our nominal rate, while other customers that maintain service with us receive a 12% discount, as well as a 50% discount on calls made between 8:00 p.m. and 7:59 a.m. from Monday to Saturday and all day Sunday. For international long distance service, customers receive a 33.3% discount on calls made to the United States and Canada between 7:00 p.m. and 6:59 a.m. from Monday to Friday, all day Saturday, and between 12:00 a.m. and 4:59 p.m. on Sunday.

Revenues from international long distance service include net payments under bilateral agreements with foreign carriers. The agreements govern the rates of our payment to foreign carriers for completing international calls from Mexico and by foreign carriers to us for completing international calls to Mexico. The rates of payment under such agreements are negotiated with each foreign carrier. Settlements among carriers are normally made monthly on a net basis. Settlement amounts payable to us in respect of calls from the United States to Mexico generally exceed amounts payable by us in respect of calls from Mexico to the United States. As a result, we receive monthly net settlement payments from U.S. carriers. We make monthly settlement payments to other international carriers taken as a whole.

The international settlement rates that U.S. carriers pay to foreign carriers have been subject to intense downward pressure due to competition and regulatory factors, including initiatives by the United States. We and certain U.S. carriers were unable to agree on settlement rates for 1998 and beyond until the first half of 1999, when we agreed to a weighted average settlement rate per minute of U.S.$0.370 for 1998, U.S.$0.250 for January through June of 1999 and U.S.$0.190 for July 1999 through 2000. In May 2001, we reached an agreement with subsidiaries of WorldCom, Inc. (collectively, WorldCom), and subsequently with certain other U.S. carriers, to reduce settlement rates for 2001 by 18.4% from U.S.$0.19 per minute to U.S.$0.155 for 2001. The agreement established further rate reductions to U.S.$0.135 for 2002 and U.S.$0.10 for 2003. The companies also agreed to urge the respective Mexican and U.S. regulatory authorities to modify the applicable regulations to permit market-based rates beginning on January 1, 2004, including the elimination as of that date of the requirements that (i) all carriers pay the same rates, (ii) incoming international calls be distributed among the Mexican carriers in proportion to the outgoing calls they originate and (iii) the Mexican carrier with the largest market share on a particular international route negotiate rates for all Mexican carriers on that route. Cofetel approved the agreement in June 2001. The U.S. carriers submitted the agreement to the U.S. Federal Communications Commission, or FCC, which has not taken action.

In February 2002, we agreed with WorldCom to further reduce settlement rates for the period from March 2002 through December 2003. Under the new agreement, rates for northbound (Mexico to the United States) and southbound (the United States to Mexico) traffic will no longer be in parity. All northbound calls will be settled at U.S.$0.055 per minute. Settlement rates for southbound calls will be based on a three-tiered rate structure that varies depending on the termination point of international calls and assigns lower rates for calls terminating in Mexican regions with the heaviest telephone traffic. Specifically, the agreement sets a settlement rate of U.S.$0.055 per minute for calls terminating in Mexico’s three largest cities (Mexico City, Guadalajara and Monterrey), U.S.$0.085 for calls terminating in the next 200 largest cities and U.S.$0.1175 for calls terminating anywhere else in Mexico. In March and April 2002, we entered into agreements setting these rates with all of the other U.S. carriers with which we correspond.

In the 2002 agreements, we also reaffirmed the commitment to request that the relevant regulatory authorities modify the applicable regulations to permit the implementation of market-based termination rates by January 1, 2004. In March 2002, we submitted the proposed agreements to Cofetel for approval. The U.S. carriers also submitted the terms of the agreements to the FCC for approval.

We believe that our international traffic volume has been adversely affected by an unauthorized practice in Mexico referred to as "illegal bypass," in which incoming international calls are carried over leased lines and then connected to the public switched network in Mexico, thus avoiding settlement payments. Illegal bypass is technically difficult to prevent or to measure, but we believe that illegal bypass was primarily responsible for the decline in the number of minutes of international long distance traffic from 1997 to 1998, and that the growth of illegal bypass was reduced in 1999 and in 2000 by the reduction in settlement and interconnection rates. In December 2000, we agreed with the two leading competing long distance carriers on a package of measures to eliminate illegal bypass. Despite these efforts, we estimate that in 2001 illegal bypass deprived us of approximately P.1,699 million, equivalent to 18% of our long distance revenues. In the WTO proceeding, the United States contends that Mexico is required to permit U.S. companies to route their calls into and out of Mexico over leased lines. There can be no assurance that our international traffic volume and our results of operations will not continue to be adversely affected by unauthorized bypass.

Public Telephony

We have several programs to meet the need for different kinds of public telephone service in different areas. We had 708 thousand fixed public telephones in operation at December 31, 2001. In order to expand coverage to more remote areas of Mexico, we have extended our rural public telephone infrastructure and established programs such as "Put Your Telephone to Work" and line sharing. At December 31, 2001, public telephone service to remote areas was provided through 200 thousand public phones, an increase of 56.3% over year-end 2000. Use of public telephones, including rural public telephones, accounted for 10.2% of our consolidated revenues in 2001.

In 2001, we sold over 268 million prepaid cards under the brand names "Ladatel" and "Multifon" for use in public telephones, an increase of 4.7% over 2000. We introduced the "Multifon" prepaid calling card that also may be used with Ladatel public phones in May 2001. We also are installing Internet kiosks in public places so that our customers have access to Internet products and services by using Ladatel cards.

In 1999, we introduced "Ladafon" shared telephone service, under which a line is available for public use by the residents of multi-unit dwellings, who pay based on usage. This system has allowed us to accommodate the practice of sharing residential lines.

In the increasingly competitive market to provide telecommunications services, independent operators have begun to install public telephones, for which we provide access. There were 12 thousand independently operated public telephones at December 31, 2001.

Internet, Data Transmission and Other Services

We believe that we are the leading Internet access provider in Mexico in terms of the number of subscribers. We had 913 thousand customers at December 31, 2001, an increase of 44.0% from year-end 2000. By March 31, 2002, the number of Internet service subscribers was 986 thousand. Much of the growth in this segment is attributable to the Prodigy Internet Plus package we launched in June 1999, which for a fixed price provides a customer with a multi-media personal computer, a personal web page, an e-mail account and two years of unlimited access time. This program accounted for 277 thousand subscribers in 2001, or 21.3% of the net new subscribers for the year.

At the beginning of 2002, we launched the Telmex National Connectivity Project (e-Telmex) with the goal of rapidly increasing the number of areas in Mexico with access to voice and broadband data services over the course of 18 months. At the core of this project are Community Digital Centers designed to offer voice and high-speed Internet services as well as carry out educational, health and economic development functions.

Of particular note in 2001 were bandwidth expansions introduced as part of our Prodigy line, including Prodigy Turbo (ISDN) and Prodigy Infinitum (ADSL). These services allow our customers to handle larger bandwidth, making it possible for them to use our high-capacity data transmission services with applications such as video-conferencing, file transfer, terminals, e-mail and protocol conversion.

During 2001, the number of line equivalents provided by means of private data transmission increased by 57.8% to 1,574 thousand, and revenue from data transmission was P.11,405 million, representing 10.3% of our consolidated revenues. We also supply telecommunications network integration services and information systems through our wholly-owned subsidiary Red Uno.

In March 2000, we launched T1MSN, an Internet portal aimed at the Spanish-speaking Americas. T1MSN is a 50-50 joint venture between us and Microsoft Corporation. T1MSN takes advantage of Microsoft’s world-class technologies and our leading infrastructure, operations and regional knowledge to offer users a broad range of communication services and superior content in Spanish, such as easy and secure shopping services and enhanced communication features. In September 2001, T1MSN acquired Yupi, an operator of a popular Spanish-language portal that targets Internet users in the United States and in certain Latin American countries. At December 31, 2001, T1MSN had 6.4 million unique users per month in Mexico and 9.8 million users per month in the rest of Latin America and the United States. Total page views reached 6.268 billion during 2001.

Through TRIARA, our Internet data center dedicated to providing infrastructure services for Internet developments, we provide several hosting, co-location and outsourcing services in Mexico, offering our corporate customers significant savings in the computer infrastructure and telecommunications investments necessary to have a Web site or carry out high-performance Internet projects. Initiatives like TRIARA provide platforms through which we serve other segments of the data business market, such as small and medium-sized businesses.

We also operate a web-based service called Eficentrum, which is a horizontal business-to-business market for the indirect exchange of goods and services. Eficentrum’s business plan emphasizes economies of scale, administrative savings, better purchasing management, fast payment, expeditious delivery services and direct contact with manufacturers. The current volume of transactions has made Eficentrum the biggest horizontal portal in Mexico. We plan to implement other new e-commerce initiatives in different market sectors, thereby continuing to broaden our range of services to the corporate sector.

We provide various other telecommunications and telecommunications-related services, including yellow pages and other directory services. We have introduced a number of new services that will permit us to meet new customer demands. These include: services based on digital technology, such as caller ID, call waiting, speed calling and automatic redialing and value-added services; public telephones providing such services as credit card and debit card operations; direct connections to foreign operators; terminal equipment; and software for data transmission, video conferencing and voice mail. We also provide air-to-ground phone service in conjunction with GTE.

Interconnection

In accordance with the Federal Telecommunications Law, we provide interconnection service pursuant to which (a) long distance, local and cellular carriers operating in Mexico establish points of interconnection between their networks and our network and (b) we carry calls between the points of interconnection and our customers. When a customer of another carrier calls a local service customer of ours, we complete the call by carrying the call from the point of interconnection to the particular customer, and when a local service customer of ours who has preselected a competing long distance carrier makes a long distance call, we carry the call from the customer to the point of interconnection with the relevant carrier's network.

We charge a variety of fees for interconnecting different categories of carriers and different types of calls. Our revenues from interconnection represented 13.3% of our consolidated revenues in 2001. Revenues from our customers under the "calling party pays" system for calls from fixed lines to mobile lines represented 90.5% of our interconnection revenues in 2001. We pay 73.3% of the amounts received under the "calling party pays" system to the cellular carriers whose customers receive calls from our customers.

Interconnection fees, and interconnection practices more generally, have been the focus of controversy among competing long distance carriers in Mexico as in many other countries. Such carriers have contended that the technical and financial terms of interconnection are unfair to them, and they have responded with a variety of measures, including the following: seeking action from Cofetel and other Mexican governmental and regulatory agencies; enlisting the support of foreign governments, including the U.S. government, in seeking action from Cofetel and other Mexican agencies; opposing our applications for licenses from the U.S. Federal Communications Commission; commencing proceedings in Mexican courts; publicizing their grievances; and withholding payment of interconnection fees due to us. Beginning in December 2000 and again in December 2001, we reached agreements with competing long distance carriers that address many of the disputes over interconnection. See "Regulation—Interconnection."

Network

Our network includes installed telephones and switchboards, a network of exchanges, access lines connecting customers to exchanges, trunk lines connecting exchanges and long distance transmission equipment. Our technologically advanced, high-capacity and high-speed fiber optic network, the largest in Mexico, extends over 70,000 kilometers, has connections via submarine cables with 39 countries and connects most major cities throughout Mexico.

Fiber optic cable provides the capability to transmit both voice and high bandwidth applications such as video and image data. The network is fully redundant and is supported by 11 fiber-optic ground rings, an intercontinental submarine segment known as Columbus II and a submarine cable system known as Maya 1, all of which feature automatic restoration capacity in 50 milliseconds. In addition, our digital microwave network serves as a secondary backup to the optical fiber network and as a primary means of transmission for rural areas and small towns, where optical fiber is not available. Our network has been constructed with a uniform integrated network architecture, using wave-length digital multiplexing (WDM) technology, resulting in a highly reliable and resilient network that operates at speeds up to 60 Gbps. We have completed the digitalization of our switching and transmission network infrastructure, designed to support a wide variety of services with a high level of quality and availability.

International long distance traffic with the United States and Canada is carried by the fiber optic network. Traffic with Central America (except Guatemala) is carried by microwave transmission. Traffic with other countries is carried by the Intelsat and Inmarsat satellite systems and by submarine cable. We are a partner in the 12,200-kilometer submarine cable Columbus II, which links the Americas and Continental Europe. We also participate in 30 submarine cables for transmission of traffic with Europe, Asia and Australia. On September 20, 2000, we inaugurated the Maya 1 submarine cable system that joins North, Central and South America with state-of-the-art technology and will increase international communications transmission quality and capacity throughout the region. The Maya 1 submarine cable has permitted us to meet rising traffic demands and continue growth while we broaden our services to other countries.

Core Network

Our core network has been constructed to allow transmission using synchronous digital hierarchy (SDH) technology over a series of connected rings. The rings give us the ability to transmit information from the origin to the destination simultaneously in both directions around the rings, which minimizes the risk of interruption of the signal in the event of damage to our network. With this structure we are able to achieve total end-to-end network availability with restoration times of less than 50 milliseconds.

We coordinate and monitor our network equipment performance and traffic levels and manage the routing of traffic, the loading of switches and other network functions through centralized network management. The single centralized management of our SDH network facilitates geographical expansion of the network and permits the exploitation of higher capacity system as required. SDH provides a platform for future information, communications and entertainment services. SDH is also well suited to operate asynchronous transfer mode (ATM) technology, which is required for advanced data transmission.

Traffic on our network is directed by both voice and data switches. Switches are essential for routing information from one point to another. The SDH technology used in the network gives flexibility in the geographic siting of switches and enables us to handle more traffic with fewer switches than a traditional network. In addition, switched network traffic can be re-routed over the SDH network to avoid congestion in periods of heavy usage.

Next Generation Network

In the face of new challenges arising from telecommunication globalization and technology growth, we are evolving our current infrastructure to a Next Generation Network. During this transition, we intend to gradually integrate our separate service infrastructures and management systems under a common infrastructure with multiservice nodes which have the capacity to provide voice, data and video services. This is achieved by integrating separate service infrastructures, such as Internet protocol (IP), cellular, intelligent network, data and paging, through multiservice nodes using SDH and dense wave division multiplexing (DWDM) technologies. The NGN will allow us to improve flexibility in offering services and increase efficiency in managing our network.

The successful installation of the NGN depends on the expansion of IP-oriented services, such as data and voice virtual private networks (VPNs). To this end, we have upgraded our data network with IP technology and are continuing the build-out of our ATM backbone. ATM permits data, text, voice and multimedia signals to be transmitted simultaneously between network access points at speeds up to 150 Mbps. By utilizing the ATM technology, we can provide superior local access network interconnection, data transmission and flexible bandwidth delivery. In launching the NGN, we will also utilize packet switching technology, which permits more efficient creation of multiservice networks based on standard formats to carry information.

Billing and Customer Service

For corporate customers, we offer SI@NA, an Internet service that permits customers to analyze their telecommunications spending. Residential customers may also access billing information over the Internet using the "Telmex on-line" *(Telmex en Línea)* service. Since 1998, we have been providing our customers with a bill format that details their local service usage.

We provide customer service through a network of customer service centers and call centers. These customer service centers have evolved from their traditional purpose as places for payment to become Telmex stores that offer telecommunications products and services. Large corporate customers also receive customer service from dedicated customer service personnel. Through our "Integrated Solutions" *(Solución Integral)* service, we assist corporate customers in meeting their telecommunications needs by providing them with integrated telecommunications solutions consisting of a broad range of telecommunications services. In 1998, our Corporate Market Service Center obtained ISO 9002 certification. We offer service level agreements to corporate customers that set service standards and guarantee continuity of service. In 1999, we introduced services using ISDN technology.

Competition

The Mexican market for fixed-line domestic and international long distance services was opened to competition beginning in 1996. Twenty-one carriers have been granted licenses to provide long distance service in Mexico, nine of which have commenced operations. Alestra (a joint venture led by Alfa, S.A. de C.V., Grupo Financiero BBVA Bancomer, S.A. de C.V., and AT&T Corp.) and Avantel (a joint venture led by Grupo Financiero Banamex and WorldCom, Inc.) have made the most substantial investments in infrastructure and marketing. Most competing carriers have been principally focused on the long distance market, although some carriers also provide certain business customers with direct access to their long distance networks using lines leased from us. In addition to granting concessions to new competitors, the Communications Ministry has established technical rules and basic access rates for interconnection between us and our competitors. We expect our market share in domestic and international long distance services to decline as a result of intensified competition.

Customers are free to choose a competing carrier at any time. Customers can also access the long distance carrier of their choice by dialing a toll-free number, which permits the carrier to bill the customer directly. An independent organization confirms all requests to change long distance carriers. In addition to pre-subscription, customers will eventually be able to select a long distance carrier on a call-by-call basis by dialing a three-digit prefix. In general, our competitors have focused their attention on obtaining market share in Mexico's most profitable markets, such as the major cities and high-volume users of international and domestic long distance.

The Mexican market for fixed-line local services was opened to competition in late 1997. As of December 31, 2001, 17 carriers have been granted licenses to provide local fixed wire and wireless telephony and 10 carriers have been granted licenses for cellular and mobile telephony. At present, there are 10 competitive local operators, primarily in Mexico City and other large cities (Axtel, Pegaso, Maxcom, Unefon and Megacable are our principal fixed-line competitors). We expect greater competition in this segment from companies that are currently long distance operators (Avantel, Alestra and Miditel) and from cellular operators with PCS and fixed wireless frequencies. To date, our competitors in local service have focused on servicing first-time customers or new housing and not on inducing our customers to switch carriers. We estimate that our market share in local service (including cellular) at year-end 2001 was 36.6%.

The competitive environment in Mexico has become the subject of controversy and of attention from Mexican regulators and from abroad. In particular, the Mexican Competition Commission has determined that we are a dominant provider of certain telecommunications services, and Mexican law provides for the regulatory authorities to impose additional regulations on a dominant provider. In September 2000, Cofetel adopted specific regulations applicable to us as a dominant carrier. See "Regulation—Dominant Carrier Regulations." In July 2001, in response to a withdrawn December 1995 claim by a competitor, the Competition Commission ruled that we had engaged in anti-competitive practices. In October 2001, the Competition Commission ruled that we had engaged in discriminatory practices in connection with the sale of private lines to Internet service providers.

In August 2000, the United States initiated WTO dispute settlement against Mexico regarding alleged illegal barriers to competition in the Mexican telecommunications market. The allegations related to our status as a "dominant" telecommunications provider in Mexico and the interconnection fees and charging mechanisms for international calls. The United States declined to proceed with a WTO dispute settlement panel, but on April 2, 2001, the United States Trade Representative announced that if sufficient progress was not made to resolve the dispute by June 1, 2001, the United States would renew its request for a dispute settlement panel at the WTO. The United States took no action on June 1, 2001, however.

On February 13, 2002, the United States requested the WTO to establish a panel to address claims that Mexico has not complied with its WTO commitments because it has failed to ensure that (i) we provide international termination to U.S. telecommunications carriers at "cost-based" and "reasonable" rates and (ii) U.S. companies can route their calls into and out of Mexico over leased lines. Consistent with its standard procedures, on April 17, 2002, the WTO established the dispute settlement panel requested by the United States. We expect that it will take the panel at least one year to resolve the dispute, and panel decisions are then subject to appeal to the WTO. While we believe that the claims made by the United States are politically motivated and incorrect, an adverse decision by the panel could lead to trade sanctions against Mexico and could prompt changes in regulation affecting our business.

In December 2000, we entered into agreements with our two principal long distance competitors, Avantel and Alestra, that addressed a variety of outstanding issues. In 2001, our remaining long distance competitors agreed to the same terms and conditions we had previously agreed upon with Alestra and Avantel. The agreements confirm the parties' acceptance of interconnection rates imposed by Cofetel for long distance calls, resolving previous disputes over rates and providing for the payment of outstanding unpaid fees by each party. We received U.S.$139.0 million (net of tax) in cash in the fourth quarter of 2000 as a result of the settlement. The agreements also establish pricing and quality standards for the provision of services between us and the other carriers, requiring us to provide discounts and establishing mechanisms to monitor compliance. We agreed to submit to Cofetel proposals to eliminate illegal bypass and to modify the allocation of incoming international calls. The parties also agreed to withdraw their outstanding legal proceedings relating to the matters in dispute. The agreements do not address the dominant carrier regulations adopted by Cofetel.

In December 2001, we entered into agreements with all our long distance competitors regarding the interconnection rates for 2002 and additional discounts for interconnection facilities and call attempts. We also reached agreements with our competitors regarding discounts on private lines and on other services.

The effects of competition on us depend, in part, on the business strategies of competitors, the general economic and business climate in Mexico, including demand growth, interest rates, inflation and exchange rates, and regulatory developments. The effects could include loss of market share and pressure to reduce rates. We believe that our strategies to meet competition will continue to help limit our loss of market share and that any loss of market share will be at least partly offset by increasing demand.

We estimate our market share in long distance service to be 66.7%, measured on the basis of total number of billed minutes generated by our local customers making domestic and international long distance calls. Our market share in Internet access is estimated to be 53%, measured on the basis of the total number of Internet access accounts in Mexico. We believe that, at present, competitors do not have a material share of the market for fixed-line local service, but we expect that this will change as the number of competitors grows and their market strategies develop. In local service, we also face competition from cellular carriers, which we believe had a combined total of 21.8 million cellular lines in service at year-end 2001. We estimate that our market share in local service (including cellular) at year-end 2001 was 36.6%.

Investments and Joint Ventures

We occasionally make investments and joint ventures in telecommunications-related businesses within and outside Mexico. The aggregated cost of such investment in 2001 was U.S.$83 million. We also invest in publicly-traded equity securities of companies in technology and communications businesses. As of December 31, 2001, we had P.700 million of marketable securities on our balance sheet. Our marketable securities are carried at market value, and gains and losses are recognized in our statement of income.

Until November 2001, we owned 17.7% of the common stock of Prodigy Communications Corporation, one of the largest providers of Internet access in the United States. We sold the interest in November 2001 for U.S.$82.6 million. We retain the right to use the Prodigy name in Mexico.

In January 2002, we and certain partnerships affiliated with Forstmann Little & Co. entered into a stock purchase agreement with XO Communications, Inc., a financially-troubled U.S. competitive telecommunications service provider, under which we and Forstmann Little each agreed to pay U.S.$400 million to XO in exchange for common stock representing approximately 40% of the outstanding shares of XO after giving effect to a financial restructuring. Our agreement with XO is subject to a number of conditions, including a financial restructuring of XO that achieves the capital structure specified in the agreement, regulatory approvals and a number of other conditions. In June 2002, XO filed a voluntary petition for bankruptcy under Chapter 11 of the U.S. Bankruptcy Code. Prior to the bankruptcy filing, we and Forstmann Little informed XO that we believed that it was "virtually impossible" for the conditions to our obligations under the agreement to be satisfied, that we would not waive any of these conditions and requested that XO agree with us to mutually terminate the agreement. XO rejected this request and has proposed a plan of reorganization with the bankruptcy court that proposes consummation of the investment contemplated by our agreement or, alternatively, a "stand-alone" plan that does not require additional equity investment in XO. As we indicated to XO prior to its bankruptcy filing, the plan of reorganization proposed by XO is not acceptable to us, which we believe provides a basis for us to refuse to consummate the investment in accordance with the terms of the proposed plan of reorganization.

We may expand our presence in telecommunications outside Mexico, especially in the United States and in Latin America, through selective investments and strategic alliances. There can be no assurance as to the extent, timing or cost of future international investments.

Property

We have transmission facilities, exchanges, outside plant and commercial and administrative offices throughout Mexico. We own most of the locations of our exchanges and offices and lease other locations. We hold a small number of operating properties under financial leases, but the aggregate amount of such financing is not material to our operations as a whole. We carry casualty insurance against loss or damage to buildings and equipment contained in buildings and do not carry insurance against most other risks.

We have purchased equipment from a variety of suppliers, and there are sufficient alternative sources of equipment so that interruption of any source would be unlikely to cause a significant disturbance to our operations or our investment plan.

The Telmex Foundation

Since 1996, we have sponsored an independent philanthropic foundation called Fundación Telmex, S.C., or the Telmex Foundation, that is active in the areas of education, health, justice and culture. During 2001, the Telmex Foundation provided nearly 9,000 scholarships to students studying for over 700 different careers in over 700 private and public educational institutions. The Foundation also supported 14 scholar houses in Mexico, each of which provides residents with computer services, Internet access, videoconferencing capabilities and libraries to enhance the professional development of all scholarship holders.

The Telmex Foundation expanded its efforts in conjunction with Mexican government health agencies in providing specialized health care to people in remote areas through a surgery program that funded treatment for over 14,000 patients in 2001. In 2001, the Foundation started a program in conjunction with the Children's Hospital to distribute nutritional supplements to approximately 450,000 children in low-income families. In cooperation with non-governmental organizations, the Foundation provided assistance to 6,267 persons charged with minor crimes whose lack of financial resources prevented them from otherwise posting bail.

CAPITAL EXPENDITURES

The following table sets forth, in constant pesos as of December 31, 2001, our capital expenditures, before retirements, for each year in the three-year period ended December 31, 2001, restated in years 2000 and 1999 to reflect the spin-off of América Móvil:

	Year ended December 31,		
	2001	**2000**	**1999**
	(in millions of pesos)		
Exchanges and power	P. 4,087	P. 4,852	P. 4,181
Telephone equipment.	578	549	372
Outside plant	6,815	5,149	2,575
Transmission	7,991	4,802	1,130
Land and buildings	1,053	684	462
Miscellaneous	1,814	2,735	1,944
Investment in affiliates, subsidiaries and other	472	1,804	2,133
Total capital expenditures	P. 22,810	P. 20,575	P. 12,797

We have budgeted capital expenditures in an amount equivalent to approximately U.S.$1.2 billion for the year 2002, although this amount may be reduced during the year. Our budgeted capital expenditures exclude the proposed U.S.$400 million investment in XO Communications and any other investments in other companies.

REGULATION

Our business is subject to comprehensive regulation and oversight by the Communications Ministry and Cofetel. The Communications Ministry is part of the executive branch of the Mexican federal government, and Cofetel is an agency of the Communications Ministry. Regulation and oversight are governed by the *Ley de Vias Generales de Comunicación* (the Law of General Means of Communication, or the General Communications Law), the Telecommunications Regulations adopted under such law, the Federal Telecommunications Law, the Concession and other concessions and license agreements granted by the Communications Ministry.

Set forth below is a summary of certain provisions of the General Communications Law, the Federal Telecommunications Law, the Telecommunications Regulations and our Concession.

General

The General Communications Law, the Federal Telecommunications Law and the Telecommunications Regulations provide the general legal framework for the regulation of telecommunications services in Mexico. The Federal Telecommunications Law replaced most of the provisions of the General Communications Law relating to telephone communications, but those provisions of the General Communications Law not specifically addressed in the Federal Telecommunications Law, such as rules governing local and long distance carriers, remain in effect. Regulations implementing particular provisions of the Federal Telecommunications Law have been issued by the Communications Ministry or Cofetel. Regulations implementing other provisions of the Federal Telecommunications Law are pending. The objectives of the Federal Telecommunications Law are to promote the efficient development of the telecommunications industry, to encourage fair competition in the provision of quality, low-priced services and to assure satisfactory breadth of coverage of the Mexican population.

In October 2001, the Mexican Congress announced the beginning of a process to reform the Federal Telecommunications Law. Some of the proposals that have been discussed, such as strengthening the regulatory power of Cofetel, stimulating increased investment in telecommunications and increasing competition, could have a material effect on our operations. We are unable to predict whether or when such amendments may be implemented and, if implemented, their effect on our business.

Regulatory Oversight

The Communications Ministry is the Mexican government agency principally responsible for regulating telecommunications services. The Ministry's approval is required for any change in our bylaws. It also has broad powers to monitor our compliance with the Concession and it may revoke our Concession or temporarily seize or expropriate our assets. The Ministry may require us to supply it with such technical, administrative and financial information as it may request. We are also required to publish our annual network expansion program, and we must advise the Ministry of the progress of our expansion and modernization program on a quarterly basis.

The Federal Telecommunications Law provided for the establishment of an administrative agency, Cofetel, to regulate the telecommunications industry. Cofetel commenced operations in August 1996. It is an independent agency within the Communications Ministry, with four commissioners appointed by the Communications Ministry on behalf of the President of Mexico, one of whom is appointed as chairman. Many of the powers and obligations of the Communications Ministry under the Federal Telecommunications Law and the Telecommunications Regulations have been delegated to Cofetel.

Mexican law gives certain rights to the government in its relations with concessionaires and provides that we may not sell or transfer any of our assets unless we give the government a right of first refusal. If the government declines to exercise its right, our unions also have a right of first refusal. In addition, Mexican law permits the government to expropriate our assets in certain circumstances.

Concessions

Under the Federal Telecommunications Law and the Telecommunications Regulations, a provider of public telecommunications services must operate under a concession granted by the Communications Ministry. Such a concession may not be transferred or assigned without the approval of the Communications Ministry. A concession to provide public fixed-network long distance services has a term for up to 30 years and may be extended for additional 30-year terms. We hold a concession to operate a public network for basic telephone services (the Concession), which was granted in 1976 and amended in August 1990, and will expire in 2026. Our subsidiary Telnor holds a separate concession in two states in northwestern Mexico, which will expire in 2026. The material terms of the Telnor concession are essentially the same as the Concession.

Operators of private networks that do not use electro-magnetic frequencies are not required to obtain a concession to provide private telecommunications services but are required to obtain approval from the Communications Ministry.

In addition to the Concession, we currently hold concessions for the use of frequencies to provide wireless local access and point-to-point and point-to-multipoint transmission, which we obtained from Cofetel through a competitive bidding process. These concessions are granted for a term up to 20 years and may be extended for additional 20-year terms.

Termination of the Concession

The Concession provides that it will remain in force until 2026, and that we may renew it for an additional 15 years subject to additional requirements the Communications Ministry may impose. Thereafter, it may be renewed for successive 30-year terms as provided under the Federal Telecommunications Law.

The Concession provides that upon its expiration the government is entitled to purchase our telecommunications assets at a price determined on the basis of an appraisal by a public official, and the Telecommunications Regulations provide that upon expiration of the Concession the government has a right of first refusal to acquire our telecommunications assets. The General Communications Law, however, provides that upon expiration of the Concession our telecommunications assets will revert to the government free of charge. There is substantial doubt as to whether the provisions of the Concession and the Telecommunications Regulations would prevail, and accordingly there can be no assurance that upon expiration of the Concession our telecommunications assets would not revert to the government free of charge.

The General Communications Law and the Concession include various provisions under which the Concession may be terminated before its scheduled expiration date. Under the General Communications Law, the Communications Ministry may cause early termination of the Concession in certain cases, including:

- failure to expand telephone services at the rate specified in the Concession;
- interruption of all or a material part of the services provided by us;

- transfer or assignment without Ministry approval of the Concession or any asset used to provide telephone service;
- violation of the prohibition against ownership of our shares by foreign states;
- any material modification of the nature of our services without prior Ministry approval, and
- breach of certain other obligations under the General Communications Law.

In addition, the Concession provides for early termination by the Communications Ministry following administrative proceedings in the event of:

- a material and continuing violation of any of the conditions set forth in the Concession;
- material failure to meet any of the service expansion requirements under the Concession;
- material failure to meet any of the requirements under the Concession for improvement in the quality of service;
- engagement in any telecommunications business not authorized under the Concession and requiring prior approval of the Communications Ministry;
- following notice and a cure period, failure without just cause to allow other concessionaires to interconnect their telephone networks to our telephone network; or
- our bankruptcy.

The General Communications Law provides that in the event of early termination of the Concession for specified causes, including violation of the prohibition on ownership of our shares by foreign states, we would forfeit all of our telecommunications assets to the government. In the event of early termination of the Concession for any other cause, the General Communications Law provides that a portion of our telecommunications assets would revert to the government free of charge, and that we may be required to dismantle the remaining portion. There is substantial doubt as to whether the provisions of the Concession and the Telecommunications Regulations regarding the consequences of expiration of the Concession would apply to mitigate the provisions of the General Communications Law in the event of early termination.

Dominant Carrier Regulations

The Federal Telecommunications Law provides that if a company is determined to be dominant in a relevant market, the Communications Ministry has the power to adopt specific regulations on rates, quality of service and information provided by a dominant provider. In February 1998, the Mexican Competition Commission issued a resolution confirming its determination that we are a dominant carrier in the following markets: (1) local telephone service, (2) access service, (3) inter-urban transport, (4) domestic long distance service, and (5) international long distance service.

In September 2000, Cofetel adopted specific regulations, which we refer to as the dominant carrier regulations, applicable to us as a dominant carrier. They apply to the five markets identified by the Competition Commission in 1998, and also to certain other services, including directory assistance, operator services and billing and collection services. The dominant carrier regulations impose standards for the quality of our services, and require that we prepare and provide specific information and specific tariff regulations. We have complied with the regulations on quality of services and on information, and we believe we will be able to continue doing so without significant cost or competitive impact.

The most significant elements of the dominant carrier regulations are three specific rules on tariffs.

- First, our prices for covered services must always exceed a floor price based on "total average costs." The Concession says our price for any service must exceed the "average incremental cost," and while the methodology for determining total average costs is not clear, it will presumably result in a higher floor price for the services to which it applies.

- Second, the regulations prohibit any rate or rate package that reduces our operating margin in a competitive market, except as a defensive response to competitors' rates that present a risk of substantial loss of market share.

- Third, prices for services (other than interconnection) that we provide to other carriers will, for the first time, be subject to prior approval of Cofetel.

It is difficult to assess the impact these regulations would have on tariffs or competition, in part because neither the methodologies nor the procedures are fully specified. We believe, however, that if they are implemented the new substantive rules and the related regulatory procedures will to at least some degree reduce our flexibility to adopt competitive tariff policies.

After the Competition Commission issued the February 1998 resolution, we commenced constitutional proceedings in the Mexican Federal courts challenging the validity of the resolution, and we commenced a proceeding in the Mexican federal courts challenging the validity of the dominant carrier regulations. We asserted that they constitute a unilateral amendment of the terms of our Concession, which we believe is not permitted under the Mexican constitution or the terms of the Concession itself. We also asserted that the determination that we are a dominant carrier, on which Cofetel's power to issue these regulations is predicated, is flawed because the Competition Commission made its determinations in 1997 in reliance on earlier findings that are now out of date, and because its determinations did not extend to all the markets covered by the dominant carrier regulations. Finally, we objected to the specific tariff regulations imposed by the dominant carrier regulations on a variety of grounds—including that they gave Cofetel excessive discretion, that they would unfairly burden competition and that they did not adequately permit us to recover our investments in infrastructure.

Following several appeals, the February 1998 resolution of the Competition Commission was held unconstitutional in May 2001. It is our assertion that all subsequent rulings by government agencies (including Cofetel) which relied upon the 1998 Resolution are also unconstitutional. We filed petitions to have dominant carrier regulations based on the 1998 Resolution declared unconstitutional, and in May 2002, several resolutions issued by the Competition Commission and Cofetel were nullified, including the September 2000 resolution adopting the dominant carrier regulations.

In May 2001, the Competition Commission issued a new resolution with the same terms as the February 1998 resolution in which it concluded that we are a dominant carrier in the same five markets. This resolution was affirmed by the Commission following an appeal, and in September 2001, we commenced constitutional proceedings in the Mexican federal courts challenging the validity of this new resolution.

Rates

The General Communications Law, the Federal Telecommunications Law and the Telecommunications Regulations provide that the basis for setting rates of a telecommunications concessionaire is set forth in its concession.

Under the Concession, our rates in any period for basic telephone services, including installation, monthly rent, measured local service and long distance service, are subject to a ceiling on the price of a "basket" of such services weighted to reflect the volume of each service provided by us during the preceding period. Within this aggregate price cap, we are free to determine the structure of our own rates. In addition to the price cap, however, the dominant carrier regulations impose floor prices for certain services and restrict our ability to lower prices in competitive markets. See "—Dominant Carrier Regulations." We must publish our rates and register them with Cofetel before they may take effect.

The price cap varies directly with the Mexican National Consumer Price Index, permitting us to raise nominal rates to keep pace with inflation, subject to consultation with the Communications Ministry. For the past several years, we have not raised our nominal rates to the full extent that would be permitted to keep pace with inflation. Under the Concession, the price cap is also adjusted downward periodically to pass on the benefits of increased productivity to our customers. The Concession fixed the adjustment for 1998 and 1999 at 0.74% per quarter in nominal terms, and requires the Communications Ministry to set a new periodic adjustment for every four-year period, beginning 1999-2002, so as to permit us to maintain an internal rate of return equal to our weighted average cost of capital. In March 1999, the Communications Ministry fixed the adjustment for 1999-2002 at 1.11% per quarter in nominal terms. We do not expect the price cap to have a material adverse impact on our revenues or our pricing policies, which are increasingly driven by competition.

For services extending beyond basic telephone service, under the Concession we are permitted to set our prices free of rate regulation. These services include private circuits, directory services and services based on digital technology such as caller ID, call waiting, speed calling, automatic redialing, three party calling and call forwarding. We are required to register the types, but not the rates, of new value-added services.

Expansion and Modernization Requirements

The Concession imposes a number of requirements for expansion and modernization of our telephone system. Most of these requirements were met by the end of 1994 and the remaining requirements were met by the end of 1998, including the requirement to reduce the maximum waiting period for new service in cities with automatic exchanges to one month by the year 2000.

Service Quality Requirements

The Concession also sets forth extensive goals for the quality and continuity of our service, including reductions in line failures, reductions in repair time, reductions in the time required to obtain dial tone, improvements in the percentage of calls completed on the first attempt and reductions in installation time. We are required to provide rebates to our customers if we fail to meet certain of the standards for quality of service set forth in the Concession. We have not been required to make any material general rebates since 1994. The dominant carrier regulations also impose specific service quality requirements in particular markets and specifically require that we provide services to our competitors at equal or better standards than those we provide to our customers. We have objected to this requirement in the proceeding we filed challenging the validity of the dominant carrier regulations. See "—Dominant Carrier Regulations."

Competition

The Telecommunications Regulations and the Concession contain various provisions designed to introduce competition in the provision of communications services. In general, the Communications Ministry is authorized to grant concessions to other parties for the provision of any of the services provided by us under the Concession. On August 10, 1996, the Communications Ministry opened to competition the Mexican market for fixed-line domestic and international long distance telephone services. There are currently nine competing long distance carriers operating in Mexico. In 1998, the Communications Ministry began granting licenses to competing local service carriers. See "Telmex—Competition." Concessions are not required to operate certain private local telecommunications networks or to provide value-added services, although other authorizations may be required.

The Communications Ministry released in June 1996 rules governing long distance services, together with basic technical plans for numbering and for signaling that address a number of technical issues including several relating to the commencement of competition in long distance services. The long distance rules establish the general framework for competitive long distance services, including rules regarding customer selection of carriers, allocation of service-related liabilities, subscription, billing and collection. They also provide for certain consultation and information-sharing mechanisms among service providers and with the Communications Ministry.

The Federal Telecommunications Law provides that the Communications Ministry may authorize resellers of long distance telecommunications services, but no regulations have been adopted implementing that provision of the law. The Communications Ministry may grant permits to long distance resellers in the future, and the impact on our operations and revenues is uncertain.

In December 1996, Cofetel issued rules governing international long distance services, covering matters such as international interconnection and mechanisms for routing calls into and out of Mexico. International traffic must be carried by Mexican concessionaires and through authorized international gateways consistent with the Cofetel's international long distance rules, and international long distance carriers must route traffic in and out of Mexico using uniform settlement rates negotiated with foreign carriers.

Incoming international calls are distributed among the Mexican carriers in proportion to the settlement fees paid in connection with outgoing international traffic originated by each of them. In May 2001, we agreed with WorldCom to urge the respective Mexican and U.S. regulatory authorities to modify the applicable regulations to permit the negotiation of market-based rates beginning on January 1, 2004. In Mexico, these regulatory modifications would include, among others, the elimination of requirements that (i) all carriers pay the same rates, (ii) incoming international calls be distributed among the Mexican carriers in proportion to the outgoing calls they originate and (iii) the Mexican carrier with the largest market share on a particular international route negotiate rates for all Mexican carriers on that route. We believe that these agreements may resolve some of the conflicts with respect to settlement rates.

In early 2002, we agreed to further settlement rate reductions with all of our U.S. carriers. The agreement provides for a three-tiered settlement rate based on the termination point of calls originating in the United States, and assigns the lowest rate to calls to the three most densely populated cities in Mexico. In the agreement, we reaffirmed our commitment to implement market-based rates beginning on January 1, 2004 and to request that the relevant authorities undertake the regulatory modifications necessary to implement the agreement. In March 2002, we submitted the proposed agreement to the Mexican authorities for approval and requested that they implement the necessary modifications to Mexico's rules. We cannot yet predict the effects of any modification of the current proportionate return system on our financial performance or on our competitive situation. We have sought Cofetel's approval of the agreement and the U.S. carriers have submitted the agreement to the U.S. Federal Communications Commission for approval.

The competitive environment in Mexico has been the subject of controversy and of attention from Mexican regulators and abroad. In September 2000, Cofetel adopted specific regulations applicable to us as a dominant carrier. The United States has initiated WTO dispute settlement regarding alleged illegal barriers to competition in the Mexican telecommunications market and its claims will be addressed by a WTO dispute panel. The United States claims that Mexico has failed to ensure that (i) we provide international termination to U.S. telecommunications carriers at "cost-based" and "reasonable" rates and (ii) U.S. companies can route their calls into and out of Mexico over leased lines. We cannot predict the outcome of the WTO proceeding or the impact of an adverse result on our business. An adverse decision by the panel could lead to trade sanctions against Mexico and could prompt changes in regulation affecting our business. In the specific area of domestic interconnection, there has been extensive litigation, but agreements reached in December 2000 and December 2001 may reduce the level of controversy. See "Telmex—Dominant Carrier Regulations," "Telmex—Interconnection," and "Telmex—Competition."

Interconnection

Since January 1, 1997, we have been required under the Federal Telecommunications Law to permit any other long distance concessionaire to connect to our network in a manner that enables customers to choose the network by which their long distance calls are carried. The Communications Ministry issued the technical rules for the interconnection of competing long distance carriers with our network in July 1994, specifying that there would be an unlimited number of long distance concessions and that we had to provide interconnection points in 60 cities by December 1997 and in over 200 cities by the year 2000. We have fulfilled these requirements. In addition, in 1997, Cofetel issued rules governing the interconnection rights and obligations of local service concessionaires. The rules require local service concessionaires to provide interconnection on a nondiscriminatory basis to any other concessionaire.

In June 1997, Cofetel ruled that we are entitled to recover certain costs of modifying our network to accommodate interconnection, by collecting a specific additional fee from all long distance carriers including ourselves over a period of seven years. The costs will be allocated among carriers pursuant to specific allocation mechanisms for each category of cost. One carrier commenced legal proceedings against the government in connection with the recovery of our interconnection investments. Pending resolution of these proceedings, none of the carriers paid the additional fee.

The Concession provides that other terms of interconnection, including fees, are to be negotiated between us and each other long distance carrier, and that, in the event the parties are unable to agree, the Communications Ministry may impose terms on us and the other carriers. We and our competitors had generally been unable to agree on interconnection rates, and accordingly Cofetel imposed rates.

The interconnection fees imposed by Cofetel have been the subject of numerous legal challenges. We have also brought proceedings contesting our obligation to renew the existing service agreements with competing carriers based on the new interconnection tariffs, on the grounds that the carriers have not honored the current agreements.

In December 2000, we reached an agreement with the two leading competing long distance carriers that addressed many of the outstanding disputes over interconnection. We agreed to the fixed tariff of U.S.$0.0125 per minute for interconnection of domestic long distance calls to the local network, which had been imposed by Cofetel in October 2000. We agreed on a variety of technical issues relating to interconnection and a mechanism for the recovery of our investment in modifying our network to accommodate interconnection, by charging a supplemental interconnection fee to all long distance carriers including ourselves. The parties also agreed to withdraw their outstanding legal proceedings relating to interconnection, and they settled and paid all disputed amounts owing between them, which related primarily to interconnection fees. As a consequence of our agreements with other long distance carriers, all prior legal disputes regarding interconnection rates have been dismissed and all disputed amounts have been paid.

In December 2001, we agreed with the two leading competing long distance carriers to reduce the interconnection rate to U.S.$0.00975 per minute and per interconnection point for 2002, with an additional discount of 15% for interconnection facilities and of 50% for call attempts. We also agreed to significant discounts on private lines and on other services. The remaining long distance carriers entered into agreements with us on the same terms in early 2002. The new rate represents a decrease of 22% compared with the prior rate and is lower than the average international rate. Mutual discounts were also negotiated up to 45% below the best market rate offered to the public in local and long-distance private interconnection links and 45% below the price of co-location registered with Cofetel.

Item 5. Operating and Financial Review and Prospects

The following discussion should be read in conjunction with the consolidated financial statements and notes thereto included in this Annual Report. The businesses we transferred to América Móvil in the spin-off are treated as discontinued operations. Except where we specify otherwise, the discussion below concerns only our continuing operations and not those we spun off.

Our consolidated financial statements have been prepared in accordance with Mexican GAAP, which differ in certain important respects from U.S. GAAP. Note 18 to our audited consolidated financial statements provides a description of the principal differences between Mexican GAAP and U.S. GAAP, as they relate to us; a reconciliation to U.S. GAAP of operating income, net income and total stockholders' equity; and a condensed statement of cash flows under U.S. GAAP.

Mexican GAAP requires that the financial statements recognize certain effects of inflation. In particular,

- nonmonetary assets (including plant, property and equipment) and stockholders' equity are restated for inflation and, in the case of imported telephone plant, as described below,
- gains and losses in purchasing power from holding monetary liabilities or assets are recognized in income, and
- all financial statements are restated in constant pesos as of December 31, 2001.

Since January 1, 1997, we have restated plant, property and equipment of non-Mexican origin based on the rate of inflation in the country of origin and the prevailing exchange rate at the balance sheet date; other fixed assets are restated based on the Mexican National Consumer Price Index. We have not reversed the effect of inflation accounting under Mexican GAAP in the reconciliation to U.S. GAAP of our net income and stockholders' equity, except with respect to the methodology for restatement of plant, property and equipment of non-Mexican origin. See Note 18 to the consolidated financial statements.

Results of Operations

Our operating revenues are derived principally from local, long distance and interconnection services. Revenues from Internet and data transmission are included in the revenues for long distance services. We also obtain revenues from leased private lines, equipment sales and telephone-related services such as directory services.

The principal factors affecting our revenues from local and long distance services have been rates and the volume of usage of telephone services. In addition, our financial statements have been restated in constant pesos and accordingly, the effect of rates on revenues is analyzed in terms of constant pesos as of December 31, 2001. Unless nominal rates increase by at least the rate of inflation, real rates will decline over time.

Our results of operations have been affected by changes in our rate structure, the impact of competition in long distance services and continued growth in demand for all service except international long distance. Growing demand and the expansion of our network have resulted in growth in lines in service and increasing domestic long distance traffic. International long distance traffic rose in 2000, but decreased in 2001. For both domestic and international long distance service, prices have fallen steadily as real rates have fallen and customer discounts have increased. Growth in cellular telecommunications and the introduction of "calling party pays" have also greatly increased our interconnection revenues and expenses.

These changes have led to a change in the composition of our operating income. Of 2001 consolidated operating income, 65.3% was attributable to local service, and 21.4% was attributable to long distance service. For 2000, the comparable percentages were 73.6% local service and 15.7% long distance service. Operating income for each segment reflects inter-segment operations, and consolidated operating income also includes other activities, adjustments and eliminations. These changes have also resulted in a disparity in operating margins between the different categories of service. See Note 17 to our consolidated financial statements. The effects of competition have been extensive, and have included lower market share and competitive pressure on prices for long distance services. We believe we are well positioned to continue meeting competition in long distance services, but we cannot assure you as to the effect of competition on our results of operations and financial condition.

Our results of operations will also continue to be affected by the state of the Mexican economy. In periods of slow economic growth, such as occurred in 1995 and 1996, demand for telecommunications services tends to be adversely affected. The slowdown of the U.S. economy in 2001 affected our results of operations, as reflected in the significant decrease in calls originating in the United States and Canada. Economic conditions, and particularly unemployment and high domestic interest rates, can also result in an increase in the allowance for doubtful accounts. In 2000 and 2001, our growth in terms of lines and minutes of traffic was satisfactory, with the exception of a contraction in the long distance segment in 2001. Though we face increasing competition, our results of operations were buoyed by the strong performance of the Mexican economy during 2000 and by steady Mexican consumption during 2001 despite negative GDP growth. However, we cannot assure you that Mexican economic conditions will not have adverse effects in the future on our financial condition and results of operations. Devaluation of the peso, such as occurred most recently in the second half of 1998, also results in exchange losses on our foreign-currency denominated indebtedness.

Summary of Operating Income

In the table below we set forth our operating revenues, operating costs and expenses and operating income for each of the years in the three-year period ended December 31, 2001, and express each amount as a percentage of total operating revenues.

	Year ended December 31,					
	2001		2000		1999	
	(millions of pesos)	(percentage of operating revenue)	(millions of pesos)	(percentage of operating revenue)	(millions of pesos)	(percentage of operating revenues)
Operating revenues:						
Local service	P. 52,420	47.2%	P. 49,292	46.3%	P. 48,364	49.9%
Domestic long distance service	28,503	25.7	26,737	25.1	24,187	25.0
International long distance service	9,422	8.5	11,873	11.1	13,125	13.5
Interconnection service	14,708	13.3	13,079	12.3	6,069	6.3
Other	5,914	5.3	5,576	5.2	5,135	5.3
Total operating revenues	110,967	100.0	106,557	100.0	96,880	100.0
Operating costs and expenses:						
Cost of sales and services	24,169	21.8	23,026	21.6	20,146	20.8
Commercial, administrative and general	17,138	15.4	17,228	16.2	16,636	17.2
Interconnection	9,810	8.8	7,179	6.7	2,876	3.0
Depreciation and amortization	17,259	15.6	17,673	16.6	18,490	19.0
Total operating costs and expenses	68,376	61.6	65,106	61.1	58,148	60.0
Operating income	P. 42,591	38.4%	P. 41,451	38.9%	P. 38,732	40.0%

Local Service Revenues

Operating revenues from local service include installation charges for new lines, monthly line rental charges and monthly measured service charges based on the number of calls. These revenues depend on the number of lines in service, the number of new lines installed and the volume of calls. Measured service charges are due from residential customers only for the number of local calls exceeding a specified monthly minimum. Accordingly, revenues from local service for residential customers do not depend solely on usage volume. Operating revenues from local service also include miscellaneous customer charges, principally for reconnecting customers who have moved or whose service has been terminated for failure to pay bills.

Revenues from local service increased by 6.3% in 2001 and by 1.9% in 2000. The increase in 2001 revenues was attributable to (i) growth in the number of lines in service, (ii) revenues from digital services (such as call waiting, call forwarding, three way calling, caller ID and voice mail), (iii) an increase in monthly rents and measured service in April 2001, (iv) payment of supplemental interconnection fees, and (v) an increase in the number of local calls. Growth in lines and traffic were attributable in part to the strength of the Mexican economy in 2000 and to steady consumption in 2001 despite negative GDP growth. During 2001, the ratio of growth in local call traffic to growth in number of lines in service was lower than in past years due to higher market penetration among populations with less disposable income. To promote the use of digital services and maximize the value of new fixed lines, we began a program in June to encourage new residential and commercial customers to subscribe to at least three digital services. Lines with at least one digital service in 2001 increased by 55.5% compared with 2000. The increase in revenues during 2000 was principally due to growth in the number of fixed lines in service and in local traffic, which was partly offset by lower real rates. In 2001, average real rates remained steady because our nominal rate increases of 6.5% of monthly rental charges for residential customers and 6.4% of monthly measured service charges for all customers in March 2001 were offset inflation. Average real rates declined in 2000 because inflation more than offset the effect of nominal increases of 6.1% in October 2000.

Competition in local service, principally from wireless service providers, has begun to develop since the issuance of rules facilitating competition in Mexico's local service market in late 1997. We believe that at present our competitors do not have a material share of the market for fixed-line local service. We expect that this will change as the number of competitors grows and their market strategies develop, but we expect to maintain a strong leadership position.

Domestic Long Distance Revenues

Operating revenues from domestic long distance service depend on rates and traffic volume. Domestic long distance revenues increased by 6.6% in 2001 and by 10.5% in 2000. The increase in both years was due largely to growth in data and Internet businesses and an increase in billed minutes, which were partly offset by lower real rates. In 2001, revenues from our data business grew 10% and revenues from our Internet business grew 47%. The 15.8% growth in billed minutes in 2001 was due to better call completion as a result of network improvements. The 18.1% increase in billed minutes in 2000 was due to the strength of the Mexican economy, the effect of lower real rates and a slight gain in our market share. The growth in billed minutes in both years was offset by lower real rates and the effect of customer discounts. Average real rates were lower in 2001 and 2000 because there were no nominal rate increases in either year.

We expect average real rates for domestic long distance service will continue to decline, and that demand will continue to grow up to a certain point. As a result of competition, our market share may decline, but we cannot predict the effects on our volume of domestic long distance traffic or on our revenues.

International Long Distance Revenues

Operating revenues from international long distance service consist of (a) amounts earned from our customers and (b) amounts earned from foreign telecommunications carriers for terminating international calls to Mexico, which are reported net of amounts payable to foreign carriers for terminating calls from Mexico. The amount of operating revenues from international long distance service depends on the volume of traffic, the rates charged to our customers, the rates charged by each party under agreements with foreign carriers, principally in the United States, and the effects of competition. The contribution of net settlements from foreign carriers represented 2.2% of our consolidated revenues and 25.5% of international long distance revenues in 2001. Settlement payments under service agreements with foreign carriers are generally denominated in U.S. dollars.

International long distance revenues decreased by 20.6% in 2001 and 9.5% in 2000. The decrease in 2001 was primarily due to lower incoming traffic, principally from the United States (which we believe is attributable to the U.S. economic slowdown), a decline in international settlement rates, lower real rates and illegal bypass practices. As a result of illegal bypass practices, we estimate that for 2001, we were deprived of approximately P.1.699 billion in revenues, equal to 18% of our international long distance revenues. The decrease in 2000 was primarily due to a decline in international settlement rates, lower real rates and illegal bypass practices, all of which were partly offset by 31.7% increase in billed minutes. The decline in international settlement rates, from U.S.$0.190 per minute for the year 2000 to U.S.$0.155 for the year 2001, was the result of agreements we reached with certain U.S. carriers. In the last quarter of 2000, international long distance revenues were reduced by a one-time payment of P.239 million to our two principal long distance competitors as payment for outstanding settlement fees. In 1999 we recognized U.S.$131.5 million arising from retroactive payments for international settlements from 1998.

At the beginning of 2002, we reached a new agreement for international settlement rates of calls that end in Mexico for the 2002 and 2003. For Mexico City, Guadalajara and Monterrey, the rate is U.S.$0.055; for the 200 next largest cities in Mexico, the rate is U.S.$0.085; and in the rest of the country the rate is U.S.$0.1175. These rates represent a significant reduction of prior years' rates and could reduce future revenues for international long distance.

Revenues from Interconnection

Revenues from interconnection represent fees from other providers of local, long distance and mobile service for connection to our local network. Under the "calling party pays" system, which replaced the previous "mobile party pays" system in May 1999, our fixed-line customers pay us an interconnection charge when they call mobile customers, and we pay approximately three-quarters of the amount to the mobile carrier that completes the call. We recognize the amount the customer pays us as interconnection revenue, and we recognize the amount we pay to the mobile carrier under cost of sales and services. Revenue from fixed-to-mobile calls represented 76.9% of interconnection revenues in 2001 and 90.5% in 2000. Revenues from competing long distance carriers represented 7.8% of interconnection revenues in 2001 and 18.7% in 2000. The balance of interconnection revenues represents payments from cellular carriers for mobile-to-fixed calls.

Revenues from interconnection increased by 12.5% in 2001 and more than doubled in 2000 (an increase of 115.5%). The increase in 2001 was due to the growth in fixed-to-mobile traffic because of increased cellular lines in service and higher usage rates, which was partly offset by the effect of lower interconnection fees from long distance carriers. The increase in 2000 was attributable to the first full year of operations under the "calling party pays" system.

Our revenues from interconnection may be affected by future reductions in interconnection tariffs. In December 2000 and December 2001, we reached agreements with competing long distance carriers that reduce interconnection tariffs. See "Telmex—Competition" under Item 4. As a result of these agreements and action taken by Cofetel, the interconnection rates we charged long distance carriers in 2001 were 62.1% lower than rates charged in 2000, but we expect that the impact on these reduced rates on revenues will be far outweighed by the effects of growing volume in cellular traffic.

Other Revenues

Other revenues increased by 6.1% in 2001 and by 8.6% in 2000. The largest components of other revenues are sales of telecommunications equipment and accessories and yellow pages advertising. The increases in 2001 and 2000 were principally due to growth in revenues from sales of telecommunication equipment and accessories.

Cost of Sales and Services

Cost of sales and services increased by 5.0% in 2001 and by 14.3% in 2000. The increase in 2001 was primarily due to higher labor costs, increased expenses for maintenance of outside plant, higher costs associated with our purchase of a higher volume of computers for the Prodigy Internet Plus service and higher costs related to equipment and accessories sold. The increase in 2000 was primarily due to higher labor costs related to growth in Internet business and higher cost of services from third parties.

Commercial, Administrative and General Expenses

Commercial, administrative and general expenses decreased by 0.5% in 2001 and increased by 3.6% in 2000. The decrease in 2001 was due primarily to the reduction of promotional expenditures and a smaller charitable contribution to the Telmex Foundation, which was partly offset by an increase in provisions for doubtful accounts and higher labor costs. The increase in 2000 was primarily due to higher labor costs, increasing promotional expenditures due to competition and the costs of introducing new services, all of which were partly offset by a reduction in provisions for doubtful accounts.

Interconnection

We make interconnection payments to cellular operators under "calling party pays." Interconnection costs increased by 36.6% in 2001 and by 149.6% in 2000 due primarily to the increase of cellular service traffic resulting from the growth in the number of cellular users.

Depreciation and Amortization

Depreciation and amortization decreased by 2.3% in 2001 and by 4.4% in 2000. The amount of our depreciable assets has increased every year. Under Mexican GAAP, however, we restate imported fixed assets based in part on the exchange rate between the peso and the currency of the country of origin, and as a result changes in exchange rates affect the amount of depreciation. Depreciation and amortization was lower in both periods because the rate of Mexican inflation exceeded the rate of devaluation, and this effect more than offset the effect of new investments in telephone equipment. In addition, in 2000 we increased the useful lives of certain categories of fixed assets.

Operating Income and Net Income

In the table below we set forth our operating income, comprehensive financing cost and provisions for each of the years in the three-year period ended December 31, 2001.

	Year ended December 31,		
	2001	**2000**	**1999**
	(millions of pesos)		
Operating income	P. 42,591	P. 41,451	P. 38,732
Comprehensive financing cost:			
Interest income	(1,279)	(3,370)	(1,572)
Interest expense	6,997	10,429	11,226
Exchange gain, net	(1,159)	(85)	(1,057)
Monetary gain, net	(2,156)	(3,581)	(5,425)
	2,403	3,393	3,172
Income before income tax and employee profit sharing	40,188	38,058	35,560
Provisions for:			
Income tax	13,279	8,181	8,891
Employee profit sharing	2,985	3,452	2,835
	16,264	11,633	11,726
Income before equity in results of affiliates	23,924	26,425	23,834
Equity in results of affiliates	(430)	(327)	(121)
Income from continuing operations	23,494	26,098	23,713
Income from discontinued operations		1,538	4,870
Net income	P. 23,494	P. 27,636	P. 28,583

In 2001, operating income increased by 2.8%, reflecting higher revenues and a slight decrease in operating margin from 38.9% to 38.4%. The increase in operating income was more than offset by a 62.3% increase in income tax, resulting in a 10.0% decrease in income from continuing operations.

The stability of operating margin reflects a decrease in margin for local service (from 38.5% to 34.8%) and an increase in margin for long-distance service (from 24.1% to 35.9%), because the reduction in interconnection rates paid by long-distance carriers reduced the costs of our long-distance segment and the revenues of our local segment.

In 2000, income from continuing operations increased by 10.1% due primarily to a 7.0% increase in operating income, reflecting higher revenues, which was partly offset by a decrease in operating margin to 38.9% from 40.0% in 1999. The decrease in operating margin reflects a decrease in margin for local service (from 42.2% to 38.5%) and a decrease in margin for long distance (from 32.9% to 24.1%) due to lower real rates as a result of inflation. The introduction of "calling party pays" for mobile service also contributed to the decline in margin. We expect that operating margins will continue to be adversely affected by declining real rates and positively affected by increasing volume. Continuing decreases in long distance interconnection fees will have a positive impact on margin in long distance service and an adverse impact on margin in local service financial statements.

We had a non-recurring gain of approximately P.1,880 million in the fourth quarter of 2000 as a result of our agreement with two long distance competitors in December 2000, as the settlement of outstanding debt resulted in the reversal of part of our allowance for doubtful accounts and the recognition of interest income. See "Telmex—Competition" under Item 4.

In 2000, we began to defer recognition of revenues from the sale of Ladatel cards based on the estimated usage of the cards. The effect was a non-recurring reduction in 2000 net income of P.437 million. The portion attributable to previous years was not material, so we did not restate results for previous years.

Comprehensive Financing Cost

Under Mexican GAAP, comprehensive financing cost reflects interest income, interest expense, foreign exchange gain or loss and the gain or loss attributable to the effects of inflation on monetary liabilities and assets. A substantial proportion of our indebtedness (75.1% at December 31, 2001) is denominated in foreign currencies, so if there is a depreciation of the peso it would result in foreign exchange loss and higher interest expense. Most of our financial assets are denominated in pesos.

Comprehensive financing cost decreased by 29.2% in 2001 and increased by 7.0% in 2000. The changes in each component were as follows:

- Interest income decreased in 2001 by 62.0% due to a lower average level of interest-bearing assets and lower interest rates in Mexico and abroad. Interest income increased in 2000 by 114.4% due to a higher average level of interest-bearing assets.

- Interest expense decreased by 32.9% in 2001 primarily as a result of lower Mexican and foreign interest rates, a lower average level of indebtedness and a higher proportion of indebtedness in foreign currency. Interest expense decreased by 7.1% in 2000 primarily as a result of lower Mexican interest rates, partially offset by a higher average level of indebtedness.

- In each year, the appreciation of the peso against the U.S. dollar resulted in a net exchange gain. The net gain was higher in 2001 than in 2000 primarily due to higher appreciation of the peso in 2001. The net gain was lower in 2000 than 1999 due to a lower rate of appreciation of the peso in 2000.

- In each year, average monetary liabilities exceeded average monetary assets, resulting in a net gain from monetary position. The decrease in both 2001 and 2000 reflected lower rates of inflation.

Income Tax and Employee Profit Sharing

The statutory rate of the Mexican corporate income tax was 35% in 1999, 2000 and 2001. Our effective rate of corporate income tax as a percentage of pretax profit was 25.0% in 1999, 21.5% in 2000 and 33.0% for 2001. Through 2000, the effective rate was below the statutory rate principally because depreciation for tax purposes exceeded depreciation for financial reporting purposes. The effective tax rate was higher in 2001 due to lower depreciation as a result of a change in statutory guidelines for depreciation method.

Like other Mexican companies, we are required by law to pay to our employees, in addition to their agreed compensation and benefits, profit sharing in an aggregate amount equal to 10% of our taxable income (calculated without reference to inflation adjustments). The amount decreased by 13.5% in 2001 and increased by 21.8% in 2000.

Mexican Accounting Principles Bulletin D-4 "Accounting for Income Tax, Asset Tax and Employee Profit Sharing," went into effect on January 1, 2000. The bulletin modifies the rules with respect to the computation of deferred income tax. It generally requires that deferred income tax be determined on virtually all temporary differences in balance sheet accounts for financial and tax reporting purposes, using the enacted income tax rate at the time the financial statements are issued. Through December 31, 1999, deferred income tax was recognized only on temporary differences that were considered to be nonrecurring and that would reverse within a definite period. The bulletin does not significantly affect the accounting for employee profit sharing. The cumulative effect of the adoption of this bulletin at the beginning of 2000 was applied to stockholders' equity, without restating the financial statements for prior years. The effect on our stockholders' equity in 2000 was a reduction of 6.9%.

Equity in Results of Affiliates

Equity in results of affiliates represented a net loss of P.430 million in 2001, P.327 million in 2000 and P.121 million in 1999.

Net Income from Discontinued Operations

Net income from discontinued operations reflects the operations we spun off to América Móvil in 2000 principally our Mexican wireless business. It decreased by 68.4% in 2000, reflecting nine months of operation in 2000 compared to twelve months of operation in 1999 and losses in 2000 in the international businesses that were spun off to América Móvil.

Liquidity and Capital Resources

Our principal capital requirements are for capital expenditures, dividend payments and our share repurchase program. We have generally met these requirements primarily from operating cash flows and limited borrowing. Resources provided by operating activities were P.46,246 million in 2001, P.43,682 million in 2000 and P.40,323 million in 1999, and EBITDA (operating income plus depreciation and amortization) was P.59,850 million in 2001, P.59,124 million in 2000 and P.57,222 million in 1999.

Our capital expenditures were P.22,810 million in 2001, P.20,575 million in 2000 and P.12,797 million in 1999. A principal component of our capital expenditures is telephone plant and equipment, and the higher levels of expenditures in 2001 and 2000 were due to investments in voice and data infrastructure. We anticipate that our capital expenditures will be approximately U.S.$1.2 billion for 2002, although this amount may be reduced during the year. Our budgeted amount excludes the proposed U.S.$400 million investment in XO Communications and any other investments we may have in other companies. For subsequent years, our capital expenditures will depend on the state of the Mexican economy and market conditions.

The amount spent on share repurchases was P.13,715 million in 2001, P.24,841 million in 2000 and P.8,611 million in 1999. The amount spent on share repurchases is determined from time to time by the Executive Committee taking into account factors including the price of our shares and our capital resources. On April 29, 2002, the shareholders approved a new authorization to the Executive Committee to spend up to P.10 billion on share repurchases. The Executive Committee is under no obligation to spend any of that amount. Dividends paid totaled P.6,701 million in 2001, P.7,010 million in 2000 and P.6,865 million in 1999. The shareholders have approved dividends of P.0.56 per share to be paid in four installments out of 2001 income. We expect to pay approximately P.7.3 billion in dividends in 2002.

In the table below we set forth our outstanding contractual obligations as of December 31, 2001, consisting of long-term debt including financial leases and operating leases, and the period in which the contractual obligations come due.

	Payments Due					
	Total	**2002**	**2003**	**2004**	**2005**	**2006 and thereafter**
	(millions of pesos)					
Contractual obligations as of December 31, 2001:						
Long-term debt including financial leases..............	P. 69,742	P. 17,487	P. 8,666	P. 17,858	P. 3,445	P. 22,286
Operating leases................	P. 2,541	P. 587	P. 717	P. 654	P. 484	P. 99

At December 31, 2001, we had total indebtedness of P.69,742 million. Our major categories of indebtedness are as follows:

- U.S. dollar-denominated bank loans. These include large syndicated loan facilities, loans with support from export credit agencies and other loans. Our bank facilities bear interest at specified spreads over LIBOR. The weighted average interest rate at December 31, 2001 was approximately 3.1%. We had U.S.$2,623 million, equivalent to P.23,984 million, in bank loans outstanding at December 31, 2001. Certain of our bank loans contain financial and operating covenants. The most restrictive covenants require us to maintain a consolidated ratio of EBITDA to interest expense of no less than 3.00 to 1 and a consolidated ratio of total debt to EBITDA of no more than 3.75 to 1 (using terms defined in the credit agreements). Compliance with these covenants has not been a significant constraint on our ability to obtain financing.

- U.S. dollar-denominated senior notes. The notes bear interest at 8.25% and mature in 2006. The aggregate principal amount of senior notes is U.S.$1,500 million, which was equivalent to P.13,713 million at December 31, 2001.

- Convertible senior debentures. The convertible debentures bear interest at 4.25% and mature in 2004. The aggregate principal amount is U.S.$1,000 million, which was equivalent to P.9,142 million at December 31, 2001. The debentures are convertible to L Share ADSs (each representing 20 L Shares) at U.S.$29.5770 per ADS, equal to a conversion rate of 33.81 L Share ADSs per U.S.$1,000 principal amount of the convertible debentures. The conversion rate reflects an adjustment implemented in 2001 as a result of the spin-off, based on the fair market value of the América Móvil shares distributed to our shareholders.

- Peso-denominated commercial paper. We regularly sell commercial paper in the Mexican market. This paper is typically sold at a discount with tenors averaging approximately 35 days. At December 31, 2001, we had P.8,675 million in outstanding commercial paper, and the weighted average interest rate was 8.0%. We have reduced our outstanding commercial paper since 2000 (P.26,814 million at December 31, 2000) and have continued to do so in 2002. We do not have committed credit lines on which we can draw if we are unable to roll over commercial paper as it matures. The Mexican commercial paper market is small, and our ability to roll over commercial paper could be limited by market developments as well as by any event that reduces our credit standing. We have reduced our outstanding commercial paper in order to reduce this risk, and we believe that we have sufficient cash and access to new financing to permit us to pay all our commercial paper even if it suddenly became impossible to roll over any commercial paper.

- Peso-denominated senior notes. In October 2001, we issued P.4,250 million in senior notes in the Mexican market, maturing in 2007. In February 2002, we issued an additional P.2,500 million, part of which matures in 2005 and part in 2007. All these notes bear interest at specified spreads over Mexican *Cetes* (short-term government obligations). At December 31, 2001, the interest rate was 11.6%.

We also have smaller amounts of other categories of indebtedness outstanding, including peso-denominated loans from Mexican banks and equipment financing. In past years, a substantial portion of our borrowing consisted of financing for the purchase of equipment, usually arranged through the supplier of equipment. A substantial amount of this financing was incurred in connection with our cellular business and was spun off to América Móvil. At present, we rely primarily on borrowings in the Mexican and international capital markets and from international banks, although this could change if market conditions change. A number of our financing instruments are subject to either acceleration or repurchase at the holder's option if there is a change of control, as defined in the respective instruments. The definitions of change of control vary, but none of them is met so long as Carso Global Telecom or its present controlling shareholders continue to control a majority of our voting stock.

When we spun off América Móvil, we had approximately P.18 billion in outstanding short-term indebtedness held by a subsidiary of América Móvil that was previously held by one of our subsidiaries and eliminated in consolidation. We paid off this commercial paper using proceeds from a U.S.$700 million syndicated bank loan in December 2000 and the issuance of U.S.$1,500 million of senior notes in January and May 2001.

At December 31, 2001, 75.1% of our total indebtedness was denominated in foreign currencies, principally U.S. dollars.

At December 31, 2001, 66.5% of our debt obligations bore interest at floating rates. The weighted average cost of all borrowed funds for 2001 (including interest and reimbursement of certain lenders for Mexican taxes withheld, but excluding fees) was approximately 7.8%. The inclusion of fees in the calculation of weighted average cost of all borrowed funds in 2001 would increase such cost by 0.2% to 8.0%.

Hedging

Because our U.S. dollar-denominated indebtedness far exceeds our U.S. dollar-denominated assets and revenues, we sometimes enter into hedging transactions to protect us to some degree against the risks of devaluation of the Mexican peso. Our hedging policies vary from time to time depending on our judgment about the level of risk and the costs of hedging. Since late 2001, we have been entering into long-term forward exchange and options contracts as hedges against our U.S. dollar-denominated debt. Gains and losses on these transactions are recognized in income as incurred. Such amounts offset gains and losses on the foreign currency liabilities that are hedged. We have been renewing these hedges as they mature. At December 31, 2001, our hedges covered liabilities of U.S.$2,740 million out of our total U.S. dollar-denominated liability of U.S.$5,728 million. In 2001, P.462,557 was charged to income on these contracts to offset exchange differences. See Note 9 to our consolidated financial statements. In 2002, we have continued this practice and increased the proportion of our U.S. dollar exposure that is covered by hedges. Our hedges are short-term and will not protect us against the long-term effects of a devaluation on our U.S. dollar-denominated indebtedness. We may stop hedging or modify our hedging practices at any time.

Substantially all of our peso-denominated indebtedness (P.17,379 million at December 31, 2001) bears interest at floating rates or is short-term. We sometimes engage in hedging transactions to reduce our exposure to changes in Mexican interest rates. During 2002, we have entered into interest-rate swaps in which we pay interest at a fixed rate and receive interest at a floating rate, on a notional amount in Mexican pesos. The general effect of these swaps is to replace an obligation to pay floating-rate interest on our debt with an obligation to pay fixed-rate interest. Because the peso-denominated swap market is not highly liquid, we do not ordinarily obtain interest-rate swaps that precisely match the tenors or amounts of our floating-rate liabilities. From time to time, the aggregate notional amount of our swaps may be greater or less than the principal amount of our floating-rate peso-denominated debt, and we may discontinue hedging at any time.

Contingent Liabilities

We have undertaken contractual commitments to support certain of the subsidiaries and investments that were transferred to América Móvil in the spin-off. We cannot be released from these commitments without the consent of the respective beneficiaries, which has not yet been obtained. We intend to seek the requisite consents to release us from these commitments, but we cannot assure you that the beneficiaries of these commitments will consent or when they will do so. In particular:

- Ownership of a 25% interest in ATL, a Brazilian B-Band cellular concessionaire, was transferred to América Móvil in the spin-off. We have guaranteed indebtedness of ATL under certain credit facilities. Our obligations in this respect are limited to U.S.$104.3 million.

- Ownership of a 17.5% interest in Iberbanda, S.A. (formerly FirstMark Comunicaciones España, S.A.), a broadband wireless company in Spain, was transferred to América Móvil in the spin-off. We have provided a guarantee relating to certain performance obligations of Iberbanda. Our obligations in this respect are limited to 4.6 billion Spanish pesetas (approximately U.S.$25 million at the December 30, 2001 exchange rate).

América Móvil is obligated to indemnify us against any losses, liabilities or expenses arising out of the contingent liabilities described above. We and América Móvil have also agreed that, for each of the undertakings we have given for the benefit of creditors of subsidiaries and affiliates that were transferred to America Móvil, we will use our best efforts to replace them with undertakings of América Móvil or its subsidiaries. See “Related Party Transactions” under Item 7.

U.S. GAAP Reconciliation

Income from continuing operations under U.S. GAAP was P.20,225 million in 2001, P.24,154 million in 2000 and P.22,592 million in 1999. Compared to Mexican GAAP, income from continuing operations under U.S. GAAP was 13.9% lower in 2001, 7.4% lower in 2000 and 4.7% lower in 1999.

There are several differences between Mexican GAAP and U.S. GAAP that affect our net income and stockholders’ equity. The most significant in its effect on net income is the difference in how the carrying value of plant, property and equipment is restated to reflect effects of inflation. Under Mexican GAAP, we restate fixed assets of non-Mexican origin based on the rate of inflation in the country of origin and the prevailing exchange rate at the balance sheet date, while under U.S. GAAP we use the Mexican inflation rate. In recent years, this has resulted in lower net income under U.S. GAAP, because Mexican inflation has exceeded the rate of depreciation of the Mexican peso against foreign currencies, particularly the U.S. dollar.

Other differences that affected net income relate to pension and seniority premium plan costs, interest on assets under construction, and deferred income tax and employee profit sharing. The differences in stockholders’ equity under Mexican GAAP and U.S. GAAP reflect these same matters, and also reflect some matters for which accounting differed in prior years but has since converged. For a discussion of the principal differences between Mexican GAAP and U.S. GAAP, see Note 18 to our consolidated financial statements. Under Mexican Accounting Principles Bulletin D-4, which went into effect on January 1, 2000, our deferred tax accounting under Mexican GAAP is closer to U.S. GAAP than in the past, resulting in a smaller U.S. GAAP difference since 2000.

Use of Estimates in Certain Accounting Policies

In preparing our financial statements, we make estimates concerning a variety of matters. Some of these matters are highly uncertain, and our estimates involve judgments we make based on the information available to us. In the discussion below, we have identified several of these matters for which our financial presentation would be materially affected if either (a) we used different estimates that we could reasonably have used or (b) in the future we change our estimates in response to changes that are reasonably likely to occur.

The discussion addresses only those estimates that we consider most important based on the degree of uncertainty and the likelihood of a material impact if we used a different estimate. There are many other areas in which we use estimates about uncertain matters, but the reasonably likely effect of changed or different estimates is not material to our financial presentation.

Estimated useful lives of plant, property and equipment

We estimate the useful lives of particular classes of plant, property and equipment in order to determine the amount of depreciation expense to be recorded in each period. Depreciation expense is a very significant element of our costs, amounting in 2001 to P.16,753 million, or 24.5% of our operating costs and expenses, under Mexican GAAP, and P.21,152 million, or 27.9% of our operating costs and expenses, under U.S. GAAP. See notes 5 and 18 to our consolidated financial statements.

The estimates are based on historical experience with similar assets, anticipated technological changes and other factors, taking into account the practices of other telecommunications companies. We review estimated useful lives each year to determine whether they should be changed, and at times we have changed them for particular classes of assets. We may shorten the estimated useful life of an asset class in response to technological changes, changes in the market or other developments. This results in increased depreciation expense, and in some cases it can result in our recognizing an impairment charge to reflect a write-down in value. The same kinds of developments can also lead us to lengthen the useful life of an asset class, resulting in reduced depreciation expense.

Employee pensions and seniority premiums

We recognize liabilities on our balance sheet and expenses in our income statement to reflect our obligations to pay employees under defined benefit retirement and seniority premium plans. The amounts we recognize are determined on an actuarial basis, which involves many estimates. In 2001, we recognized net period cost relating to these obligations of P.3,557 million under Mexican GAAP and P.2,979 million under U.S. GAAP.

We use estimates in three specific areas that have a significant effect on these amounts: (a) the real discount rates that we use to calculate the present value of our future obligations, (b) the real rate of increase in salaries that we assume we will observe in future years and (c) the rate of return we assume our pension fund will achieve on its investments. The assumptions we have applied are identified in note 8 (Mexican GAAP) and note 18 (U.S. GAAP) to our consolidated financial statements. These estimates are based on our historical experience, on current conditions in the financial markets and on our judgments about the future development of our salary costs and the financial markets. We review the estimates each year, and if we change them, our reported expense for pension costs may increase or decrease.

In 2000, as a result of the stabilizing long-term outlook for the Mexican economic and political environment, we undertook a comprehensive review of the actuarial assumptions we apply in accounting for our future pension liabilities. The changes in actuarial assumptions resulted, on average, in:

- An increase in the real discount rates that we use to calculate the present value of our future obligations. This reflects better data on long-term rates that have become available due to changes in the financial markets.

- A decrease in the real rate of increase in salaries that we assume we will observe in future years. This reflects the long-term trends in the Mexican and U.S. economies for salaries to decline in real terms, even though since 1996 the positive conditions in the Mexican economy have contributed to real increases in our salaries.

Both of these changes tend to reduce our reserve for future pensions and seniority premiums and also to reduce our net period cost, which is the amount we recognize in income each year for labor obligations. The effect in our balance sheet as of December 31, 2000, was to reduce the projected benefit obligation, the accumulated benefit obligation and the charge to stockholders' equity for labor obligation by approximately P.6,160 million. The effect on the income statement occurred for the first time in 2001, when the changes in actuarial assumptions reduced net period cost by approximately P.1,200 million in 2001 as compared to the cost that would have been determined based on prior actuarial assumptions.

Net period cost and the reserve for future pensions and seniority premiums are also affected over the long term by (i) the difference between estimated and actual annual salary increases, which resulted in a gain of P.2,143 million in 2000 and in a loss of P.4,012 million in 2001 and (ii) the return on investments of our pension fund. As of December 31, 2001, 66% of fund assets consisted of peso-denominated fixed-income securities and 34% consisted of equity securities of Mexican companies.

The fund has experienced volatile returns on its investments in equity securities, which resulted in net losses on plan assets. Our actuarial assumptions as of December 31, 2001 include an assumed return of 6.84% in real terms on plan assets in 2002, based on (a) an assumed return of 15% in nominal terms on the variable income portion of the portfolio, (b) an assumed average return of approximately 10.7% in nominal terms on the fixed-income portion of the portfolio, and (c) an assumed inflation of 5%.

Allowance for doubtful accounts

We maintain an allowance for doubtful accounts based on our estimates of losses we may experience because our customers or other telecommunications carriers do not pay the amounts they owe us. At December 31, 2001, the amount of the allowance was P.1,394 million. For our customers, we perform a statistical analysis based on our past experience, current delinquencies and economic trends. For carriers, we make individual estimates which may reflect our evaluation of pending disputes over amounts owed. Our allowance could prove insufficient if our statistical analysis of our customer receivables is inadequate, or if one or more carriers refuse or are unable to pay us. See note 4 to our consolidated financial statements.

Item 6. Directors and Officers of Registrant

Directors

Management of our business is vested in the Board of Directors. Our bylaws provide for the Board of Directors to consist of at least 5 directors and up to an equal number of alternate directors. A majority of the directors and a majority of the alternate directors must be Mexican nationals and elected by Mexican shareholders. Directors are elected by a majority of the holders of the AA Shares and A Shares voting together, provided that any holder or group of holders of at least 10% of the total AA Shares and A Shares is entitled to name one of such directors and one of such alternate directors, and two directors and two alternate directors are elected by a majority vote of the holders of L Shares. Each alternate director may attend meetings of the Board of Directors and vote in the absence of a corresponding director. Directors and alternate directors are elected at each annual ordinary general meeting of shareholders and each annual ordinary special meeting of holders of L Shares, and each serves until a successor is elected and takes office. Pursuant to our bylaws and Mexican law, at least 25% of our directors and 25% of our alternate directors must be independent, as defined under the Mexican Securities Market Law. In order to have a quorum for a meeting of the Board of Directors, a majority of those present must be Mexican nationals.

Carso Global Telecom and SBC International have agreed to vote for the number of directors and alternate directors named by Carso Global Telecom and SBC International, respectively, in proportion to their respective share ownership.

Our bylaws provide that the members of the Board of Directors are appointed for terms of one year. Pursuant to Mexican law, members of the Board continue in their positions after the expiration of their terms if new members are not appointed. The names and positions of the current members of the Board, as of April 30, 2002, their dates of birth, and information on their principal business activities outside Telmex are as follows:

Carlos Slim Helú Chairman	Born:	1940
	First elected:	1990
	Term expires:	2003
	Principal occupation:	Honorary chairman of the board of directors of Grupo Carso; chairman of the board of directors of Carso Global Telecom and América Telecom
	Other directorships and business experience:	Chairman of the board of directors of América Móvil and Grupo Financiero Inbursa; member of the board of SBC Communications
Emilio Azcárraga Jean Director	Born:	1968
	First elected:	2000
	Term expires:	2003
	Principal occupation:	President of Grupo Televisa, S.A. de C.V.
	Other directorships:	Chairman of the board of directors of Grupo Televisa, member of Consejo Mexicano de Hombres de Negocios

Jaime Chico Pardo Vice chairman; member of the Executive Committee	Born:	1950
	First elected:	1990
	Term expires:	2003
	Principal occupation:	Chief executive officer of Telmex
	Other principal directorships:	Vice chairman of the board of directors of Carso Global Telecom and América Telecom; director of América Móvil, Grupo Financiero Inbursa and Industrias Nacobre, S.A. de C.V.
	Business experience:	Chief executive officer of Grupo Condumex, S.A.; president of Corporación Industrial Llantera (Euzkadi General Tire de México)
Antonio Cosío Ariño Director	Born:	1935
	First elected:	1990
	Term expires:	2003
	Principal occupation:	General manager of Cía Industrial de Tepeji del Río, S.A. de C.V.
	Other directorships:	Chairman of the board of directors of Agrocultivos Todos Santos, S.A. de C.V., Bodegas de Santos Tomás, S.A. de C.V., Cía Inmobiliaría Cabo San Lucas, S.A. de C.V. and Grupo Hotelero Brisas, S.A. de C.V.
Amparo Espinosa Rugarcía Director	Born:	1941
	First elected:	1990
	Term expires:	2003
	Principal occupation:	President of the Center for Women's Studies in México City
Elmer Franco Macías Director	Born:	1940
	First elected:	1990
	Term expires:	2003
	Principal occupation:	President and director of Grupo Infra, S.A. de C.V.
	Other directorships:	Director of Banco Nacional de México, S.A., Grupo Financiero Inbursa and Grupo Condumex
	Business experience:	Various positions at Grupo Infra since 1958
Angel Losada Moreno Director	Born:	1955
	First elected:	1990
	Term expires:	2003
	Principal occupation:	Chief executive officer of Grupo Gigante, S.A. de C.V.
	Other directorships:	Vice president of the board of directors of Grupo Gigante, director of Grupo Financiero Banamex—Accival

Rómulo O'Farrill Jr. Director	Born:	1917
	First elected:	1990
	Term expires:	2003
	Principal occupation:	Chairman and general manager of Novedades Editores, S.A. de C.V.
	Other directorships:	Chairman of the board of directors of Grupo Automotriz O'Farrill y Balderrama, S.A. de C.V., Novedades de Acapulco, S.A. de C.V., Novedades de Quintana Roo, S.A. de C.V. and Distrituidores O'Farrill Puebla
Juan Antonio Pérez Simón Vice chairman; member of the Executive Committee	Born:	1941
	First elected:	1990
	Term expires:	2003
	Principal occupation and other directorships:	Chairman of the board of directors and member of the executive committee of Sanborns Hermanos, S.A., and member of the board of directors of América Telecom
Fernando Senderos Mestre Director	Born:	1950
	First elected:	2000
	Term expires:	2003
	Principal occupation:	Chairman and chief executive officer of Desc, S.A. de C.V.
	Other directorships:	Director of Industrial Peñoles, S.A. de C.V., Kimberly Clark de México, S.A. de C.V., Alfa, S.A. de C.V., Grupo Televisa and Dana Corporation
Carlos Slim Domit Vice chairman; member of the Executive Committee	Born:	1967
	First elected:	1995
	Term expires:	2003
	Principal occupation and other directorships:	Chairman of the board of directors of Grupo Carso, and member of the board of directors of Carso Global Telecom and América Telecom
	Business Experience:	President of Sanborns Hermanos
Marco Antonio Slim Domit Director	Born:	1968
	First elected:	2002
	Term expires:	2003
	Principal occupation and other directorships:	President and Director of Grupo Financiero Inbursa
	Business Experience:	Member of the board of directors of Grupo Carso, *Bolsa Mexicana de Valores* and Sears Roebuck; alternate member of the board of Carso Global Telecom and América Telecom

James W. Callaway	Born:	1946
Director	First elected:	2000
	Term expires:	2003
	Principal occupation:	Group president of SBC Communications, Inc., International Operations
	Business experience:	Various positions in the wireless sector within the SBC group
Janet M. Duncan	Born:	1961
Director	First elected:	2000
	Term expires:	2003
	Principal occupation:	Director of Finance, SBC International Management Services, Inc.
Mark E. Royse	Born:	1959
Director; member of the Executive Committee	First elected:	2000
	Term expires:	2003
	Principal occupation:	President of SBC International Management Services, Inc.
	Other directorships:	Director of ATL—Algar Telecom Leste S.A. and Telecomunicaciones de Guatemala, S.A.
Rafael Kalach Mizrahi	Born:	1946
Director	First elected:	2000
	Term expires:	2003
	Principal occupation:	Chairman and chief executive officer of Grupo Kaltex, S.A. de C.V.
	Other directorships:	Director of Grupo Carso, Sears Roebuck, S.A. de C.V., and Grupo Sanborns, S.A. de C.V.
Ricardo Martín Bringas	Born:	1960
Director	First elected:	2000
	Term expires:	2003
	Principal occupation:	Chief executive officer of Organización Soriana, S.A. de C.V.
	Other directorships:	Director of Banco Bital, S.A., Grupo Financiero Banamex—Accival, Banco Mexicano, S.A. and Home Mart de México, S.A. de C.V.

The alternate directors as of April 30, 2002 are as follows:

Name	First Elected Director or Alternate Director
Patrick Slim Domit	1999
Jorge Esteve Campdera	1990
Humberto Gutierrez-Olvera Zubizarreta	1996
Antonio Cosío Pando	2002
Angeles Espinosa Rugarcía	1993
Agustín Franco Macías	1990
Jaime Alverde Goya	1993
Antonio del Valle Ruíz	1990
José Kuri Harfush	1995
Fernando Solana Morales	2002
Arturo Elias Ayub	2000
Eduardo Valdés Acra	2000
Carlos Bernal Verea	1990
Francisco Medina Chávez	2002
Federico Laffan Fano	1990
Bernardo Quintana Isaac	1990
Jorge A. Chapa Salazar	2002

Of our directors and alternate directors, Elmer Franco Macías and Agustín Franco Macías are brothers; Antonio Cosío Pando is the son of Antonio Cosío Ariño; Carlos Slim Domit, Marco Antonio Slim Domit and Patrick Slim Domit are sons of Carlos Slim Helú; and Amparo Espinosa Rugarcía and Angeles Espinosa Rugarcía are sisters. Arturo Elias Ayub is the son-in-law of Carlos Slim Helú. The Secretary of the Board of Directors is Sergio F. Medina Noriega.

Executive Committee

Our bylaws provide that the Executive Committee may generally exercise the powers of the Board of Directors. The Board of Directors is also required to consult the Executive Committee before deciding on certain matters set forth in the bylaws, and the Executive Committee must provide its views within 10 calendar days following a request from the Board of Directors.

The Executive Committee is elected from among the directors and alternate directors by a majority vote of the AA Shares, A Shares and A Share ADSs voting together. Under the agreement entered into in December 2000 between Carso Global Telecom and SBC International, the Executive Committee consists of four members. The majority of its members must be of Mexican nationality and elected by Mexican shareholders. Carso Global Telecom and SBC International have agreed to vote for three members named by Carso Global Telecom and one member named by SBC International. The current members of the Executive Committee are Messrs. Chico Pardo, Pérez Simón and Carlos Slim Domit, all named by Carso Global Telecom and various other Mexican investors, and Mr. Royse, named by SBC International. The current alternate members of the Executive Committee are Messrs. Cosío Ariño, Gutierrez-Olvera Zubizarreta and Marco Antonio Slim Domit, all named by Carso Global Telecom and various other Mexican investors, and Ms. Duncan, named by SBC International.

Other Committees

In January 2001, a Mexican commission of business leaders (*Consejo Coordinador Empresarial*), with the support of the Comisión Nacional Bancaria y de Valores (CNBV), issued a Code of Best Corporate Practices (*Código de Mejores Prácticas Corporativas*) for publicly traded

Mexican companies, recommending certain actions with respect to various areas of corporate governance. Following these recommendations, on February 14, 2001 the Board of Directors created an Audit Committee and a Compensation Committee. Subsequently, the Securities Market Law was amended effective June 2001 to require that all publicly traded Mexican companies have an audit committee.

The Audit Committee consists of Messrs. Agustín Franco Macías, Valdés Acra, Marco Antonio Slim Domit, del Valle Ruíz and Ms. Duncan. The mandate of the Audit Committee is to establish and monitor procedures and controls in order to ensure that the financial information we distribute is useful, appropriate and reliable and accurately reflects our financial position. In particular, it is required (a) to assist the Board of Directors in selecting candidates for our auditors and reviewing the scope and terms of their engagement, (b) to assist the Executive Committee in monitoring the performance of our auditors and re-evaluating the terms of their engagement, (c) to recommend procedures for preparing financial statements and internal controls, (d) to monitor internal controls and to monitor accounting for specified types of matters, (e) to propose procedures for the preparation of financial statements for internal use that are consistent with the published financial statements, (f) to review with the auditors the annual financial statements and the accounting principles being applied in the annual and the interim financial statements, (g) to report to the Board of Directors on its activities and (h) to perform any other functions the Board of Directors may delegate to the Audit Committee. The Audit Committee has reviewed our consolidated financial statements and notes thereto included elsewhere in this Annual Report and recommended that they be included herein. In addition, pursuant to our bylaws and Mexican law, (i) the Audit Committee is required to submit an annual report to the Board of Directors and (ii) the Board must seek the opinion of the Audit Committee regarding any transaction with a related party that is outside the ordinary course of our business.

The Compensation Committee consists of Messrs. Cosío Ariño, Kalach Mizrahi, Carlos Slim Domit, Pérez Simón and Royse. The mandate of the Compensation Committee is to assist the Board of Directors in evaluating and compensating our senior executives. In particular, it is required (a) to recommend to the Board of Directors procedures for the selection and succession of our chief executive officer and our principal executives, (b) to propose criteria for evaluating executive performance, (c) to analyze the proposals of the chief executive officer concerning the structure and amount of compensation for our senior executives, and to raise them with the Board of Directors, (d) to review new executive compensation programs and the operations of existing programs, (e) to establish contracting practices to avoid excessive payments to executives, (f) to assist the Board of Directors in developing appropriate personnel policies, (g) to participate with the Board of Directors in developing a plan for employees to invest in our Series L Shares, and to review the implementation of such plan, (h) to report to the Board of Directors on its activities and (i) to perform any other functions the Board of Directors may delegate to the Compensation Committee.

Senior Management

As of April 30, 2002, the names, responsibilities and prior business experience of our senior officers are as follows:

Jaime Chico Pardo General Manager and Chief Executive Officer	Appointed: Business Experience:	1995 Director and member of executive committee of Telmex since 1990
Isidoro Ambe Attar Corporate Markets	Appointed: Business Experience:	1997 Various positions in marketing and procurement areas

Adolfo Cerezo Pérez Chief Financial Officer	Appointed: Business Experience:	1991 Various positions in finance, including treasurer of Telmex and counselor for World Bank
Javier Elguea Solís Dean of Inttelmex	Appointed: Business Experience:	1995 Head of human resources at Telmex
Arturo Elías Ayub Strategic Alliances, Communications and Institutional Relations	Appointed: Business Experience:	1998 Various positions in regulation and Internet areas at Telmex
Eduardo Gómez Chibli Technical and Long Distance	Appointed: Business Experience:	1995 Various positions in technical and long distance areas
Javier Mondragón Alarcón General Counsel	Appointed: Business Experience:	1999 Vice president of Grupo Televicentro, S.A. de C.V. and a partner at Bufete Mondragón Alarcón, S.C.
Jaime Pérez Gómez Human Resources	Appointed: Business Experience:	2000 Various positions in legal and human resources areas
Patrick Slim Domit Mass Markets	Appointed: Business Experience:	2000 President of Grupo Carso
Héctor Slim Seade Operational Support	Appointed: Business Experience:	1995 Head of Fianzas Guardiana-Inbursa and Factoraje-Inbursa
Andrés R. Vázquez del Mercado Benshimol Investments and Strategic Development	Appointed: Business Experience:	1999 Head of marketing at Radio Móvil Dipsa, S.A. de C.V. (Telcel)
Oscar Von Hauske Solís Systems and Processes	Appointed: Business Experience:	1996 Head of Finance at Grupo Condumex

Statutory Auditors

Under our bylaws, the holders of a majority of the outstanding AA Shares and A Shares voting together may elect one or more statutory auditors (*comisarios*) and corresponding alternate statutory auditors. The primary role of the statutory auditors is to report to the holders of AA Shares and A Shares at the annual ordinary general meeting regarding the accuracy of the financial information presented to such holders by the Board of Directors. The statutory auditors are also authorized (1) to call ordinary or extraordinary general shareholders' meetings, (2) to place items on the agenda for meetings of shareholders or the Board of Directors, (3) to attend meetings of shareholders or the Board of Directors and (4) generally to monitor our affairs. The statutory auditors also receive monthly reports from the Board of Directors regarding material aspects of our affairs, including our financial condition. The current statutory auditor and alternate statutory auditor are:

Name	Position	First Elected Statutory Auditor or Alternate Statutory Auditor
Alberto Tiburcio Celorio	Statutory Auditor	1993
Fernando Espinosa López	Alternate Statutory Auditor	2001

Compensation of Directors and Officers

In September 2001, we established a stock option plan for our executive officers. The plan has a duration of four years, and 50 million Series L shares are to be made available. Each year, plan participants may select between acquiring all shares available or deferring their purchase until the final year. In 2001, options made available totaled 11,673,401 shares and 106,248 were subscribed. No amounts were accrued or set aside during 2001 to provide pension, retirement or similar benefits for our directors and officers, except amounts computed on an actuarial basis for fixed benefits under our pension plan.

For the year ended December 31, 2001, the aggregate compensation of all of our directors, alternate directors and executive officers paid for services in all capacities was approximately P.64.5 million. Each director or alternate director received an average fee of P.34,833 (nominal) for each meeting of the Board of Directors attended in 2001.

Share Ownership

Share ownership of Carlos Slim Helú and certain members of his immediate family is set forth in "Major Shareholders" under Item 7. Except as discussed therein, none of our other directors, alternate directors or executive officers is the beneficial owner of more than 1% of any class of our capital stock.

Employees

We are one of the largest non-governmental employers in Mexico. The following table sets forth the number of employees and a breakdown of employees by main category of activity and geographic location as of the end of each year in the three-year period ended December 31, 2001.

	December 31,		
	2001	2000	1999
End-of-period number of employees	67,550	66,928	66,262
Categories of activity:			
Local	42,390	42,835	42,849
Long distance	7,679	7,670	8,109
Other	17,481	16,423	15,304
Geographic locations:			
Mexico	67,550	66,928	66,262

At December 31, 2001, the Telephone Workers' Union of Mexico (known by its Spanish acronym, STRM) represented approximately 70.0% of our employees and members of other unions represented approximately 11.3% of our employees. Most management positions are held by non-union employees. Salaries and certain benefits for unionized personnel are renegotiated every year and the collective bargaining agreements with our unionized employees are renegotiated every two years. In April 2002, we and the STRM agreed to a 5.5% nominal increase in basic wages and a 3.4% nominal increase in benefits.

We consider our current relations with our workforce to be good. Under Mexican law, the unions have a right of first refusal if we sell or transfer any of our assets and the government does not exercise its right of first refusal.

Under our labor agreements and Mexican labor law, we are obligated to pay seniority premiums to retiring employees and pensions and death benefits to retired employees. Retirees are entitled to receive pension increases whenever salary increases are granted to current employees. We fund a specific trust for our obligations to retirees. In January 2001, the trust converted 50 million L Shares into full voting AA Shares.

Item 7. Major Shareholders and Related Party Transactions

MAJOR SHAREHOLDERS

The AA Shares represented 32.7% of the total capital stock and 93.3% of the full voting shares (AA shares and A Shares) as of April 30, 2002. The AA Shares are owned by (1) Carso Global Telecom, (2) SBC International, a subsidiary of the U.S. telecommunications company SBC Communications, Inc. and (3) various other Mexican investors. Carso Global Telecom holds interests in telecommunications and was spun off from Grupo Carso in 1996. Carso Global Telecom may be deemed to control us. According to reports of beneficial ownership of our shares filed with the SEC, Carso Global Telecom is controlled by Mr. Carlos Slim Helú and members of his immediate family.

Carso Global Telecom and SBC International are parties to an agreement entered into in December 2000 providing for certain matters relating to their ownership of AA Shares. Among other things, the agreement subjects certain transfers of AA Shares by either party to a right of first offer in favor of the other party, although the right of first offer does not apply to the conversion of AA Shares to L Shares, as permitted by our bylaws, or the subsequent transfer of L Shares. The agreement also provides for the composition of the Board of Directors and the Executive Committee (see "Directors" and "Executive Committee" under Item 6) and for each party to enter into a Management Services Agreement with us (see "Related Party Transactions").

The following table identifies each owner of more than five percent of any class of our shares as of April 30, 2002. Except as described below, we are not aware of any holder of more than five percent of any class of our shares.

	AA Shares(1)		A Shares(2)		L Shares(3)		Percent
	Shares (millions)	Percent of class	Shares (millions)	Percent of class	Shares (millions)	Percent of class	of voting shares(4)
Carso Global Telecom(5)	3,000.0	70.3%	46.0	15.0%	1,086.9	12.8%	66.6%
SBC International(6)	1,059.9	24.8%	—	—	—	—	23.2%
Franklin Resources, Inc.(7)	—	—	—	—	476.5	5.4%	—
Brandes Investment Partners L.P.(7)	—	—	—	—	707.4	8.3%	—

(1) As of April 30, 2002, there were 4,268 million AA Shares outstanding, representing 93.3% of the total full voting shares (AA Shares and A Shares).

(2) As of April 30, 2002, there were 308 million A Shares outstanding, representing 6.7% of the total full voting shares (AA Shares and A Shares).

(3) As of April 30, 2002, there were 8,495 million L Shares outstanding.

(4) AA Shares and A Shares.

(5) According to reports of beneficial ownership of our shares filed with the SEC on May 15, 2001, Carso Global Telecom would have beneficially owned 2,775.4 million L Shares on such date, representing 32.7% of the total shares of the class outstanding as of April 30, 2002, upon conversion of 1,132.5 million AA Shares and all of its A Shares, subject to the restrictions set forth in our bylaws.

(6) According to reports of beneficial ownership of our shares filed with the SEC on March 30, 2001, SBC International would have beneficially owned 1,059.9 million L Shares on such date, representing 12.5% of the total shares of the class outstanding as of April 30, 2002 upon conversion of all of its AA Shares in accordance with the provisions of our bylaws.

(7) Derived from reports of beneficial ownership of our shares filed with the SEC.

The following table sets forth the share ownership, as of April 30, 2002, of our officers and directors who own more than 1% of any class of our capital stock. Mr. Carlos Slim Helú, together with certain members of his immediate family, may be deemed to share beneficial ownership of 3,000.0 million AA Shares and 46.0 million A Shares held by Carso Global Telecom and 1,092.9 million L Shares held by Carso Global Telecom and Grupo Carso. Except as provided below, none of our directors, alternate directors or executive officers is the beneficial owner of more than 1% of any class of our capital stock.

	AA Shares		A Shares		L Shares		Percent
	Shares (millions)	Percent of class	Shares (millions)	Percent of class	Shares (millions)	Percent of class	of voting shares
Carlos Slim Helú(1)	3,000.0	70.3%	46.0	15.0%	1,092.9	12.9%	66.6%
Carlos Slim Domit(2)(5).........	3,000.0	70.3%	46.0	15.0%	1,092.9	12.9%	66.6%
Marco Antonio Slim Domit(3)(5).......................	3,000.0	70.3%	46.0	15.0%	1,092.9	12.9%	66.6%
Patrick Slim Domit(4)(5)........	3,000.0	70.3%	46.0	15.0%	1,092.9	12.9%	66.6%
Antonio Cosío Ariño.............	65.2	1.5%	—	—	—	—	1.5%

(1) Includes 40,000 A shares and 100,000 L Shares owned directly by Carlos Slim Helú. According to reports of beneficial ownership of our shares filed with the SEC on May 15, 2001, Carlos Slim Helú would have beneficially owned 2,779.9 million L Shares on such date, representing 33.0% of the total shares of the class outstanding as of April 30, 2002, upon conversion of all of his AA Shares and A Shares, subject to the restrictions set forth in our bylaws.

(2) Includes 8,132 L Shares owned directly by Carlos Slim Domit.

(3) Includes 8,132 L Shares owned directly by Marco Antonio Slim Domit.

(4) Includes 8,134 L Shares owned directly by Patrick Slim Domit.

(5) According to reports of beneficial ownership of our shares filed with the SEC on May 15, 2001, each of Carlos Slim Domit, Marco Antonio Slim Domit and Patrick Slim Domit would have beneficially owned 2,779.9 million L Shares on such date, representing 33.0% of the total shares of the class outstanding as of April 30, 2002, upon conversion of 1,132.5 million of his AA Shares and all of his A Shares, subject to the restrictions set forth in our bylaws.

At December 31, 2001, 83.2% of our outstanding L Shares were represented by L Share ADSs, each representing the right to receive 20 Telmex L Shares and 99.2% of the L Share ADSs were held by 17,499 holders (including The Depository Trust Company) with registered addresses in the United States. In November 2000, we established a sponsored ADS program for the A Share ADSs. 27.8% of our A Shares were held in the form of A Share ADSs at December 31, 2001, each representing the right to receive 20 Telmex A Shares and there were 4,189 holders (including The Depository Trust Company) with registered addresses in the United States. We have no information concerning holdings of A Shares and L Shares that are not represented by ADSs, or A Share ADSs that are held under the unsponsored A Share ADS programs, which antedate the establishment of the sponsored program, and have not been exchanged for ADSs issued under such sponsored program, by holders with registered addresses in the United States. See “Trading Market” under Item 9.

We purchase our shares on the Mexican Stock Exchange from time to time up to a specified maximum aggregate value authorized by the holders of AA Shares and A Shares and our Board of Directors. In 2001, we purchased 843.7 million L Shares and 1.5 million A Shares, representing 6.0% of the shares outstanding at the beginning of 2001, with an aggregate value of P.13,715 million. As of April 29, 2002, we are authorized to purchase shares with an aggregate value of up to P.10 billion.

Since January 1, 1997, Carso Global Telecom has purchased A Shares and L Shares on the open market from time to time. In percentage terms, the ownership position of Carso Global Telecom has also increased as a result of our repurchase of our own shares. Carso Global Telecom’s percentage ownership of the A Shares was 11.4% on January 1, 1999, 12.4% on January 1, 2000 and 14.1% on January 1, 2001. Its percentage ownership of the L Shares was 19.8% on January 1, 2000, 16.8% on January 1, 2001 and 12.7% on January 1, 2002. In June 2001, Carso Global Telecom converted 500 million L Shares to AA Shares, raising its total ownership of AA Shares to 3,000 million.

RELATED PARTY TRANSACTIONS

General

We engage in a variety of transactions in the ordinary course of business with affiliates. Pursuant to our bylaws and Mexican law, the Audit Committee of our Board of Directors must express an opinion on, and our Board of Directors has exclusive power to approve, any transaction with a related party that is outside the ordinary course of our business.

Our transactions with affiliates include purchasing cable and network construction services from a subsidiary of Grupo Condumex, S.A. de C.V. and insurance from Seguros Inbursa, S.A. The aggregate amount of these purchases was P.8.3 billion in 2001. Grupo Condumex is controlled by Grupo Carso and Seguros Inbursa is controlled by Grupo Financiero Inbursa, each of which are affiliates of Carso Global Telecom. We believe that the prices we paid in these transactions are comparable to those that would be obtained in arms' length negotiations with unaffiliated parties.

From time to time we make investments together with affiliated companies as well as sell our investments to affiliates, as described below.

- In April 2001, we sold our subsidiary Kb/Tel to a subsidiary of Grupo Carso for U.S.$4.2 million.

- In June 2001, we acquired a 45% interest in The Telvista Company, a U.S. telemarketing company, for U.S.$47.0 million. We made this investment together with our affiliates, the other shareholders of Telvista, América Móvil (45%) and Grupo Carso (10%).

- In 1998, we invested in Prodigy Communications Corporation, or Prodigy, jointly with Carso Global Telecom. From 1998 through 2000, our investment in Prodigy totaled U.S.$121.3 million. In November 2001, we sold our interest in Prodigy for U.S.$82.6 million to an affiliate of SBC International that conducted a public tender offer.

We also pay fees to Carso Global Telecom and SBC International for consulting and management services, pursuant to agreements with each party negotiated on behalf of us by a special committee of directors unaffiliated with any of the parties. The aggregate amount paid to each company (and France Télécom Financiére Internationale before it sold all its shares in Telmex in June 2000) under these agreements was U.S.$30 million in 2001, U.S.$28.3 million in 2000 and U.S.$45 million in 1999. The current agreements with Carso Global Telecom and SBC International were renewed in December 2001 on substantially similar terms, providing for payments to both of them in the aggregate of U.S.$29 million for the year 2002.

We make substantial regular contributions to the Telmex Foundation, which is controlled by a committee, the chairman of which is Mr. Carlos Slim Helú. See "Telmex—The Telmex Foundation" under Item 3. We contributed P.500.0 million in 2001, P.1,302.7 million in 2000 and P.1,141.7 million in 1999.

Transactions between Telmex and América Móvil

América Móvil has or will have a variety of contractual relationships with us and our subsidiaries. These include agreements arising out of the spin-off, certain transitional arrangements and continuing commercial relationships.

Continuing Commercial Relationships

Because both we and Telcel, the leading wireless operator that we spun-off to América Móvil in 2000, provide telecommunications services in the same geographical markets, we have extensive operational relationships. These include interconnection between our respective networks; use of facilities, particularly for the co-location of equipment on premises we own; use by Telcel of our private circuits; and use by each of the services provided by the other. These operational relationships are subject to a variety of different agreements which, for the most part, were in place prior to the spin-off without being significantly modified as a result of the spin-off. Many of them are also subject to specific regulations governing all telecommunications operators. Interconnection fees represent the largest component of amounts paid under these agreements. In 2001, the aggregate amount we paid Telcel for interconnection fees totaled P.7,012 million and the aggregate amount paid to us by Telcel totaled P.3,172 million. The terms of the arrangements with Telcel are generally similar to those on which each company does business with other, unaffiliated parties.

In addition, we distribute Telcel's handsets and prepaid cards on commercial terms similar to those given to other cellular distributors.

Implementation of the Spin-off

The separation of América Móvil from us and the transfer of equity, assets and liabilities to América Móvil was effected by the action taken at our extraordinary shareholders' meeting held on September 25, 2000. Neither we nor América Móvil has made any promises to the other regarding the value of any of the assets América Móvil received in the spin-off. Under the shareholder resolution adopted at the meeting, América Móvil is obligated to indemnify us against any liability, expense, cost or contribution asserted against us that arises out of the assets owned directly or indirectly by Sercotel, the subsidiary whose shares were transferred to América Móvil in the spin-off.

América Móvil has entered into an agreement with us to ensure that the purposes of the spin-off are fully achieved. Among other things, this agreement provides in general terms as follows:

- América Móvil agrees to indemnify us against any loss or expense resulting from the assertion against us of any liabilities or claims that were transferred to América Móvil in the spin-off or that relate to the businesses transferred to América Móvil in the spin-off.

- We agree to indemnify América Móvil against any loss or expense resulting from the assertion against América Móvil of any liabilities or claims that we retained in the spin-off or that relate to the businesses we retained in the spin-off.

- We and América Móvil agree to cooperate in obtaining consents or approvals, giving notices or making filings, as may be required as a result of the spin-off or in order to achieve the purposes of the spin-off.

- We and América Móvil each agree to provide the other with information required to prepare financial statements, tax returns, regulatory filings or submissions and for other specified purposes.

- We and América Móvil each agree to maintain the confidentiality of any information concerning the other that we obtained prior to the spin-off or that we obtain in connection with the implementation of the spin-off.

- We and América Móvil each agree that we will not take any action that could reasonably be expected to prevent the spin-off from qualifying as tax-free under Mexican or U.S. federal tax laws.

- We and América Móvil each release the other from certain claims arising prior to the spin-off.

- With respect to undertakings we have given for the benefit of creditors of subsidiaries and affiliates that were transferred to América Móvil, we and América Móvil agree that we will use our best efforts to replace each of these undertakings with undertakings of América Móvil or its subsidiaries.

We have entered into specific agreements with América Móvil with respect to several of these undertakings, providing for América Móvil to indemnify us and to take steps to succeed to our obligations.

Transitional Services

We provided certain services to América Móvil on an interim basis through the third quarter of 2001 while América Móvil developed the personnel and systems necessary to provide these services itself. The services were provided at a fixed periodic price based on the estimated cost of providing the services plus a percentage. They included legal, financial, administrative, accounting and investor relations services.

Contingent Liabilities

Under Mexican law, we remain jointly and severally liable for any obligations transferred to América Móvil pursuant to the spin-off for a period of three years beginning on September 25, 2000, the date the spin-off was approved by our shareholders. Such liability, however, does not extend to any obligation to a creditor that has given its express consent relieving us of such liability and approving the spin-off. We have undertaken contractual commitments to support certain of the subsidiaries and investments that were transferred to América Móvil in the spin-off. We cannot be released from these commitments without the consent of the respective beneficiaries, which has not yet been obtained. We intend to seek the requisite consents to release us from these commitments, but we cannot assure you that the beneficiaries of these commitments will consent or know when they may do so. These commitments are described in “Contingent Liabilities” under Item 5.

Item 8. Financial Information

CONSOLIDATED FINANCIAL STATEMENTS

See “Item 18—Financial Statements” and pages F-1 through F-42.

LEGAL PROCEEDINGS

There were a number of pending proceedings before the Mexican courts in which we or our competitors had challenged determinations or regulations issued by Cofetel, most of which were withdrawn as a result of December 2000 agreements with certain competitors. These are described in “Regulation” under Item 4. We are also involved in legal proceedings in the ordinary course of our business, none of which is material. The following paragraphs describe certain legal proceedings, other than those involving Cofetel regulations or determinations, that are outside the ordinary course of business.

We were notified in August 1994 of a civil complaint brought in the Mexican courts by our former employee Mr. Antonio Hernández. Mr. Hernández claimed that he invented a certain telecommunications system, referred to in the complaint as the “High Traffic System,” and claimed that we were using this system in violation of Mexican copyright law. We settled this suit in 2001.

In December 1995, our cellular competitor Grupo Iusacell, S.A. de C.V. commenced proceedings against us before the Competition Commission, claiming that we engaged in anti-competitive practices such as cross-subsidization, predatory pricing and discrimination in access for the benefit of Telcel, our then-cellular subsidiary. In the petition, Iusacell requested that the Competition Commission impose sanctions against us, including fines, an order requiring us to sell Telcel and an order nullifying certain provisions in the interconnection agreement between Iusacell and us. In January 2001, we reached an agreement with Iusacell, which, among others, confirmed the parties’ acceptance of interconnection rates imposed by Cofetel for long distance calls and provided for the payment of outstanding unpaid fees by each party. As a result, the parties agreed to withdraw their outstanding legal proceedings. Despite the parties’ withdrawal, in July 2001, the Competition Commission ruled that we had engaged in anti-competitive practices. We filed an appeal for reconsideration that was denied. We are preparing a challenge to this denial.

DIVIDENDS

We have paid cash dividends on our shares each year since 1958. The table below sets forth the nominal amount of dividends paid per share in each year indicated, in pesos and translated into U.S. dollars at the free exchange rate on each of the respective payment dates.

Year ended December 31,	Pesos per Share	Dollars per Share
2001	P. 0.4900	U.S.$ 0.0529
2000	0.4450	0.0424
1999	0.3875	0.0412
1998	0.3500	0.0377
1997	0.2625	0.0330

Since 1998, we have paid dividends quarterly. The dividends from earnings in a given year are determined at the annual meeting of shareholders in April of the following year and paid in June, September and December of such following year and in March of the year after that. In April 2000, we declared a dividend of P.0.460 per share, which we paid in equal installments of P.0.115 per share in June 2000, September 2000, December 2000 and March 2001. In April 2001, we declared a dividend of P.0.500 per share, which we paid in equal installments of P.0.125 per share in June 2001, September 2001, December 2001 and March 2002. In April 2002, we declared a dividend of P.0.56 per share, which will be payable in equal installments of P.0.14 per share in June 2002, September 2002, December 2002 and March 2003.

The declaration, amount and payment of dividends are determined by majority vote of the holders of AA Shares and A Shares, generally on the recommendation of the Board of Directors, and will depend on our results of operations, financial condition, cash requirements, future prospects and other factors deemed relevant by the holders of AA Shares and A Shares. Accordingly, we cannot assure you that we will continue to pay dividends or that future dividends will be comparable to historical dividends. Our bylaws provide that holders of the AA Shares, the A Shares and the L Shares share equally on a per-share basis in dividend payments and other distributions.

Item 9. The Offer and Listing

TRADING MARKET

The L Share ADSs, each representing 20 L Shares of Telmex, are issued by Morgan Guaranty Trust Company of New York, or the Depositary, as depositary for the L Share ADSs. The L Share ADSs are traded on the New York Stock Exchange and listed on the Frankfurt Stock Exchange, and the L Shares are traded on the Mexican Stock Exchange and listed on the Mercado de Valores Latinoamericano ("Latibex") in Madrid, Spain.

In November 2000, we established a sponsored ADS program for the A Share ADSs. The A Share ADSs, each representing 20 A Shares of Telmex, are issued by the Depositary, as depositary for the A Share ADSs. There have been for many years "unsponsored" A Share ADSs programs established by several depositaries without our agreement. Holders of over 91% of the A Share ADSs issued under the unsponsored ADS programs, each representing one A share, have exchanged their A Share ADSs for those issued by the Depositary under the sponsored program. Holders who do not exchange will not receive dividends and eventually will escheat their A Share ADSs to their respective states. The A Shares are traded on the Mexican Stock Exchange, and the sponsored A Share ADSs are quoted on the NASDAQ SmallCap Market. Trading has ceased with respect to the unsponsored A Share ADSs.

The following table sets forth, for the periods indicated, the reported high and low sales prices for the L Shares on the Mexican Stock Exchange and the reported high and low sales prices for the L Share ADSs on the New York Stock Exchange. Prices have not been restated in constant currency units.

	Mexican Stock Exchange (Pesos per L Share)		New York Stock Exchange (U.S. Dollars per L Share ADS)	
	High	**Low**	**High**	**Low**
Annual highs and lows				
2001	P. 16.90	P. 13.79	U.S.$37.04	U.S.$27.48
2000	35.30	20.10	76.31	42.31
1999	26.50	11.20	56.35	21.13
1998	13.65	8.85	28.75	16.75
1997	11.40	6.51	28.19	16.57
Quarterly highs and lows				
2002:				
First quarter	P. 18.26	P. 16.26	U.S.$41.05	U.S.$37.73
2001:				
First quarter	P. 16.90	P. 13.79	U.S.$34.31	U.S.$27.48
Second quarter	16.80	13.88	36.62	29.41
Third quarter	16.86	14.04	37.04	29.35
Fourth quarter	16.35	15.10	35.60	31.76
2000:				
First quarter	P. 35.30	P. 24.68	U.S.$76.31	U.S.$51.66
Second quarter	31.55	21.55	68.00	45.37
Third quarter	31.00	22.85	65.81	49.50
Fourth quarter	26.05	20.10	54.31	42.31

	Mexican Stock Exchange (Pesos per L Share)		New York Stock Exchange (U.S. Dollars per L Share ADS)	
	High	Low	High	Low
2002:				
January	P. 17.83	P. 16.26	U.S.$39.09	U.S.$35.73
February	17.51	16.63	38.75	36.40
March	18.62	17.75	41.05	39.00
April	18.55	17.02	40.35	37.03
May	18.06	16.65	38.35	34.49
2001:				
December	16.35	15.46	35.60	33.35

The table below sets forth, for the periods indicated, the reported high and low sales prices for the A Shares on the Mexican Stock Exchange and the high and low bid prices for A Share ADSs published by NASDAQ. Bid prices published by NASDAQ for the A Share ADSs are inter-dealer quotations and may not reflect actual transactions. Prices have not been restated in constant currency units.

	Mexican Stock Exchange (Pesos Per A Share)		NASDAQ (U.S. Dollars per A Share ADS)	
	High	Low	High	Low
Annual highs and lows				
2001	P. 16.88	P. 13.86	U.S.$36.80	U.S.$26.86
2000	35.80	20.80	3.75	2.09
1999	26.80	11.10	2.86	1.00
1998	13.75	8.76	1.41	0.80
1997	11.40	6.50	1.44	0.53
Quarterly highs and lows				
2002:				
First quarter	P. 18.56	P. 16.19	U.S.$41.00	U.S.$35.52
2001:				
First quarter	P. 16.88	P. 14.55	U.S.$34.00	U.S.$26.86
Second quarter	16.63	13.86	36.49	29.25
Third quarter	16.70	14.00	36.80	29.15
Fourth quarter	16.35	15.00	35.30	31.75
2000:				
First quarter	P. 35.80	P. 24.80	U.S.$ 3.75	U.S.$ 2.56
Second quarter	31.50	21.50	3.25	2.19
Third quarter	31.00	22.00	3.22	2.41
Fourth quarter	25.85	20.80	2.69	2.09

	Mexican Stock Exchange (Pesos Per A Share)		NASDAQ (U.S. Dollars per A Share ADS)	
	High	**Low**	**High**	**Low**
Monthly highs and lows				
2002:				
January	P. 17.60	P. 16.19	U.S.$39.00	U.S.$35.52
February	17.45	16.50	38.55	36.05
March	18.56	17.70	41.00	39.00
April	18.45	17.00	40.04	36.90
May	17.90	16.70	38.00	34.20
2001:				
December	16.35	15.20	32.85	32.96

TRADING ON THE MEXICAN STOCK EXCHANGE

The Mexican Stock Exchange (*Bolsa Mexicana de Valores, S.A. de C.V.*), located in Mexico City, is the only stock exchange in Mexico. Founded in 1907, it is organized as a corporation whose shares are held by 26 brokerage firms, which are exclusively authorized to trade on the Exchange. Trading on the Mexican Stock Exchange takes place principally on the Exchange through automated systems, which is open between the hours of 8:30 a.m. and 3:00 p.m., Mexico City time, each business day. Trades in securities listed on the Mexican Stock Exchange can also be effected off the Exchange. The Mexican Stock Exchange operates a system of automatic suspension of trading in shares of a particular issuer as a means of controlling excessive price volatility, but under current regulations this system does not apply to securities such as the A Shares or the L Shares that are directly or indirectly (for example, through American Depositary Shares) quoted on a stock exchange (including for these purposes NASDAQ) outside Mexico.

Settlement is effected two business days after a share transaction on the Mexican Stock Exchange. Deferred settlement, even by mutual agreement, is not permitted without the approval of the Mexican National Securities Commission. Most securities traded on the Mexican Stock Exchange, including those of Telmex, are on deposit with S.D. Indeval, S.A. de C.V. (Indeval), a privately owned securities depositary that acts as a clearinghouse for Mexican Stock Exchange transactions.

Item 10. Additional Information

BYLAWS

Set forth below is a brief summary of certain significant provisions of our bylaws and Mexican law. The full text of our bylaws has been filed as an exhibit to this Annual Report. For a description of the provisions of our bylaws relating to our Board of Directors, Executive Committee and statutory auditors, see Item 6.

Organization and Register

Telmex is a *sociedad anónima de capital variable* organized in Mexico under the Mexican Companies Law (*Ley General de Sociedades Mercantiles*). It is registered with the Public Registry of Commerce of Mexico City under the number 5229.

Share Capital

Our capital stock comprises Series AA Shares, without par value, Series A Shares, without par value and Series L Shares, without par value. All of the outstanding shares are fully paid and non-assessable.

AA Shares and A Shares have full voting rights. Holders of L Shares may vote only in limited circumstances as described under "—Voting Rights." The rights of holders of all series of capital stock are otherwise identical except for limitations on non-Mexican ownership of AA Shares. The AA Shares, which must always represent at least 51% of the combined AA Shares and A Shares, may be owned only by holders that qualify as Mexican investors as defined in the Foreign Investment Law and our bylaws. See "—Limitations on Share Ownership."

Each AA Share or A Share may be exchanged at the option of the holder for one L Share, provided that the AA Shares may never represent less than 20% of our outstanding capital stock or less than 51% of our combined AA Shares and A Shares.

Pursuant to provisions of our bylaws, each L Share is exchangeable at the option of the holder for one AA Share by delivering the L Share certificate to our treasury for cancellation and receiving the corresponding AA Share certificate. The right to exchange is subject to limitations on non-Mexican ownership of AA Shares and to the requirement that the AA Shares and A Shares together may never represent more than 51% of our outstanding capital stock.

Voting Rights

Each AA Share and A Share entitles the holder thereof to one vote at any meeting of our shareholders. Each L Share entitles the holder to one vote at any meeting at which holders of L Shares are entitled to vote. Holders of L Shares are entitled to vote only to elect two members of the Board of Directors and the corresponding alternate directors and on the following matters:

- the extension of Telmex's term of duration,
- the transformation of Telmex from one type of company to another,
- any merger in which Telmex is not the surviving entity or any merger with an entity whose principal corporate purposes are different from those of Telmex,

- removal of our shares from listing on the Mexican Stock Exchange or any foreign stock exchange, and

- any action that would prejudice the rights of holders of L Shares and not prejudice the other classes of shares similarly. A resolution on any of the specified matters requires the affirmative vote of both a majority of all outstanding shares and a majority of the AA Shares and the A Shares voting together.

Under Mexican law, holders of shares of any series are also entitled to vote as a class on any action that would prejudice the rights of holders of shares of such series but not rights of holders of shares or other series, and a holder of shares of such series would be entitled to judicial relief against any such action taken without such a vote. The determination whether an action requires a class vote on these grounds would initially be made by the Board of Directors or other party calling for shareholder action. A negative determination would be subject to judicial challenge by an affected shareholder, and the necessity for a class vote would ultimately be determined by a court. There are no other procedures for determining whether a proposed shareholder action requires a class vote, and Mexican law does not provide extensive guidance on the criteria to be applied in making such a determination.

Shareholders' Meetings

General shareholders' meetings may be ordinary meetings or extraordinary meetings. Extraordinary general meetings are those called to consider certain matters specified in Article 182 of the Mexican Companies Law, including, principally, amendments of the bylaws, liquidation, merger and transformation from one type of company to another, as well as to consider the removal of our shares from listing on the Mexican Stock Exchange or any foreign stock exchange. General meetings called to consider all other matters are ordinary meetings. The two directors elected by the holders of L Shares are elected at a special meeting of holders of L Shares. All other matters on which holders of L Shares are entitled to vote would be considered at an extraordinary general meeting. Holders of L Shares are not entitled to attend or address meetings of shareholders at which they are not entitled to vote.

A special meeting of the holders of L Shares must be held each year for the election of directors. An ordinary general meeting of the holders of AA Shares and A Shares must be held each year to consider the approval of the financial statements for the preceding fiscal year, to elect directors and statutory auditors and to determine the allocation of the profits of the preceding year.

The quorum for an ordinary general meeting of the AA Shares and A Shares is 50% of such shares, and action may be taken by a majority of the shares present. If a quorum is not available, a second meeting may be called at which action may be taken by a majority of the AA Shares and A Shares present, regardless of the number of such shares. Special meetings of holders of L Shares are governed by the same rules applicable to ordinary general meetings of holders of AA Shares and A Shares. The quorum for an extraordinary general meeting at which holders of L Shares may not vote is 75% of the AA shares and A Shares, and the quorum for an extraordinary general meeting at which holders of L Shares are entitled to vote is 75% of the outstanding capital stock. If a quorum is not available in either case, a second meeting may be called and action may be taken, provided a majority of the shares entitled to vote is present. Whether on first or second call, actions at an extraordinary general meeting may be taken by a majority vote of the AA Shares and A Shares outstanding and, on matters which holders of L Shares are entitled to vote, a majority vote of all the capital stock.

Holders of 20% of our outstanding capital stock may have any shareholder action set aside by filing a complaint with a court of law within 15 days after the close of the meeting at which such action was taken and showing that the challenged action violates Mexican law or our bylaws. In addition, any holder of our capital stock may bring an action at any time within five years challenging any shareholder action. Relief under these provisions is only available to holders

- who were entitled to vote on, or whose rights as shareholders were adversely affected by, the challenged shareholder action, and
- whose shares were not represented when the action was taken or, if represented, were voted against it.

Shareholders' meetings may be called by the Board of Directors, its chairman, the statutory auditors or a court. The Board of Directors or the statutory auditors may be required to call a meeting of shareholders by the holders of 10% of the outstanding capital stock. Notice of meetings must be published in the *Diario Oficial* (Official Gazette) or a newspaper of general circulation in Mexico City at least 15 days prior to the meeting. In order to attend a meeting, shareholders must deposit their shares with us at our office in Mexico City, with a Mexican or foreign banking institution or with a Mexican exchange broker. If so entitled to attend the meeting, a shareholder may be represented by proxy. The depositary for the L Share ADSs and the A Share ADSs does not satisfy this requirement, so ADS holders are not entitled to attend shareholder meetings. However, ADS holders may still vote through the depositary.

Dividend Rights

At the annual ordinary general meeting of holders of AA Shares and A Shares, the Board of Directors submits our financial statements for the previous fiscal year, together with a report thereon by the Board, to the holders of AA Shares and A Shares for approval. The holders of AA Shares and A Shares, once they have approved the financial statements, determine the allocation of our net profits for the preceding year. They are required by law to allocate 5% of such net profits to a legal reserve, which is not thereafter available for distribution except as a stock dividend, until the amount of the legal reserve equals 20% of our capital stock. The remainder of net profits is available for distribution.

All shares outstanding at the time a dividend or other distribution is declared are entitled to participate in such dividend or other distribution.

Limitation on Capital Increases

Our bylaws require that any capital increase be represented by new shares of each series in proportion to the number of shares of each series outstanding.

Preemptive Rights

In the event of a capital increase, a holder of existing shares of a given series has a preferential right to subscribe for a sufficient number of shares of the same series to maintain the holder's existing proportionate holdings of shares of that series. Preemptive rights must be exercised within 15 days following the publication of notice of the capital increase in the *Diario Oficial* (Official Gazette) and a newspaper of general circulation in Mexico City. Under Mexican law, preemptive rights cannot be traded separately from the corresponding shares that give rise to such rights. As a result, there is no trading market for the rights in connection with a capital increase. Holders of ADSs may exercise preemptive rights only through the depositary. We are not required to take steps that may be necessary to make this possible.

Limitations on Share Ownership

Ownership by non-Mexicans of shares of Mexican enterprises in certain economic sectors, including telephone services, is regulated by the 1993 Foreign Investment Law and the 1998 Regulations thereunder. The National Commission on Foreign Investment is responsible for administration of the Foreign Investment Law and Regulations. In order to comply with restrictions on the percentage of their capital stock that may be owned by non-Mexican investors, Mexican companies typically limit particular classes of their stock to Mexican ownership. Under the Foreign Investment Law, a trust for the benefit of one or more non-Mexican investors may qualify as Mexican if the trust meets certain conditions that will generally ensure that the non-Mexican investors do not determine how the shares are voted.

Non-Mexican investors are not permitted to own more than 49% of the capital stock of a Mexican corporation engaged in the telephone business. Pursuant to a decision of the Foreign Investment Commission dated August 10, 1990, the L Shares of Telmex, because of their limited voting rights, are not taken into account in determining compliance with this restriction and accordingly are not subject to Mexican ownership restrictions. This decision is expected to be renewed with respect to Telmex's L Shares. The A Shares are also unrestricted. The AA Shares, however, which must always represent at least 51% of the combined AA Shares and A Shares, may be owned only by holders that qualify as Mexican investors as defined in the Foreign Investment Law and our bylaws. A holder that acquires AA Shares in violation of the restrictions on non-Mexican ownership will have none of the rights of a shareholder with respect to those AA Shares. As a consequence of these limitations, non-Mexican investors cannot under Mexican law own AA Shares except through trusts that effectively neutralize the votes of non-Mexican investors.

Pursuant to the Foreign Investment Law and Regulations, we have registered any foreign owner of our shares, and the depositary with respect to the ADSs representing our shares, with the National Registry of Foreign Investment.

In addition, pursuant to the Foreign Investment Law and Regulations, our Mexican shareholders retain the power to determine our administrative control and management.

Foreign states are prohibited under the General Communications Law from directly or indirectly owning shares of Telmex. The Telecommunications Regulations provide, however, that foreign state-owned enterprises organized as separate entities with their own assets may own minority interests in Telmex or any number of shares with limited voting rights. Ownership of A Shares or L Shares by such foreign state-owned companies, or by pension or retirement funds organized for the benefit of employees of state, municipal or other governmental agencies, will not be considered direct or indirect ownership by foreign states for the purposes of the General Communications Law.

Restrictions on Certain Transactions

Our bylaws provide that any acquisition or transfer of more than 10% of any shares issued by the company, effected in one or more transactions by any person or group of persons acting in concert, requires prior approval by our Board of Directors.

Registration and Transfer

Our shares are registered with the National Registry for Securities, as required under the Securities Market Law and regulations issued by the CNBV. If we wish to cancel our registration, or if it is cancelled by the CNBV, the stockholders having control of Telmex at that time will be required to make a public offer to purchase all outstanding shares prior to such cancellation. Unless the CNBV authorizes otherwise, the offer price will be the higher of: (i) the average of the closing price during the previous 30 days on which the shares may have been quoted, or (ii) the book value of the shares in accordance with the most recent quarterly report submitted to the CNBV and to the Mexican Stock Exchange. Any amendments to the foregoing provisions included in our bylaws require the prior approval of the Mexican Banking and Securities Commission and the resolution of an extraordinary stockholders' meeting adopted by at least 95% of our outstanding capital stock.

Other Provisions

Variable capital. We are permitted to issue shares constituting fixed capital and L Shares constituting variable capital. All of our outstanding shares of capital stock constitute fixed capital. The issuance of variable-capital L Shares, unlike the issuance of fixed-capital L Shares, does not require an amendment of the bylaws, although it does require a majority vote of the AA Shares and the A Shares. Under Mexican law and our bylaws, if we issued variable-capital L Shares, any holder of such shares would be entitled to redeem them at the holder's option at any time at a redemption price equal to the lower of:

- 95% of the average market value of such shares on the Mexican Stock Exchange for 30 trading days preceding the date on which the exercise of the option is effective and

- the book value of such shares at the end of the fiscal year in which the exercise of the option is effective.

If the option is exercised during the first three quarters of a fiscal year, it is effective at the end of the next succeeding fiscal year. The redemption price would be payable following the annual ordinary general meeting of holders of AA Shares and A Shares at which the relevant annual financial statements were approved.

Forfeiture of shares. As required by Mexican law, our bylaws provide that "any alien who at the time of incorporation or at any time thereafter acquires an interest or participation in the capital of the corporation shall be considered, by virtue thereof, as Mexican in respect thereof and shall be deemed to have agreed not to invoke the protection of his own government, under penalty, in case of breach of such agreement, of forfeiture to the nation of such interest or participation." 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 it may have, including any rights under the U.S. securities laws, with respect to its investment in Telmex. If the shareholder invokes such governmental protection in violation of this agreement, its shares could be forfeited to the Mexican government. Mexican law requires that such a provision be included in the bylaws of all Mexican corporations unless such bylaws prohibit ownership of shares by non-Mexican persons.

Exclusive jurisdiction. Our bylaws provide that legal actions relating to the execution, interpretation or performance of the bylaws shall be brought only in Mexican courts.

Duration. Telmex's existence under the bylaws is 100 years from the date of registration with the Public Registry of Commerce.

Purchase of our own shares. According to the bylaws, we may repurchase our shares on the Mexican Stock Exchange at any time at the then prevailing market price. Any such repurchase must be approved by the Board of Directors, and the amount of shares to be repurchased must be approved by the general ordinary shareholders meeting. In the event that we repurchase shares, our shareholders' equity will be reduced automatically in an amount equal to the assumed par value of each repurchased share. However, if repurchased shares are held as treasury stock, our capital stock will be reduced automatically in an amount equal to the assumed par value of each repurchased share, pending future sales thereof on the Mexican Stock Exchange or cancellation. Our capital stock is automatically increased upon the resale of such shares in an amount equal to their assumed par value. The economic and voting rights corresponding to repurchased shares may not be exercised during the period in which we own such shares, and such shares are not deemed to be outstanding for purposes of calculating any quorum or vote at any shareholders' meeting during such period.

Conflict of interest. A shareholder that votes on a business transaction in which its interest conflicts with Telmex's may be liable for damages, but only if the transaction would not have been approved without its vote.

Appraisal rights. Whenever the shareholders approve a change of corporate purposes, change of nationality of the corporation or transformation from one type of company to another, any shareholder entitled to vote on such change that has voted against it may withdraw from Telmex and receive the book value attributable to its shares, provided it exercises its right within 15 days following the adjournment of the meeting at which the change was approved.

Rights of Shareholders

The protections afforded to minority shareholders under Mexican law are different from those in the United States and many other jurisdictions. The substantive law concerning fiduciary duties of directors has not been the subject of extensive judicial interpretation in Mexico, unlike many states in the United States where duties of care and loyalty elaborated by judicial decisions help to shape the rights of minority shareholders. Mexican civil procedure does not contemplate class actions or shareholder derivative actions, which permit shareholders in U.S. courts to bring actions on behalf of other shareholders or to enforce rights of the corporation itself. Shareholders cannot challenge corporate action taken at a shareholders' meeting unless they meet certain procedural requirements, as described above under "Shareholders' Meetings." As a result of these factors, in practice it may be more difficult for our minority shareholders to enforce rights against us or our directors or controlling shareholders than it would be for shareholders of a U.S. company.

Enforceability of Civil Liabilities

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 their assets 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. It may also be difficult to enforce against them, either inside or outside the United States, judgments obtained against them in U.S. courts, or to enforce in U.S. courts judgments obtained against them in courts in jurisdictions outside the United States, 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.

CERTAIN CONTRACTS

We are party to concession agreements that authorize us to provide certain telecommunications services on specific terms. These are described in "Regulation" under Item 4.

Our agreements with related parties are described in "Related Party Transactions" under Item 7.

EXCHANGE CONTROLS

Mexico has had a free market for foreign exchange since 1991, and the government has allowed the peso to float freely against the U.S. dollar since December 1994. There can be no assurance that the government will maintain its current foreign exchange policies. See “Exchange Rate Information” under Item 3.

TAXATION

The following summary contains a description of certain Mexican federal and U.S. federal income tax consequences of the acquisition, ownership and disposition of L Shares, A Shares, AA Shares, L Share ADSs, A Share ADSs, or AA Share ADSs, but it does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a decision to purchase or hold shares or ADSs.

The Convention for the Avoidance of Double Taxation and the Prevention of Tax Evasion and a Protocol thereto (the "Tax Treaty") between the United States and Mexico entered into force on January 1, 1994. The United States and Mexico have also entered into an agreement concerning the exchange of information with respect to tax matters.

The summary is based upon tax laws of Mexico and the United States as in effect on the date of this Annual Report, including the Tax Treaty, which are subject to change, including changes that may have retroactive effect. Holders of shares or ADSs should consult their own tax advisers as to the Mexican, U.S. or other tax consequences of the purchase, ownership and disposition of shares or ADSs, including, in particular, the effect of any foreign, state or local tax laws.

Mexican Tax Considerations

The following is a general summary of the principal consequences under the Mexican Income Tax Law (*Ley del Impuesto sobre la Renta*) and rules and regulations thereunder, as currently in effect, of an investment in Shares or ADSs by a holder that is not a resident of Mexico and that will not hold shares or ADSs or a beneficial interest therein in connection with the conduct of a trade or business through a permanent establishment or fixed base in Mexico.

For purposes of Mexican taxation, a natural person is a resident of Mexico for tax purposes if he has established his home in Mexico, unless he has resided in another country for more than 183 days, whether consecutive or not, in any one calendar year and can demonstrate that he has become a resident of that country for tax purposes, and a legal entity is a resident of Mexico if it was incorporated in Mexico or maintains the principal administration of its business or the effective location of its management in Mexico. A Mexican citizen is presumed to be a resident of Mexico unless such person can demonstrate the contrary. If a non-resident of Mexico is deemed to have a permanent establishment or fixed base in Mexico for tax purposes, all income attributable to such permanent establishment or fixed base will be subject to Mexican taxes, in accordance with applicable laws.

Tax Treaties

Provisions of the Tax Treaty that may affect the taxation of certain U.S. holders are summarized below. The United States and Mexico have also entered into an agreement that covers the exchange of information with respect to tax matters.

The Mexican Income Tax Law has established procedural requirements for a holder disposing of his shares to be entitled to the benefits under any of the tax treaties to which Mexico is a party. These procedural requirements include the obligation to (i) prove tax treaty residence, (ii) present tax calculations made by authorized certified public accountants and (iii) appoint representatives in Mexico for taxation purposes.

Payment of Dividends

Dividends, either in cash or in kind, paid with respect to the L Shares, A Shares, AA Shares, L Share ADSs, A Share ADSs or AA Share ADSs will not be subject to Mexican withholding tax.

When dividends are paid from a corporation's previously taxed net earnings account *(cuenta de utilidad fiscal neta* or CUFIN), the corporation is not required to pay any Mexican corporate tax on the dividends. When such dividends are paid from a corporation's previous net reinvested tax profit account *(cuenta de utilidad fiscal neta reinvertida* or CUFINRE), the corporation will be required to pay a 5% Mexican corporate tax on the dividends multiplied by 1.5385. If dividends are paid from neither the CUFIN nor the CUFINRE, a corporation will be required to pay a 35% Mexican corporate tax on the dividends multiplied by 1.5385.

As of January 1, 2002, Mexican entities may no longer defer 5% of their corporate income tax on reinvested earnings, and therefore they will no longer have a CUFINRE account. However, according to applicable transition rules, when paying dividends, Mexican entities with a favorable balance in their CUFINRE corresponding to taxes deferred for earnings obtained in the years 1999, 2000 and 2001, must pay such deferred tax before comparing the dividend to the CUFIN.

The corporate income tax rate will be reduced annually by 1% until 2005. For the year 2002, the applicable corporate tax rate is 35% and will be reduced by 1% each year until reaching the 32% level in 2005.

Taxation of Dispositions

Under current Mexican law and regulations, there is no basis for the Mexican tax authorities to impose taxes on income obtained by non-Mexican residents, individuals or entities from dispositions of ADSs.

The sale of shares by a non-resident individual holder will not be subject to any Mexican tax if the transaction is carried out through the Mexican Stock Exchange or other securities markets approved by the Mexican Ministry of Finance and certain additional requirements are met. Sales or other dispositions of shares made in other circumstances generally would be subject to Mexican tax, regardless of the nationality or residence of the transferor.

For non-resident corporations and individuals that do not meet the requirements referred to above, gross income obtained on the sale or other disposition of shares will be subject to a 5% tax if the transaction is carried out through the Mexican Stock Exchange. Under certain circumstances, non-resident corporations and those individuals, alternatively, may elect to pay a 20% tax on the net income earned on these transactions.

On April 11, 2002, a general ruling was issued by the Mexican Ministry of Finance allowing non-resident legal entities to elect not to pay the tax discussed in the previous paragraph. On May 30, 2002 the Mexican Ministry of Finance extended the effective date of this ruling until February 28, 2003, but the Mexican Ministry of Finance may withdraw this tax benefit after such extension has expired. Certain restrictions will apply if the L Shares, A Shares or AA Shares are transferred as a consequence of public offerings.

If a corporation is a resident in a tax haven (as defined by the Mexican Income Tax Law), the applicable rate will be 40% on the gross income obtained. Corporations located in a tax haven that sell shares of a Mexican company to a Mexican resident are given the opportunity in 2002 to seek an authorization from the Mexican Tax Authorities that would allow them to pay tax at a rate of 1.8% on the gross income obtained, in the event that the buyer and the seller are part of the same group of companies and certain requirements are met.

Pursuant to the Tax Treaty, gains realized by qualifying U.S. holders from the sale or other disposition of shares, even if the sale is not conducted through a recognized stock exchange, will not be subject to Mexican income tax except that Mexican taxes may apply if such U.S. holder owned at least 25% of the shares representing our capital stock (including ADSs), directly or indirectly, during the 12-month period preceding such disposition.

Gains realized by other holders that are eligible to receive benefits pursuant to other income tax treaties to which Mexico is a party may be exempt form Mexican income tax in whole or in part. Non-U.S. holders should consult their own tax advisors as to their possible eligibility under such treaties.

Other Mexican Taxes

A non-resident holder will not be liable for estate, inheritance or similar taxes with respect to its holdings of shares or ADSs; provided, however, that gratuitous transfers of shares may in certain circumstances result in imposition of a Mexican tax upon the recipient. There are no Mexican stamp, issue registration or similar taxes payable by a non-resident holder with respect to shares or ADSs.

U.S. Federal Income Tax Considerations

The following is a summary of certain U.S. federal income tax consequences to U.S. holders (as defined below) of the acquisition, ownership and disposition of shares or ADSs. The summary does not purport to be a comprehensive description of all of the tax consequences of the acquisition, ownership or disposition of shares or ADSs. The summary applies only to U.S. holders that will hold their Shares or ADSs as capital assets and does not apply to special classes of U.S. holders such as dealers in securities or currencies, holders with a functional currency other than the U.S. dollar, holders of 10% or more of our voting shares (whether held directly or through ADSs or both), tax-exempt organizations, financial institutions, holders liable for the alternative minimum tax, securities traders electing to account for their investment in their shares or ADSs on a mark-to-market basis, and persons holding their shares or ADSs in a hedging transaction or as part of a straddle or conversion transaction.

For purposes of this discussion, a “U.S. holder” is a holder of shares or ADSs that is:

- a citizen or resident of the United States of America,
- a corporation organized under the laws of the United States of America or any state thereof, or
- otherwise subject to U.S. federal income taxation on a net income basis with respect to the shares or ADSs.

Each U.S. holder should consult such holder’s own tax advisor concerning the overall tax consequences to it of the ownership or disposition of shares or ADSs that may arise under foreign, state and local laws.

Treatment of ADSs

In general, a U.S. holder of ADSs will be treated as the owner of the shares represented by those ADSs for U.S. federal income tax purposes. Deposits or withdrawals of shares by U.S. holders in exchange for ADSs will not result in the realization of gain or loss for U.S. federal income tax purposes. U.S. holders that withdraw any shares should consult their own tax advisors regarding the treatment of any foreign currency gain or loss on any pesos received in respect of such shares.

Taxation of Distributions

In this discussion, we use the term “dividends” to mean distributions paid out of our current or accumulated earnings and profits with respect to Shares or ADSs. In general, the gross amount of any dividends will be includible in the gross income of a U.S. holder as ordinary income on the day on which the dividends are received by the U.S. holder in the case of shares or by the depositary in the case of ADSs. Dividends will be paid in pesos and will be includible in the income of a U.S. holder in a U.S. dollar amount calculated by reference to the exchange rate in effect on the day that they are received by the U.S. holder in the case of shares or by the depositary in the case of ADSs. U.S. holders should consult their own tax advisors regarding the treatment of foreign currency gain or loss, if any, on any pesos received by a U.S. holder or depositary that are converted into U.S. dollars on a date subsequent to receipt. Dividends paid by us will not be eligible for the dividends-received deduction allowed to corporations under the U.S. Internal Revenue Code of 1986, as amended (the “Code”).

Distributions of additional shares or ADSs to U.S. holders with respect to their shares or ADSs that are made as part of a pro rata distribution to all of our shareholders generally will not be subject to U.S. federal income tax.

Dividends paid on shares or ADSs generally will be treated for U.S. foreign tax credit purposes as foreign source passive income, or, in the case of certain U.S. holders, as foreign source financial services income.

Under certain U.S. Treasury Department guidance, foreign tax credits may not be allowed for withholding taxes imposed in respect of certain short-term or hedged positions in securities or in respect of arrangements in which a U.S. holder’s expected economic profit is insubstantial. U.S. holders should consult their own advisors concerning the implications of these rules in light of their particular circumstances.

Taxation of Dispositions

A U.S. holder will recognize gain or loss on the sale or other disposition of the shares or ADSs in an amount equal to the difference between the U.S. holder’s basis in such shares or ADSs (in U.S. dollars) and the amount realized on the disposition (in U.S. dollars, determined at the spot rate on the date of disposition if the amount realized is denominated in a foreign currency). Gain or loss realized by a U.S. holder on such sale or other disposition generally will be long-term capital gain or loss if, at the time of disposition, the shares or ADSs have been held for more than one year. Long-term capital gain realized by a U.S. holder that is an individual generally is subject to a maximum federal income tax rate of 20%. Such gain or loss generally will be treated as U.S. source gain or loss for U.S. foreign tax credit purposes.

Gain, if any, realized by a U.S. holder on the sale or other disposition of the shares or ADSs will be treated as U.S. source income for U.S. foreign tax credit purposes. Consequently if a Mexican withholding tax is imposed on the sale or disposition of L Shares, A Shares, or AA shares, a U.S. holder that does not receive significant foreign source income from other sources may not be able to derive effective U.S. foreign tax credit benefits in respect of these Mexican taxes. U.S. holders should consult their own tax advisors regarding the application of the foreign tax credit rules to their investment in, and disposition of, L Shares, A Shares or AA Shares.

Exchange of Shares

A U.S. holder's exchange of AA Shares or A Shares for L Shares will not constitute a taxable event for U.S. federal income tax purposes. An exchanging U.S. holder will have a tax basis in the L Shares equal to the basis such holder had in the exchanged AA Shares or A Shares. An exchanging U.S. holder's holding period for the L Shares will include the holding period such U.S. holder had in the AA Shares or A Shares before such shares were exchanged.

A U.S. holder's exchange of L Shares for AA Shares, pursuant to the option to exchange in respect of such L Shares, will not constitute a taxable event for U.S. federal income tax purposes. An exchanging U.S. holder will have a tax basis in the AA Shares received equal to the basis such holder had in the exchanged L Shares. A U.S. holder's holding period for AA Shares received in such an exchange will include the holding period such U.S. holder had in the L Shares prior to such exchange.

Information Reporting and Backup Withholding

Dividends on, and proceeds from the sale or other disposition of, the shares or ADSs paid to a U.S. holder generally may be subject to the information reporting requirements of the Code and may be subject to backup withholding unless the holder:

- establishes that it is a corporation or other exempt holder, or
- provides an accurate taxpayer identification number on a properly completed Internal Revenue Service Form W-9 and certifies that no loss of exemption from backup withholding has occurred.

The amount of any backup withholding from a payment to a holder will be allowed as a credit against the U.S. holder's U.S. federal income tax liability and may entitle such holder to a refund, provided that certain required information is furnished to the Service.

U.S. Tax Consequences for Non-U.S. holders

Distributions. A holder of shares or ADSs that is, with respect to the United States, a foreign corporation or a non-resident alien individual (a "non-U.S. holder") generally will not be subject to U.S. federal income or withholding tax on dividends received on shares or ADSs, unless such income is effectively connected with the conduct by the holder of a U.S. trade or business.

Dispositions. A non-U.S. holder of shares or ADSs will not be subject to U.S. federal income or withholding tax on gain realized on the sale of shares or ADSs, unless

- such gain is effectively connected with the conduct by the holder of a U.S. trade or business, or
- in the case of gain realized by an individual holder, the holder is present in the United States for 183 days or more in the taxable year of the sale and certain other conditions are met.

Information Reporting and Backup Withholding. Although non-U.S. holders generally are exempt from backup withholding, a non-U.S. holder may be required to comply with certification and identification procedures in order to establish its exemption from information reporting and backup withholding.

DOCUMENTS ON DISPLAY

We file reports, including annual reports on Form 20-F, and other information with the SEC pursuant to the rules and regulations of the SEC that apply to foreign private issuers. You may read and copy any materials filed with the SEC at its Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20459. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. You may also read and copy any materials we file with the SEC at the regional office of the SEC at Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. As a foreign private issuer, we will not be required to make filings with the SEC by electronic means until November 2002, although we may do so sooner. Any filings we make electronically will be available to the public over the Internet at the SEC's web site at http://www.sec.gov.

Item 11. Quantitative and Qualitative Disclosures about Market Risk

EXCHANGE RATE AND INTEREST RATE RISKS

We are exposed to market risk from changes in currency exchange rates and interest rates. Interest rate risk exists principally with respect to our indebtedness that bears interest at floating rates. We had P.45,374 million of indebtedness bearing interest at floating rates at December 31, 2001. Beginning in 2002, we have entered into long-term contracts to hedge against our floating rate peso-denominated indebtedness.

Exchange rate risk exists principally with respect to our indebtedness denominated in currencies other than Mexican pesos. As of December 31, 2001, indebtedness denominated in foreign currencies was P.52,363 million, of which P.52,145 million was denominated in U.S. dollars and P.218 million of indebtedness was denominated in other foreign currencies.

We regularly assess our exposure and monitor opportunities to manage these risks, for example through the use of financial instruments. From time to time we use financial instruments to manage our market risk exposures. Since late 2001, we have entered into hedging transactions with respect to our U.S. dollar-denominated indebtedness. We use these transactions, which may be foreign exchange forward contracts or options, to hedge against changes in the exchange rate between the U.S. dollar and the Mexican peso.

SENSITIVITY ANALYSIS DISCLOSURES

The potential loss in fair value of financial instruments held at December 31, 2001 that would have resulted from a hypothetical, instantaneous and unfavorable 10% change in currency exchange rates would have been approximately P.2,598 million. Such a change in currency exchange rates would also have resulted in additional interest expense of approximately P.508 million per year, assuming no change in the principal amount of such indebtedness, reflecting the increased costs in pesos of servicing foreign currency indebtedness. This sensitivity analysis assumes an instantaneous unfavorable 10% fluctuation in exchange rates affecting the foreign currencies in which our indebtedness is denominated.

The potential loss in fair market value of financial instruments held at December 31, 2001 that would have resulted from a hypothetical, instantaneous and unfavorable change of 100 basis points in the interest rate applicable to such financial instruments would have been approximately P.338 million. This effect would be fully attributable to the impact of the interest rate change on fixed-rate financial assets and liabilities. A hypothetical, instantaneous and unfavorable change of 100 basis points in the interest rate applicable to floating-rate financial assets and liabilities held at December 31, 2001 would have resulted in additional interest expense of approximately P.876 million per year, assuming no change in the principal amount of such indebtedness. The above sensitivity analyses are based on the assumption of an unfavorable 100 basis point movement of the interest rates applicable to each homogeneous category of financial assets and liabilities. A homogeneous category is defined according to the currency in which financial assets and liabilities are denominated and assumes the same interest rate movement with each homogeneous category. As a result, interest rate risk sensitivity analysis may overstate the impact of interest rate fluctuations for such financial instruments, as consistently unfavorable.

PART II

Item 13. Defaults, Dividend Arrearages and Delinquencies

None.

Item 14. Material Modifications to the Rights of Securities Holders and Use of Proceeds

In March 2001, as a result of the spin-off of América Móvil, we adjusted the conversion rate of our 4.25% Convertible Senior Debentures due 2004, from 21.07 ADSs per U.S.$1,000 principal amount of debentures to 33.81 ADSs per U.S.$1,000 principal amount of debentures.

PART III

Item 18. Financial Statements

See pages F-1 through F-42, incorporated herein by reference.

Item 19. Exhibits

Documents filed as exhibits to this Annual Report:

1.1 Amended and restated bylaws (*estatutos sociales*) of Teléfonos de México, S.A. de C.V., dated as of February 1, 2002, together with an English translation.

2.1 L Share Deposit Agreement (incorporated by reference to our registration statement on Form F-6 (File No. 333-11362)).

2.2 A Share Deposit Agreement (incorporated by reference to our registration statement on Form F-6 (File No. 333-12936) filed on November 28, 2000).

2.3 Indenture dated June 11, 1999 between Teléfonos de México, S.A. de C.V. and Citibank, N.A., as Trustee, and Officers' Certificate dated June 11, 1999, pursuant to Section 301 of the Indenture, with respect to the terms of the 4.25% Convertible Senior Debentures due 2004 (incorporated by reference to our annual report on Form 20-F for the year ended December 31, 1999 (File No. 1-10749)).

2.4 First Supplemental Indenture dated January 26, 2001 between Teléfonos de México, S.A. de C.V. and Citibank, N.A., as Trustee, with respect to the terms of the 8.25% Senior Notes due 2006 (incorporated by reference to our annual report on Form 20-F for the year ended December 31, 2000 (File No. 1-10749) filed on May 4, 2001).

2.5 Certificate, dated March 7, 2001, pursuant to Indenture, dated June 11, 1999, between Teléfonos de México, S.A. de C.V. and Citibank, N.A., as Trustee, with respect to the adjustment of the conversion rate of the 4.25% Convertible Senior Debentures due 2004.

3.1 Agreement dated December 20, 2000 between Carso Global Telecom, S.A. de C.V. and SBC International, Inc. (incorporated by reference to our annual report on Form 20-F for the year ended December 31, 2000 (File No. 1-10749) filed on May 4, 2001).

4.1 Concession dated March 10, 1976 between Teléfonos de México, S.A. de C.V. and the Mexican Ministry of Communications and Transportation, together with an English translation (incorporated by reference to our registration statement on Form F-1 (File No. 333-39893)).

4.2 Concession Amendment dated August 10, 1990 between Teléfonos de México, S.A. de C.V. and the Mexican Ministry of Communications and Transportation, together with an English translation (incorporated by reference to our registration statement on Form F-1 (File No. 333-39893)).

8.1 List of subsidiaries of Teléfonos de México, S.A. de C.V.

SIGNATURE

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the registrant certifies that it meets all of the requirements for filing on Form 20-F and has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: June 27, 2002

TELÉFONOS DE MÉXICO, S.A. DE C.V.

By: /s/ Adolfo Cerezo
Name: Ing. Adolfo Cerezo P.
Title: Chief Financial Officer

Exhibit Index

Exhibit Number	Description of Exhibit	Page Number
1.1	Amended and restated bylaws (*estatutos sociales*) of Teléfonos de México, S.A. de C.V., dated as of February 1, 2002, together with an English translation.	
2.5	Certificate, dated March 7, 2001, pursuant to Indenture, dated June 11, 1999, between Teléfonos de México, S.A. de C.V. and Citibank, N.A., as Trustee, with respect to the adjustment of the conversion rate of the 4.25% Convertible Senior Debentures due 2004.	
8.1	List of subsidiaries of Teléfonos de México, S.A. de C.V.	

REPORT OF INDEPENDENT AUDITORS

To the Stockholders of
Teléfonos de México, S.A. de C.V.

We have audited the accompanying consolidated balance sheets of Teléfonos de México, S.A. de C.V. and subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of income, changes in stockholders' equity and changes in financial position for each of the three years in the period ended December 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and in Mexico. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and the disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Teléfonos de México, S.A. de C.V. and subsidiaries at December 31, 2001 and 2000, and the consolidated results of their operations and changes in their financial position for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in Mexico, which differ in certain respects from those followed in the United States of America (see Note 18).

As described in Note 1 to the accompanying financial statements, effective January 1, 2000, the Company adopted the requirements of the new Mexican Accounting Principles Bulletin D-4, “Accounting for Income Tax, Asset Tax and Employee Profit Sharing”, issued by the Mexican Institute of Public Accountants. The effects are described in Note 15.

Mancera, S.C.
A Member Practice of
Ernst & Young Global

C.P.C. Fausto Sandoval Amaya

Mexico City, Mexico
February 15, 2002

TELÉFONOS DE MÉXICO, S.A. DE C.V. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands of Constant Pesos as of December 31, 2001, except for earnings per share)

	Year ended December 31,			
	2001	**2000**	**1999**	Millions of U.S. dollars, except for earnings per share **2001**
Operating revenues:				
Local service	P. 52,419,607	P. 49,292,474	P. 48,364,236	$ 5,735
Domestic long-distance service	28,502,881	26,736,848	24,186,567	3,118
International long-distance service	9,421,797	11,872,492	13,125,229	1,031
Interconnection service	14,708,101	13,079,028	6,069,257	1,609
Other	5,914,554	5,576,166	5,134,323	647
	110,966,940	106,557,008	96,879,612	12,140
Operating costs and expenses:				
Cost of sales and services	33,978,768	30,204,882	23,021,934	3,717
Commercial, administrative and general (exclusive of depreciation and amortization shown below)	17,137,824	17,228,123	16,636,022	1,875
Depreciation and amortization (Notes 5 to 7) (includes P.16,189,247 in 2001, P. 15,947,550 in 2000 and , P. 16,626,118 in 1999, respectively, not included in cost of sales and services)	17,258,752	17,673,235	18,490,007	1,888
	68,375,344	65,106,240	58,147,963	7,480
Operating income	42,591,596	41,450,768	38,731,649	4,660
Comprehensive financing cost :				
Interest income	(1,279,220)	(3,369,739)	(1,572,148)	(140)
Interest expense	6,997,237	10,428,753	11,226,242	766
Exchange gain, net	(1,158,524)	(84,924)	(1,057,113)	(127)
Monetary gain, net	(2,156,381)	(3,581,250)	(5,425,419)	(236)
	2,403,112	3,392,840	3,171,562	263
Income before income tax and employee profit sharing	40,188,484	38,057,928	35,560,087	4,397
Provisions for (Note 15) :				
Income tax	13,279,170	8,181,154	8,890,994	1,453
Employee profit sharing	2,985,115	3,451,825	2,834,653	326
	16,264,285	11,632,979	11,725,647	1,779
Income before equity interest in results of affiliates	23,924,199	26,424,949	23,834,440	2,618
Equity in results of affiliates	(430,082)	(327,454)	(121,108)	(48)
Income from continuing operations	23,494,117	26,097,495	23,713,332	2,570
Income from discontinued operations, net of income tax and employee profit sharing (Note 2)		1,538,274	4,869,289	
Net income	P. 23,494,117	P.27,635,769	P. 28,582,621	$ 2,570
Weighted average common shares outstanding (in millions) (Notes 1 and 14):				
Basic	13,541	14,669	15,092	13,541
Diluted	14,217	15,345	15,326	14,217
Income per share from continuing operations :				
Basic	1.735	1.779	1.571	0.190
Diluted	1.629	1.683	1.534	0.178
Net income per share:				
Basic	P. 1.735	P. 1.884	P. 1.894	$ 0.190
Diluted	P. 1.629	P. 1.784	P. 1.852	$ 0.178

See accompanying notes.

TELÉFONOS DE MÉXICO, S.A. DE C.V. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands of Constant Pesos as of December 31, 2001)

	December 31, 2001	December 31, 2000	Millions of U.S. dollars 2001
ASSETS			
Current assets:			
Cash and short-term investments	P. 8,814,029	P. 13,741,340	$ 964
Marketable securities (Note 3)	700,936	355,466	77
Accounts receivable, net (Note 4)	20,085,315	22,155,603	2,197
Prepaid expenses	1,427,102	1,508,184	156
Total current assets	31,027,382	37,760,593	3,394
Plant, property and equipment, net (Note 5)	114,454,386	111,205,486	12,519
Inventories, primarily for use in construction of the telephone plant	1,899,225	2,547,262	208
Licenses, net (Note 6)	608,643	645,890	67
Investments in affiliates and others (Note 7)	1,071,166	2,109,887	117
Intangible asset (Note 8)	7,571,437	8,612,605	828
Goodwill, net (Note 7)	278,807	907,324	30
Total assets	P. 156,911,046	P.163,789,047	$ 17,163
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities:			
Short-tem debt and current portion of long-term debt (Note 9)	P. 17,487,311	P. 46,059,201	$ 1,913
Accounts payable and accrued liabilities	17,307,169	13,756,139	1,893
Taxes payable	1,244,533	718,306	136
Total current liabilities	36,039,013	60,533,646	3,942
Long-term debt (Note 9)	52,254,382	31,628,886	5,716
Employee pensions and seniority premiums (Note 8)	5,323,729	6,779,611	582
Deferred taxes (Note 15)	11,523,792	11,896,597	1,261
Deferred credits (Note 10)	1,008,014	1,324,159	110
Total liabilities	106,148,930	112,162,899	11,611
Stockholders' equity (Note 14) :			
Capital stock:			
Historical	329,121	350,250	36
Restatement increment	26,440,583	27,689,401	2,892
	26,769,704	28,039,651	2,928
Premium on sale of shares	10,382,688	10,382,688	1,136
Retained earnings :			
Unappropriated earnings of prior years	59,003,203	50,513,841	6,454
Net income for the year	23,494,117	27,635,769	2,570
	82,497,320	78,149,610	9,024
Accumulated other comprehensive income items	(68,887,596)	(64,945,801)	(7,536)
Total stockholders' equity	50,762,116	51,626,148	5,552
Total liabilities and stockholders' equity	P. 156,911,046	P.163,789,047	$ 17,163

See accompanying notes.

TELÉFONOS DE MÉXICO, S.A. DE C.V. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION

(Amounts in thousands of Constant Pesos as of December 31, 2001)

	Year ended December 31,			Millions of U.S. dollars
	2001	2000	1999	2001
Operating activities:				
Net income	P 23,494,117	P.27,635,769	P.28,582,621	$ 2,570
Add (deduct) items not requiring the use of resources:				
Depreciation	16,752,861	17,332,976	18,214,952	1,833
Amortization	505,891	340,259	275,055	55
Deferred taxes	2,702,020	1,859,918	580,170	296
Equity in results of affiliates	430,082	327,454	121,108	48
Income from discontinued operations, net		(1,538,274)	(4,869,289)	
Adjustment to value of equity investments	881,618			96
Changes in operating assets and liabilities:				
Decrease (increase) in:				
Accounts receivable	2,070,288	(3,794,249)	(3,299,348)	226
Prepaid expenses	38,771	(522,513)	521,069	4
Increase (decrease) in:				
Employee pensions and seniority premiums:				
Reserve	3,556,858	3,536,433	3,427,027	389
Contributions to trust fund	(4,894,966)	(1,887,095)	(2,695,774)	(536)
Payments to employees	(3,041,014)	(2,605,701)	(2,257,143)	(333)
Accounts payable and accrued liabilities	3,551,030	3,584,031	1,125,628	389
Taxes payable	514,350	(1,341,473)	990,031	56
Deferred credits	(316,145)	754,395	(393,530)	(35)
Resources provided by operating activities of continuing operations	46,245,761	43,681,930	40,322,577	5,058
Financing activities:				
New loans	70,283,971	62,557,484	25,789,791	7,688
Repayment of loans	(72,912,305)	(35,542,956)	(25,733,363)	(7,975)
Effect of inflation and of exchange rate differences on debt	(5,318,060)	(4,928,482)	(6,418,336)	(582)
Decrease in capital stock and retained earnings due to purchase of Company's own shares	(13,715,382)	(24,672,187)	(8,932,578)	(1,500)
Cash dividends paid	(6,700,972)	(7,010,051)	(6,865,146)	(733)
Resources used in financing activities of continuing operations	(28,362,748)	(9,596,192)	(22,159,632)	(3,102)
Investing activities:				
Investment in plant, property and equipment	(22,944,770)	(18,457,936)	(10,436,911)	(2,510)
Reduction (investment) in inventories	784,094	(312,643)	(227,207)	86
Investment in affiliated companies	(127,196)	(1,426,018)	(461,580)	(14)
Investment in subsidiary companies		(216,759)	(370,568)	
Other investments	(522,452)	(161,707)	(1,300,842)	(57)
Resources used in investing activities of continuing operations	(22,810,324)	(20,575,063)	(12,797,108)	(2,495)
Net change in assets and liabilities of discontinued operations		(6,694,823)	(1,807,035)	
Net (decrease) increase in cash and short-term investments	(4,927,311)	6,815,852	3,558,802	(539)
Cash and short-term investments at beginning of year	13,741,340	6,925,488	3,366,686	1,503
Cash and short-term investments at end of year	P. 8,814,029	P.13,741,340	P. 6,925,488	$ 964

See accompanying notes.

TELÉFONOS DE MÉXICO, S.A. DE C.V. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Amounts in thousands of Constant Pesos as of December 31, 2001, except for dividends per share)

	Capital stock						Premium on sale of shares
	Series "AA"		Series "A"		Series "L"		
	Number	Amount	Number	Amount	Number	Amount	
Balances at January 1, 1999	4,326	P.29,173,454	429	P. 3,062,002	10,694	P.26,801,861	P. 10,382,688
Appropriation of earnings approved at stockholders' meetings held in March and April, 1999:							
Cash dividends paid at P.0.457 per share (P. 0.388 historical)							
Increase in reserve for purchase of Company's own shares							
Increase in legal reserve							
Cash purchase of Company's own shares					(500)	(130,619)	
Conversion of A shares to L shares			(60)	(405,091)	60	405,091	
Minority Interest							
Comprehensive income:							
Net Income for the year							
Other comprehensive income items:							
Minimum pension and seniority premium liability adjustment (Note 8)							
(Deficit) surplus from holding nonmonetary assets							
Comprehensive income							
Balances at December 31, 1999	4,326	29,173,454	369	2,656,911	10,254	27,076,333	10,382,688
Cumulative effect of accounting change (notes 1 and 15)							
Appropriation of earnings approved at stockholders' meetings held in March and April, 2000:							
Cash dividends paid at P.0.479 per share (P.0. 445 historical)							
Increase in legal reserve							
Cash Purchase of Company own shares				(2,747)	(939)	(2,094,250)	
Conversion of AA shares to L shares	(1,060)	(7,147,496)			1,060	7,147,496	
Conversion of A shares to L shares			(30)	(181,029)	30	181,029	
Comprehensive income:							
Net income for the year							
From continuing operations							
From discontinued operations							
Other comprehensive income items:							
Minimum pension and seniority premium liability adjustment (Note 8)							
Deficit from holding nonmonetary assets, net of deferred taxes							
Comprehensive income							
Spun-off stockholders' equity (Note 2)		(11,014,384)		(1,248,469)		(16,507,197)	
Balance at December 31, 2000	3,266	11,011,574	339	1,224,666	10,405	15,803,411	10,382,688
Appropriation of earnings approved at stockholder's meetings held in February and April 2001:							
Cash dividends paid at P. 0.498 per share (P. 0.490 historical)							
Increase in reserve for purchase of Company's own shares							
Increase in legal reserve							
Cash purchase of Company's own shares			(1)	(5,249)	(844)	(1,264,698)	
Conversion of L shares to AA shares	1,106	2,460,863			(1,106)	(2,460,863)	
Conversion of AA shares to L shares	(65)	(200,890)			65	200,890	
Conversion of A shares to L shares			(25)	(90,125)	25	90,125	
Comprehensive income:							
Net income for the year							
Other comprehensive income items:							
Minimum pension and seniority premium liability adjustment , net of deferred taxes (Note 8)							
Deficit from holding nonmonetary assets, net of deferred taxes							
Comprehensive income							
Balances at December 31, 2001 (Note 14)	4,307	P. 13,271,547	313	P. 1,129,292	8,545	P.12,368,865	P.10,382,688

See accompanying notes.

TELÉFONOS DE MÉXICO, S.A. DE C.V. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Amounts in thousands of Constant Pesos as of December 31, 2001, except for dividends per share)

	Retained earnings								
	Legal reserve	Reserve for purchase of Company's own shares	Unappropriated	Total	Accumulated other comprehensive income items	Comprehensive income	Total majority stockholders' equity	Minority interest	Total stockholders' equity
Balances at January 1, 1999..	P.14,271,061	P.17,524,070	P. 89,019,637	P.120,814,768	P.(54,930,720)		P.135,304,053		P. 135,304,053
Appropriation of earnings approved at stockholders' meetings held in March and April, 1999:									
Cash dividends paid at P.0.457 per share (P. 0.388 historical)................			(6,865,146)	(6,865,146)			(6,865,146)		(6,865,146)
Increase in reserve for purchase of Company's own shares......................		27,416,824	(27,416,824)						
Increase in legal reserve..	11,648		(11,648)						
Cash purchase of Company's own shares..		(8,480,073)	(321,886)	(8,801,959)			(8,932,578)		(8,932,578)
Conversion of A shares to L shares..									
Minority Interest..								P. 788,127	788,127
Comprehensive income:									
Net Income for the year..			28,582,621	28,582,621		P. 28,582,621	28,582,621	(243,723)	28,338,898
Other comprehensive income items:									
Minimum pension and seniority premium liability adjustment (Note 8)					902,080	902,080	902,080		902,080
(Deficit) surplus from holding nonmonetary assets...........................					(10,635,300)	(10,635,300)	(10,635,300)	218,181	(10,417,119)
Comprehensive income..						P. 18,849,401			
Balances at December 31, 1999..	14,282,709	36,460,821	82,986,754	133,730,284	(64,663,940)		138,355,730	762,585	139,118,315
Cumulative effect of accounting change (Notes 1 and 15)...........................			(13,840,359)	(13,840,359)	4,280,762		(9,559,597)		(9,559,597)
Appropriation of earnings approved at stockholders' meeting held in April, 2000:									
Cash dividends paid at P.0.479 per share (P.0.445 historical)...................			(7,010,051)	(7,010,051)			(7,010,051)		(7,010,051)
Increase in legal reserve..	84,098		(84,098)						
Cash purchase of Company's own shares..		(22,743,899)	168,709	(22,575,190)			(24,672,187)		(24,672,187)
Conversion of AA shares to L shares..									
Conversion of A shares to L shares..									
Comprehensive income..									
Net income for the year..									
From continuing operations..			26,097,495	26,097,495		P. 26,097,495	26,097,495		26,097,495
From discontinued operations..			1,538,274	1,538,274		1,538,274	1,538,274		1,538,274
Other comprehensive income items:..									
Minimum pension and seniority premium liability adjustment (Note 8)					(2,766,911)	(2,766,911)	(2,766,911)		(2,766,911)
Deficit from holding nonmonetary assets, net of deferred taxes............					(1,291,811)	(1,291,811)	(1,291,811)		(1,291,811)
Comprehensive income..						P. 23,577,047			
Spun-off stockholders' equity (Note 2)..	(44,228)	(8,622,874)	(31,123,741)	(39,790,843)	(503,901)		(69,064,794)	(762,585)	(69,827,379)
Balance at December 31, 2000..	14,322,579	5,094,048	58,732,983	78,149,610	(64,945,801)		51,626,148		51,626,148
Appropriation of earnings approved at stockholder's meetings held in February and April 2001:									
Cash dividends paid at P. 0.498 per share (P. 0.490 historical)..................			(6,700,972)	(6,700,972)			(6,700,972)		(6,700,972)
Increase in reserve for purchase of Company's own shares......................		5,256,174	(5,256,174)						
Increase in legal reserve..	51,373		(51,373)						
Cash purchase of Company's own shares..		(10,350,222)	(2,095,213)	(12,445,435)			(13,715,382)		(13,715,382)
Conversion of L shares to AA shares..									
Conversion of AA shares to L shares..									
Conversion of A shares to L shares..									
Comprehensive income:									
Net income for the year..			23,494,117	23,494,117		P. 23,494,117	23,494,117		23,494,117
Other comprehensive income items:									
Minimum pension and seniority premium liability adjustment , net of deferred taxes (Note 8)..					(1,415,682)	(1,415,682)	(1,415,682)		(1,415,682)
Deficit from holding nonmonetary assets, net of deferred taxes...........					(2,526,113)	(2,526,113)	(2,526,113)		(2,526,113)
Comprehensive income..						P. 19,552,322			
Balances at December 31, 2001 (Note 14)..	P. 14,373,952	P.	P. 68,123,368	P. 82,497,320	P. (68,887,596)		P. 50,762,116	P.	P.50,762,116

1. Description of the Business and Significant Accounting Policies

I. *Description of business*

Teléfonos de México, S.A. de C.V. and its subsidiaries (collectively “the Company” or "TELMEX") provide telecommunications services primarily in Mexico.

TELMEX obtains its revenues primarily from telecommunications services, including domestic and international long-distance and local telephone services, data transmission and internet services, as well as the interconnection of domestic long-distance operators', cellular telephone companies’ and local service operators’ networks with the TELMEX local network. The Company also obtains revenues from other activities related to its telephone operations, such as the publication of the telephone directory.

The amended concession under which the Company operates was signed on August 10, 1990. The concession runs through year 2026, but it may be renewed for an additional period of fifteen years. The concession defines, among other things, the quality standards for telephone service and establishes the basis for regulating rates.

Under the concession, the Company’s rates for basic telephone services are subject to a ceiling on the price of a “basket” of such services, weighted to reflect actual volume of each service during the preceding period. Within this aggregate price cap, the Company is free to determine the structure of its own rates. Approval of the Communications Ministry is not required for rates to take effect, although the Company must publish its rates and register them with the Ministry. In March 1999, the Federal Telecommunications Commission (COFETEL) established a new four years productivity factor of 1.11% per quarter that will apply to the price cap for the period from 1999 to 2002, as well as an initial adjustment of 1% in the rates for basic services that has been applied since March 1999.

At the end of 1996 the competition was allowed to provide domestic and international long-distance telephone services. In 1999 the competition began to provide basic local telephone service.

At an extraordinary shareholders’ meeting held on September 25, 2000, TELMEX’s shareholders approved the spin-off of the Company’s wireless telecommunication business and most of its international operations into América Móvil, S.A. de C.V. (América Móvil), to which certain specified assets, liabilities and equity were transferred (See Note 2 for additional information).

II. *Significant accounting policies*

The significant accounting policies and practices followed in the preparation of these financial statements are described below:

a) Consolidation:

The consolidated financial statements include the accounts of Teléfonos de México, S.A. de C.V. and its subsidiaries, all of which are wholly owned, except for three in which the Company holds equity interests ranging from 51% to 85%. Related minority interest is not significant to these financial statements. All the companies operate in the telecommunications sector or they provide services to companies operating in this sector.

All significant intercompany accounts and transactions have been eliminated in consolidation.

b) *Recognition of revenues:*

Revenues are recognized as they accrue.

Local service revenues are derived from new-line installation charges, monthly service fees, measured usage charges based on the number of calls made, and other service charges to subscribers, including, among others, charges for interconnecting fixed-system users with cellular users.

Revenues from domestic and international long-distance telephone services are determined on the basis of the duration of the calls and the type of service used. All these services are billed monthly, based on the rates authorized by the Ministry of Communications and Transportation (SCT), through COFETEL. International long-distance service revenues include the revenues earned under agreements with foreign telephone service providers or operators for the use of facilities in interconnecting international calls. These agreements specify the rates for the use of such international interconnecting facilities. These service revenues represent the net settlement between the parties.

In 1998 revenues obtained from U.S. long-distance service operators were conservatively recognized at the time payments were received because no agreement with respect to settlement rates had been reached at the end of the year. In 1999, based on the agreements reached, the Company recorded as revenue for the year, approximately U.S.$ 131.5 million, as a complement to the interconnection services provided in 1998.

Due to the important growth in the sale of prepaid telephone service cards and their potential in the future, effective in 2000, the Company changed its policy with respect to the recognition of revenues from these cards, providing for the deferral of revenue based on an estimate of the usage of time covered by the prepaid card.

As a result of this change in policy, revenues and net income for the year ended December 31, 2000 were decreased by P. 672,030 and P. 436,820, respectively.

c) *Recognition of the effects of inflation on financial information:*

The Company recognizes the effects of inflation on financial information as required by Mexican Accounting Principles Bulletin B-10 "*Accounting Recognition of the Effects of Inflation on Financial Information*", issued by the Mexican Institute of Public Accountants (MIPA). Consequently, the amounts shown in the accompanying financial statements and in these notes are expressed in thousands of constant pesos as of December 31, 2001. The December 31, 2001 restatement factor applied to the financial statements at December 31, 2000 and 1999 were 4.40% and 13.76%, respectively (which represent the rate of inflation from December 2000 and 1999 up to December 2001), based on the Mexican National Consumer Price Index (NCPI) published by Banco de México (the Central Bank) .

The NCPI (with an average base of 100 for the year of 1994) at the respective balance sheet dates was as follows:

December 31, 1998	275.038
December 31, 1999	308.919
December 31, 2000	336.596
December 31, 2001	351.418

Plant, property and equipment and construction in progress were restated as described in Note 5. Telephone plant and equipment depreciation is computed on the restated investment using the composite group method. All other assets are depreciated using the straight-line method based on the estimated useful lives of the related assets.

Inventories are valued at average cost and are restated on the basis of specific indexes. The stated value of inventories is similar to replacement value, not in excess of market.

Other nonmonetary assets were restated using adjustment factors obtained from the NCPI.

Capital stock, premium on sale of shares, and retained earnings were restated using adjustment factors obtained from the NCPI .

Other accumulated comprehensive income items includes the deficit from restatement of stockholders' equity, which consists of the accumulated monetary position loss at the time the provisions of Bulletin B-10 were first applied, which was P. 11,756,417 at December 31, 2001 and 2000, and of the result from holding nonmonetary assets, which represents the net difference between restatement by the specific indexation method (see Note 5) and restatement based on the NCPI.

The net monetary gain represents the impact of inflation on monetary assets and liabilities. The net monetary gain of each year is included in the statements of income as a part of the comprehensive financing cost.

Bulletin B-12 specifies the appropriate presentation of the statement of changes in financial position based on financial statements restated in constant pesos in accordance with Bulletin B-10. Bulletin B-12 identifies the sources and applications of resources representing differences between beginning and ending financial statement balances in constant pesos. In accordance with this bulletin, monetary and foreign exchange gains and losses are not treated as noncash items in the determination of resources provided by operations.

d) Short-term investments:

Short-term investments, represented basically by time deposits in financial institutions, are stated at market value.

e) Marketable securities:

Marketable securities, presented at market value, are held for trading purposes and include equity securities.

f) Equity investments in affiliates:

The investment in shares of affiliates is valued using the equity method. This accounting method consists basically of recognizing the investor's equity interest in the results of operations and in the result from holding nonmonetary assets of investees at the time such results are incurred (see Note 7).

g) Exchange differences:

Transactions in foreign currency are recorded at the prevailing exchange rate at the time of the related transactions. Foreign currency denominated assets and liabilities are translated at the prevailing exchange rate at the balance sheet date. Exchange rate differences are applied to income of the year.

h) Labor obligations:

Pension and seniority premium costs are recognized periodically during the years of service of personnel, based on actuarial computations made by independent actuaries, using the projected unit-credit method and financial hypotheses net of inflation, as required by Mexican Accounting Principles Bulletin D-3 *"Labor Obligations*", issued by the MIPA (see note 8). Termination payments are charged to income in the year in which the decision to dismiss an employee is made.

i) Income tax and employee profit sharing:

Requirements of the new Mexican Accounting Principles Bulletin D-4, "*Accounting for Income Tax, Asset Tax and Employee Profit Sharing"*, issued by the MIPA, went into effect on January 1, 2000. The new bulletin modifies the rules with respect to the determination and presentation of deferred income tax (deferred taxes). Basically, the new bulletin requires that deferred taxes be determined on virtually all temporary differences in balance sheet accounts for financial and tax reporting purposes, using the enacted income tax rate at the date of the financial statements. Through December 31, 1999, deferred taxes were recognized only on temporary differences that were considered to be non-recurring and that had a known turnaround time. Accordingly, the provision for income tax includes both the current year tax and the deferred portion. See Note 15 for additional information.

The new bulletin did not significantly affect how employee profit sharing is accounted for.

j) Basis of translation of financial statements of foreign subsidiaries:

The financial statements of the subsidiaries located in the United States of America (U.S.A). Guatemala and in Ecuador, which were transferred to América Móvil in the spin-off described in Note 2, represent approximately 18% of net revenues of the discontinued operations and approximately 39% of the total assets of the discontinued operations in 2000 (10% of net revenues of the discontinued operations in 1999) and together with the foreign subsidiaries that remain in TELMEX, were translated into Mexican pesos in conformity with Mexican Accounting Principles Bulletin B-15, "*Transactions in Foreign Currency and Translation of Financial Statements of Foreign Operations*", issued by the MIPA, as follows:

All balance sheet amounts, except for capital stock and retained earnings, were translated at the prevailing exchange rate at year-end; capital stock and retained earnings were translated at the prevailing exchange rate at the time capital contributions were made and earnings were generated. The statement of income amounts were translated at the prevailing exchange rate at the end of the reporting period. The effect of inflation and changes in exchange rates were not material and are presented as part of the result from holding nonmonetary assets.

Under Mexican GAAP, the financial statements of foreign subsidiaries and affiliates for periods prior to the most recent period are translated following the guidelines of Bulletin B-15. This bulletin requires that the financial statements of foreign subsidiaries and affiliates for periods prior to the most recent period be translated into constant Mexican pesos by restating the balances to constant units in the local currency using the inflation rate of the country in which the subsidiary or affiliate is located before being translated into Mexican pesos at the rate of exchange at the end of the reporting period.

In the Company's financial statements for each of the three years in the period ended December 31, 2001, such restatements were made based on the inflation in Mexico because the Company's investments in foreign subsidiaries and affiliates were not material in any of these periods.

k) *Comprehensive income*:

Requirements of Mexican Accounting Principles Bulletin B-4, "*Comprehensive Income"*, issued by the MIPA, went into effect on January 1, 2001. The Company's comprehensive income is the net income for the year presented in the statement of income, plus the minimum pension and seniority premium liability adjustment, the result from holding nonmonetary assets and the corresponding deferred taxes for the year applied directly to stockholders' equity.

l) *Earnings per share:*

TELMEX determined the earnings per share in conformity with Mexican Accounting Principles Bulletin B-14, *"Earnings per Share*", issued by the MIPA (see Note 14).

m) *Use of estimates:*

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

n) *Concentration of risk:*

The Company invests a portion of its excess cash in cash deposits in financial institutions with strong credit ratings and has established guidelines relating to diversification and maturities that maintain safety and liquidity. The Company has not experienced any important losses in its investments in marketable securities. TELMEX does not believe it has significant concentrations of credit risks in its accounts receivable, because the Company's customer base is geographically diverse, thus spreading the trade credit risk.

o) *Financial instruments:*

Requirements of the new Mexican Accounting Principles Bulletin C-2, "*Financial Instruments"*, issued by the MIPA, went into effect on January 1, 2001. This new bulletin establishes the basic rules to be observed by issuers of and investors in financial instruments when valuing, presenting and disclosing these instruments in their financial information. The new Bulletin C-2 requires that financial instruments (including derivatives) be recognized as assets and liabilities and that the gains and losses on such instruments be credited and charged, respectively, to income, except for asset and liability hedges. The Company contracts short-term exchange-rate hedges to offset the risk of loss on certain U.S. dollar denominated transactions. The gains or losses on these hedges are credited or charged to income using the accrual method, net of the gains or losses on the related assets and liabilities. In 2001, the observance of the requirements of this bulletin had no material effects, nor were there any equivalent transactions of importance in 2000.

p) *Convenience Translation:*

United States dollar amounts as of December 31, 2001 shown in the financial statements have been included solely for the convenience of the reader and are translated from pesos with purchasing power as of December 31, 2001, as a matter of mathematical computation only, at an exchange rate of P. 9.1423 to U.S.$ 1.00, the December 31, 2001 exchange rate. Such translations should not be construed as a representation that the peso amounts have been or could be converted into U.S. dollar at this or any other rate.

q) *Reclassifications:*

Certain amounts shown in the 2000 and 1999 financial statements have been reclassified for uniformity of presentation with 2001.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

2. Spin-Off

On September 25, 2000, TELMEX shareholders approved the spin-off of the wireless telecommunication business in Mexico and most of its international operations. As a result of the spin-off, América Móvil was established as a new Mexican corporation, independent of TELMEX, to which certain specified assets, liabilities and equity were transferred.

As a result of the spin-off, each TELMEX shareholder became a shareholder in América Móvil, and consequently, both companies are controlled by the same group of shareholders. Neither TELMEX nor América Móvil owns any capital stock in the other. The relationships between the two companies are limited to: (a) agreements related to the implementation of the spin-off; (b) commercial relationships in the ordinary course of business between a major fixed-line network operator and a major wireless network operator, such as interconnection and co-location of facilities; and (c) certain transitional arrangements that continued until the third quarter of 2001, when América Móvil had its own administrative structure in place.

In the accompanying financial statements, the revenues and expenses of the spun-off entities are shown in the statement of income as income of discontinued operations, net of income tax and employee profit sharing.

Assets and liabilities of the discontinued operations were transferred to América Móvil at their book value. The amount of stockholders' equity transferred to América Móvil in the spin-off was determined as the difference between the assets and liabilities transferred and was accounted for as a reduction in TELMEX's equity at the time of the spin-off.

Interest earned by a spun-off subsidiary from holding commercial paper and medium-term notes issued by TELMEX, which amounted to P. 2,295,004 for the nine-month period ended September 30, 2000 and P. 5,889,429 for the twelve-month period ended December 31, 1999, is included in income from discontinued operations.

The summarized statement of income for the nine-month period ended September 30, 2000 and twelve-month period ended December 31, 1999, are as follows :

	Nine-month period ended September 30, 2000	Twelve-month period ended December 31, 1999
Operating revenues	P. 20,401,766	P. 16,389,353
Operating costs and expenses	17,715,501	13,830,862
Operating income	2,686,265	2,558,491
Comprehensive financing income, net	1,184,475	3,287,282
Income before income tax and employee profit sharing	3,870,740	5,845,773
Provisions for:		
Income tax	1,884,687	1,176,580
Employee profit sharing	120,039	118,612
Income before equity in results of affiliates and minority interest	1,866,014	4,550,581
Equity in results of affiliates	(498,836)	74,982
Income before minority interest	1,367,178	4,625,563
Minority interest in loss of subsidiaries	171,096	243,726
Net income of discontinued operations	P. 1,538,274	P. 4,869,289

(Amounts in thousands of Constant Pesos as of December 31, 2001)

3. Marketable Securities

At December 31, 2001, the Company has investments in equity securities in the amount of P. 700,396 (P. 355,466 in 2000) for trading purposes. The Company included in the comprehensive financing cost for the year 2001, unrealized gains of P. 305,981 (unrealized losses of P. 1,457,874 in 2000) on the valuation of shares held. The realized net loss on the sale of equity investments for 2001 was P. 96,559 (realized net gain of P. 710,718 for 2000). Realized and unrealized gains and losses for the year ended December 31, 1999 had no material effect on the accompanying financial statements. During 2000, the Company invested in and sold Ecuadorian government bonds for U.S.$177.3 million, obtaining a gain of P. 929,143.

4. Accounts Receivable

Accounts receivable consist of the following:

	2001	2000
Subscribers	P. 18,364,566	P. 17,394,476
Net settlement receivables	709,409	1,298,323
Related parties	600,931	841,956
Other	1,804,051	5,282,742
	21,478,957	24,817,497
Less:		
Allowance for doubtful accounts	1,393,642	2,661,894
Total	P. 20,085,315	P. 22,155,603

Activity in the allowance for doubtful accounts for the years ended December 31, 2001, 2000 and 1999 was as follows:

	2001	2000	1999
Opening balance as of December 31	P. (2,661,894)	P. (3,112,785)	P. (2,091,982)
Additions charged to costs and expenses	(1,133,177)	(1,662,124)	(1,701,489)
Deductions to reserve for write-offs	2,401,429	2,113,015	680,686
Ending balance	P. (1,393,642)	P. (2,661,894)	P. (3,112,785)

In December 2000, TELMEX and its two major long-distance competitors agreed, among other things, on long-distance interconnection rates, thus settling existing disputes with respect to such rates. The parties also agreed to withdraw unresolved legal proceedings in connection with the matters in dispute. Under this agreement, in 2000 the competitors paid TELMEX U.S.$139 million (net of taxes) for interconnection services provided in the past. As a result, TELMEX reversed approximately P.1,775,000 of the allowance for doubtful accounts that it had conservatively recognized previously.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

5. Plant, Property and Equipment

a) Plant, property and equipment consist of the following:

	2001	2000
Telephone plant and equipment	P. 176,372,523	P. 173,876,040
Land and buildings	25,275,966	24,927,028
Computer equipment and other assets	20,936,070	19,604,915
	222,584,559	218,407,983
Less:		
Accumulated depreciation	120,146,075	117,637,865
Net	102,438,484	100,770,118
Construction in progress and advances to equipment suppliers	12,015,902	10,435,368
Total	P. 114,454,386	P. 111,205,486

Included in plant, property and equipment are the following assets held under capital leases:

	2001	2000
Assets under capital leases	P. 2,720,509	P. 1,678,089
Less accumulated depreciation	224,254	71,747
	P. 2,496,255	P. 1,606,342

b) Through December 31, 1996, items comprising the telephone plant were restated based on the acquisition date and cost, applying the factors derived from the specific indexes determined by the Company and validated by an independent appraiser registered with the National Banking and Securities Commission (NBSC).

Effective January 1, 1997, Bulletin B-10 eliminated the use of appraisals to present plant, property and equipment in the financial statements. This caption was restated as follows at December 31, 2001 and 2000:

- The December 31, 1996 appraised value of the imported telephone plant, as well as the cost of subsequent additions to such plant, were restated based on the rate of inflation in the respective country of origin and the prevailing exchange rate at the balance sheet date (i.e., specific indexation factors).

- The appraised value of land, buildings and other fixed assets of domestic origin at December 31, 1996, and the cost of subsequent additions to such assets were restated based on the NCPI.

At December 31, 2001 and 2000, approximately 51% of the value of the plant, property and equipment has been restated using specific indexation factors.

c) Following are the plant, property and equipment amounts at December 31, 2001 and 2000, restated on the basis of the 2001 NCPI (starting with the appraised values at December 31, 1996) to meet NBSC disclosure requirements with respect to the restatement of fixed assets based on specific indexation factors:

(Amounts in thousands of Constant Pesos as of December 31, 2001)

		2001		2000
Telephone plant and equipment………………………..	P.	221,971,435	P.	210,524,123
Land and buildings……………………………………..		25,275,966		24,927,028
Computer equipment and other assets………………..		24,689,649		22,509,082
		271,937,050		257,960,233
Less:				
Accumulated depreciation………………………………		152,030,632		142,756,072
Net……………………………………………………		119,906,418		115,204,161
Construction in progress and advances to equipment suppliers……………………………….		12,323,047		10,536,148
Total…………………………………………………	P.	132,229,465	P.	125,740,309

d) Depreciation of the telephone plant has been calculated at annual rates ranging from 3.3% to 16.7%. The rest of the Company's assets are depreciated at rates ranging from 3.3% to 33.3%. Depreciation charged to income was P. 16,752,861 in 2001, P. 17,332,976 in 2000 and P. 18,214,952 in 1999.

Because of the important progress and the technological advances in telecommunications equipment, the Company makes a periodic assessment of the estimated useful lives of its fixed assets, adjusting annual depreciation whenever it believes this to be appropriate. In 2001, the Company did not make change in useful lives. In 2000, the Company extended the useful lives of certain assets, thereby decreasing depreciation expense for 2000, as compared to 1999, by approximately P. 52,200.

The following table shows the changes in useful lives that were made in 2000:

	Useful Lives	
	Former	New
Various kinds of cable…………………	13	14 and 17
Poles……………………………………	16	21
Power equipment………………………	13	12
Microwave equipment…………………	12	11
PBX equipment…………………………	10	7
Optic terminal equipment……………....	10	11

6. Licenses

In May 1998, TELMEX acquired from the Mexican Government licenses to operate radio spectrum wave frequency bands to provide fixed wireless telephone services at a cost of P. 573,970. In December 1997, the Company also acquired from the Mexican Government concessions to operate radio spectrum wave frequency bands for point-to-point and point-to-multipoint microwave communications at a cost of P. 171,833. These costs are being amortized over a period of twenty years (see Note 15).

As of December 31, 2001 and 2000 licenses are as follows:

		2001		2000
Investment…………………………………………..…….	P.	745,803	P.	745,803
Accumulated amortization……………………..………..		137,160		99,913
Net…………………………………………………..…..	P.	608,643	P.	645,890

Amortization expense for the years ended December 31, 2001, 2000 and 1999 was P. 37,247 each.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

7. Investments in Affiliates and Others

a) An analysis of investments in affiliated and other companies at December 31, 2001 and 2000, that remain in TELMEX after the spin-off, and a brief description is as follows:

		2001		2000
Prodigy Communications Corporation………………...			P.	535,279
Williams Communications Group, Inc…………….……	P.	99,098		1,075,093
Technology and Internet, LLC…………………………..		320,567		390,228
The Telvista Company………………………………...		362,802		
Other………………………………………….…………		288,699		109,287
Total……………………………………………………….	P.	1,071,166	P.	2,109,887

From 1998 through 2000, the Company made an equity investment of U.S.$121.3 million in Prodigy Communications Corporation (Prodigy), which is engaged in providing internet services in U.S.A. In May 2000, other stockholders made capital contributions to Prodigy for more than the book value of the shares acquired. Although this resulted in a reduction in the equity interest of TELMEX of 8.1%, it increased the proportional book value of the investment by P. 700,983, which was credited to income of 2000. At December 31, 2000, the Company held a 10.3% equity interest in Prodigy. In November 2001, the Company sold to a related party its entire equity interest in Prodigy for U.S.$82.6 million, obtaining a gain of P. 103,099 on the transaction. At December 31, 2000, the goodwill of P. 983,674 generated on these transactions was being amortized over a period of five years. The remaining unamortized goodwill at the date of sale was included in the computation of the gain on the sale.

In May 1999, the Company entered into an agreement with Williams Communications Group, Inc. (Williams), which is engaged in providing telecommunications services in U.S.A., to acquire approximately 1% of the shares comprising the capital stock of Williams. This transaction was consummated in October 1999. Williams and TELMEX agreed to interconnect their fiber optics and long-distance networks in supplying international telecommunications services. Because the market value of this investment at December 31, 2001 had substantially decreased, the Company recognized in results of operations a decrease in the value of this asset of P. 881,618; the amount is included in comprehensive financing cost.

In 2001, TELMEX made capital contributions to Technology and Internet, LLC (TAI), equivalent to 50% of TAI's capital contributions, totaling U.S.$3 million (U.S.$103 million in 2000). TAI has made investments in companies engaged in e-commerce, located basically in the U.S.A. and Latin America.

In June 2001, TELMEX invested U.S.$47 million in The Telvista Company (Telvista), which represents 45% of its capital stock. Telvista is engaged in providing telemarketing services in the U.S.A.

In 2001, TELMEX made other investments in affiliated companies of U.S.$33 million, mostly in telecommunications interests.

Total equity investments in affiliated companies during 2001 aggregated approximately U.S. $83 million (U.S. $123 million in 2000). Goodwill derived from these investments was not material.

TELMEX's equity interest in the results of operations of affiliated companies represented a charge to operations of P. 430,082 in 2001 (P. 327,454 in 2000 and P. 121,108 in 1999).

(Amounts in thousands of Constant Pesos as of December 31, 2001)

Goodwill

An analysis of goodwill at December 31, 2001 and 2000 is as follows:

		2001		2000
Goodwill:………………………………………………………..				
Subsidiaries………………………………………………..	P.	552,164	P.	552,164
Affiliates………………………………………………..		42,036		983,674
		594,200		1,535,838
Accumulated amortization……………………………….		(315,393)		(628,514)
Net………………………………………………………..	P.	278,807	P.	907,324

Amortization expense in 2001, 2000 and 1999 was P. 291,448, P. 300,959 and P. 237,726 respectively.

Subsequent event

b) On January 16, 2002, TELMEX, together with Fortsmann Little & Co. (Fortsmann Little), located in the U.S.A., entered into a definitive agreement to make capital contributions of as much as U.S.$400 million each to XO Communications, Inc. (XO), a broadband services telecommunications supplier. Such contribution is expected to give TELMEX up to a 39% share in XO. The consummation of the agreement depends on, among other things, XO's complete restructuring of its balance sheet and the approval of the transaction by the competent authorities. XO will continue its negotiations with financial institutions and bond holders, in order to satisfy the restructuring requirements of its liability, contemplated by the definitive agreement with TELMEX and Fortsmann Little.

8. Employee Pensions and Seniority Premiums

Substantially all of the Company's employees are covered under defined benefit retirement and seniority premium plans.

Pension benefits are determined on the basis of compensation to employees in their final year of employment, their seniority, and their age at the time of retirement.

In 1990, the Company set up an irrevocable trust fund to cover the payment of these obligations. It adopted the policy of making annual contributions to the fund, which totaled P. 4,894,966 in 2001, P. 1,887,095 in 2000 and P. 2,695,774 in 1999. These contributions are deductible for Mexican corporate income tax purposes.

The transition liability, past services liability and variances in assumptions are being amortized over a period of twelve years, which is the estimated average remaining working lifetime of Company employees.

The most important information related to labor obligations is as follows:

Analysis of the net period cost:

		2001		2000		1999
Labor cost………………………………………	P.	1,841,541	P.	2,039,001	P.	1,780,823
Financial cost of projected benefit obligation..		3,748,978		3,706,803		3,157,936
Return on plan assets……………………….…		(3,175,865)		(3,247,868)		(2,525,297)
Amortization of past service costs……………		1,041,350		1,041,349		1,014,971
Amortization of variances in assumptions…...		100,854		(2,852)		(1,406)
Net period cost	P.	3,556,858	P.	3,536,433	P.	3,427,027

(Amounts in thousands of Constant Pesos as of December 31, 2001)

Reserve for employee pensions and seniority premiums**:**

	2001	2000
Projected benefit obligation………………………………..	P. 63,128,815	P. 56,353,130
Plan assets………………………………………………..	(54,056,488)	(46,160,465)
Transition liability………………………………………….	(7,254,315)	(8,268,520)
Actuarial loss to be amortized…………………………..	(11,030,677)	(6,730,723)
Past service costs and plan amendments………………..	(317,122)	(344,085)
Net projected asset………………………………………	(9,529,787)	(5,150,663)
Additional minimum liability………………………………	14,853,516	11,930,274
Reserve for employee pensions and seniority premiums………………………………………………	P. 5,323,729	P. 6,779,611
Accumulated benefit obligation…………………………	P. 59,380,217	P. 52,940,076
Intangible asset included on balance sheet…………….	P. 7,571,437	P. 8,612,605
Minimum pension and seniority premium liability adjustment on stockholders' equity……………	P. 7,282,079	P. 3,317,669

The increase in the unamortized actuarial loss in 2001 of approximately P. 4,300,000 is attributable basically to the increase in the projected benefit obligation resulting from the increase in salaries over what was estimated at the beginning of the year. The actuarial loss in 2000 of approximately P. 3,200,000 is attributable primarily to the negative results of plan assets and the positive behavior of the projected benefit obligation. The negative behavior of plan assets in 2000 was due largely to the pervasive decline in the value of securities traded on the Mexican Stock Exchange.

In the last quarter of 2000, the Company decided to review and modify the actuarial assumptions used for several years to make the actuarial computations of the projected benefit obligation and the accumulated benefit obligation at December 31, 2000, as well as the net period cost for 2001. The net period cost is systematically computed in a prospective manner at the beginning of the year. The changes in actuarial assumptions were based on objective judgmental elements considered by both the Company and the independent actuary, including past experience of the Company and of the country in recent years, as well as expectations with respect to the future. Also, in the final quarter of 2001, because of the general economic situation, the Company decided to review and modify the annual rate of return on the fund, which was reduced from 7.84% to 6.84%.

The rates used in the actuarial studies were:

	2001	2000	1999
Discount of labor obligations:			
First year……………………………	6.84%	6.84%	6.90%
Long-term average……………….	5.85%	5.85%	4.91%
Increase in salaries:			
First year…………………………..	1.85%	1.85%	0.88%
Long-term average……………….	0.96%	0.96%	1.42%
Annual return from the fund………	6.84%	6.84%	6.90%

The changes in financial assumptions resulted in a decrease of approximately P. 1,200,000 in the net period cost of 2001, compared to the cost that would have been determined on the basis of the previous actuarial assumptions. The change represented a decrease of approximately P. 6,160,000 in the projected benefit obligation, the accumulated benefit obligation, and in the charge to stockholders' equity for labor obligations at December 31, 2000.

At December 31, 2001, 66% (71% in 2000) of plan assets were invested in fixed-income securities and 34% (29% in 2000) in variable-income securities.

9. Long-term Debt

Long-term debt consists of the following:

	Weighted average interest rates at December 31,		Maturities from 2002 through	Balance at December 31,	
	2001	**2000**		**2001**	**2000**
Debt denominated in foreign currency:					
Convertible senior debentures (1)	4.2%	4.2%	2004	P. 9,142,300	P. 10,022,087
Senior notes (2)	8.2%		2006	13,713,450	
Banks	3.1%	7.4%	2011	23,983,947	22,234,617
Suppliers' credits	3.3%	7.6%	2022	2,832,010	3,884,871
Financial leases	2.9%	7.2%	2006	2,527,044	1,503,621
Mexican Government	2.8%	7.0%	2006	164,186	212,691
Total				52,362,937	37,857,887
Debt denominated in Mexican pesos:					
Medium-term notes		20.2%			6,264,000
Commercial paper	8.0%	18.0%	2002	8,675,122	26,814,431
Domestic senior notes (“Certificados bursátiles”)	11.6%		2007	4,250,000	
Banks	7.2%	18.1%	2004	4,440,000	6,682,293
Financial leases	8.9%	19.9%	2004	13,634	69,476
Total				17,378,756	39,830,200
Total debt				69,741,693	77,688,087
Less short-term debt and current portion of long-term debt				17,487,311	46,059,201
Long-term debt				P. 52,254,382	P. 31,628,886

The above-mentioned rates are subject to variances in international and local rates and do not include the effect of the Company’s agreement to reimburse certain lenders for Mexican taxes withheld. The Company’s weighted average cost of borrowed funds at December 31, 2001 (including interest, fees and reimbursement of such lenders for Mexican taxes withheld) was approximately 7.5% (12.2% at December 31, 2000).

Short-term debt as of December 31, 2001 amounted P. 11,941,377 (P. 41,462,596 in 2000), comprised of P. 8,675,123 of commercial paper (P. 26,814,431 of commercial paper and P. 6,264,000 of medium-term notes in 2000) and P. 3,266,254 of banks (P. 8,384,165 in 2000), with an weighted average interest rate of 7.7% (17.7% in 2000).

An analysis of the foreign currency denominated debt at December 31, 2001 is as follows:

	Foreign currency (in thousands)	Exchange rate at December 31, 2001 (in units)	Mexican peso equivalent
U.S. dollar…………………………….	5,703,734	P. 9.1423	P. 52,145,247
French franc………………………….	176,482	1.2335	217,690
Total…………………………………..			P. 52,362,937

(Amounts in thousands of Constant Pesos as of December 31, 2001)

(1) On June 11, 1999, the Company issued U.S.$ 1,000 million of convertible senior debentures. The debentures are convertible to common stock at the option of the holders, at any time prior to their maturity into American Depositary Shares (ADSs), each representing 20 TELMEX "L" shares. The conversion ratio at December 31, 2001, after adjustments due to a stock split and the spin-off, is 33.81 "L" shares ADSs per U.S.$ 1,000 principal amount of the convertible debentures, subject to adjustments under certain circumstances.

Should any person or group (other than the present controlling stockholders) acquire 50% or more of the issuer's voting shares, the holders of the convertible debentures may ask TELMEX to repurchase the convertible debentures, for 100% of the principal amount plus unpaid accrued interest through the repurchase date.

The maturity date of the convertible debentures is June 15, 2004. The debentures bear 4.25% annual interest, payable semiannually. In 2001, 2000 and 1999, accrued interest on these debentures aggregated P. 436,479, P. 435,733 and P. 281,889, respectively.

(2) On January 26, 2001, TELMEX issued senior notes for U.S.$ 1,000 million, maturing in 2006 and bearing 8.25% annual interest payable semiannually. Additionally, on May 8, 2001, TELMEX issued supplemental senior notes for U.S.$ 500 million with similar characteristics. In 2001, accrued interest on the bonds was P. 1,057,636.

On September 25, 2000, one of the entities that was part of the spin-off of América Móvil held P. 17,996,128 of medium-term notes and commercial paper issued by TELMEX. On December 31, 2000, this entity held P. 10,554,571 of these financial instruments, and interest expense for the years ended December 31, 2000 and 1999 were P. 3,112,924 and P. 5,889,429, respectively (See Note 2).

At December 31, 2001, the Company has long-term lines of credit with certain banks that do not require compensating balances. Origination fees range from 0.25% to 1.5% of available balances. The unused committed lines of credit at December 31, 2001 totaled approximately P. 6,120,000, at a floating interest rate of approximately LIBOR plus one point at the time of use.

As a part of its currency hedging strategy, the Company utilizes forward contracts to minimize the impact of exchange rate fluctuations on U.S. dollar denominated transactions. During 2001, the Company entered into short-term exchange hedges which, at December 31, 2001, cover liabilities of U.S.$2,740 million. In 2001, P. 462,557 was charged to income on these contracts to offset exchange differences. In 2000 a loss of P. 41,417 and in 1999 a gain of P. 29,933 on these contracts, were recognized in the income statement as an offset against exchange differences.

Long-term debt maturities at December 31, 2001 are as follows:

Year ended December 31,	Amount
2003…………………………..	P. 8,666,212
2004…………………………..	17,858,460
2005…………………………..	3,444,846
2006…………………………..	16,329,101
2007 and beyond…………….	5,955,763
Total…………………………..	P. 52,254,382

Subsequent event

On February 15, 2002, TELMEX made two placements of domestic senior notes ("Certificados bursátiles") for P. 850 million and P. 1,650 million with maturities of three and five years, respectively, bearing interest at the 91-day CETES rate plus one point and the 182-day CETES rate plus 0.8%, respectively.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

10. Deferred Credits

Deferred credits consist of the following at December 31, 2001 and 2000:

	2001		2000	
Advance billings………………………...	P.	995,444	P.	1,316,175
Advances from subscribers and others		12,570		7,984
Total…………………………………...	P.	1,008,014	P.	1,324,159

11. Foreign Currency Position and Transactions

a) At December 31, 2001, TELMEX and its Mexican subsidiaries have a net foreign currency short position of U.S.$5,650 million (net foreign currency short position of U.S.$3,648 million at December 31, 2000).

The prevailing exchange rate at December 31, 2001 was P. 9.14 per U.S. dollar (P. 9.60 per U.S. dollar at December 31, 2000). At February 15, 2002, the date of the issuance of these consolidated financial statements, the exchange rate of the Mexican peso relative to the U.S. dollar was P. 9.06 per U.S. dollar.

b) In the years ended December 31, 2001, 2000 and 1999, TELMEX and its Mexican subsidiaries had the following transactions denominated in foreign currencies. Currencies other than the U.S. dollar were translated to U.S. dollars using the average exchange rate for the year.

	Million of dollars					
	2001		2000		1999	
Net settlement revenues……..	U.S.$	253	U.S.$	516	U.S.$	534
Interest expense……………...		284		165		146
Operating expenses………….		136		139		124

12. Commitments and Contingencies

a) The Company leases certain equipment used in its operation under capital leases. At December 31, 2001, the Company had the following commitments under noncancelable leases:

Year ended December 31,		
2002……………………………………………..	P.	606,288
2003……………………………………………..		739,940
2004……………………………………………..		674,545
2005……………………………………………..		499,487
2006……………………………………………..		102,435
Total……………………………………………..		2,622,695
Less interest…………………………………….		82,017
Present value of net minimum lease payments		2,540,678
Less current installment………………………….		587,143
Long-term obligation at December 31, 2001	P.	1,953,535

b) At December 31, 2001, the Company has noncancelable commitments of approximately P. 2,450,000 (P. 3,763,000 in 2000) for the purchase of equipment.

Payments made under the purchase agreements were P.4,197,136 in 2001, P. 4,393,188 in 2000 and P. 4,393,255 in 1999.

c) At December 31, 2001, there are no outstanding letters of credit (P. 6.264 in 2000, which were issued to foreign suppliers for the purchase of materials and supplies).

d) In February 1998, the Federal Commission of Economic Competition (COFECO) determined that Teléfonos de México, S.A. de C.V. has substantial power in what it referred to as five telecommunications markets so that, in conformity with Article 63 of the Federal Telecommunications Act, COFETEL may impose specific obligations with respect to rates charged and quality of services and information.

The Company's external lawyers who are handling this matter are of the opinion that this finding is unjustified. Consequently, Teléfonos de México, S.A. de C.V. filed an appeal in the Federal District Court and obtained protection and shelter under Mexican Federal law. COFETEL, based on the COFECO ruling, which was later reversed, handed down a new ruling imposing certain specific obligations on Teléfonos de México, S.A. de C.V. The ruling of COFETEL was appealed in a Federal Court and is still pending. Also, the SCT imposed a fine on Teléfonos de México, S.A. de C.V. for not complying with certain obligations. The fine was also appealed and the matter is pending. In 2001, COFECO upheld its previous ruling and handed down a new ruling supporting the findings with respect to the substantial power that Teléfonos de México, S.A. de C.V exercises over five telecommunications markets. Teléfonos de México, S.A. de C.V. has also appealed in a Federal District Court.

As a result of these findings, COFECO has initiated other proceedings against Teléfonos de México, S.A. de C.V. that are also being appealed.

e) In December 1995, a competitor that provides cellular telephone services reported Teléfonos de México, S.A. de C.V. to COFECO for alleged monopolistic practices.

In July 2001, the COFECO ruled that Teléfonos de México, S.A. de C.V. was responsible for monopolistic practices. Teléfonos de México, S.A. de C.V. filed an appeal for reconsideration against the ruling, but the appeal was declared unfounded and denied.

Currently, the respective defense against the denial is being prepared.

f) Under Mexican law, Teléfonos de México, S.A. de C.V. remains jointly and severally liable for any obligations transferred to América Móvil pursuant to the spin-off for a period of three years beginning on September 25, 2000, the spin-off date. Such liability, however, does not extend to any obligation with a creditor that has given its express consent relieving Teléfonos de México, S.A. de C.V. of such liability and approving the spin-off. In addition, Teléfonos de México, S.A. de C.V. has the following specific obligations:

- Teléfonos de México, S.A. de C.V. has guaranteed indebtedness of ATL Algar Telecom Leste, S.A. under certain credit facilities, for up to U.S.$104.3 million. América Móvil has agreed to indemnify Teléfonos de México, S.A. de C.V. against any liability under these guarantees.

- Teléfonos de México, S.A. de C.V. has guaranteed certain obligations of Iberbanda, S.A., (formerly FirstMark Comunicaciones España, S.A.). The guarantee is limited to 4,606.3 million Spanish pesetas. América Móvil has agreed to indemnify Teléfonos de México, S.A. de C.V. for any liability derived from these guarantees.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

13. Related Parties

In the years ended December 31, 2001, 2000 and 1999, the Company had the following significant transactions with related parties:

	2001	2000	1999
Purchase of materials, inventories and fixed assets (1).	P. 6,745,360	P. 6,149,795	P. 2,008,321
Payment of insurance premiums, fees for administrative and operating services and others (2)...	1,834,149	2,002,447	1,103,507
Payment of CPP interconnection fees (3)……………….	7,011,828	5,970,070	1,875,964
Donations to a non-profit social welfare organization….	500,013	1,302,701	1,141,753
Discount on sale of doubtful accounts receivable………			555,857
Sale of materials, inventories and fixed assets (4)……..	416,178	492,448	475,009
Sale of long distance and other telecommunication services (5)……………………………...…………...	3,171,635	2,636,968	1,327,190

(1) Includes P. 5,588,619 in 2001 (P. 4,921,823 in 2000 and P. 1,374,070 in 1999) for fiber optic and satellite network services with a subsidiary of the Condumex group.

(2) In 2001, includes P. 471,339 for insurance premiums with Seguros Inbursa, S.A. (P. 543,521 in 2000 and P. 305,188 in 1999), as well as P. 306,132 (P. 375,322 in 2000 and P. 640,149 in 1999) for fees paid for administrative and operating services to technology partners.

(3) Interconnection fee from the "Calling Party Pays" program (CPP); incoming calls from a fixed line telephone to a wireless telephone paid to a subsidiary of América Móvil. In 2000, this income is included in income of discontinued operations, eliminating the effect at net income level.

(4) Includes P. 164,078 in 2001 (P. 159,960 in 2000 and P. 106,476 in 1999) from the sale of construction materials to a subsidiary of the Condumex group.

(5) Interconnection revenues from interconnection of outgoing calls from the wireless network of a subsidiary of América Móvil to the fixed line network.

At December 31, 2001, TELMEX had amounts due to a subsidiary of the Condumex group and a subsidiary of América Móvil of P. 1,123 million and P. 581 million, respectively (P. 206 million and P. 477 million in 2000).

TELMEX purchases materials or services from a variety of subsidiaries of Grupo Carso, S.A. de C.V. TELMEX purchases these materials and services on terms no less favorable than it could obtain from unaffiliated parties, and would have access to other sources if its affiliates ceased to provide them on competitive terms. Additionally, TELMEX receives insurance and banking services provided by Grupo Financiero Inbursa, S.A. de C.V. and its subsidiaries (see table above).

14. Stockholders' Equity

a) At an extraordinary stockholders' meeting held on September 25, 2000, as described in Note 2, it was decided to spin-off the wireless telecommunications segment and most of its international transactions. When the spin-off occurred and TELMEX made its capital contribution to América Móvil, the capital stock of both TELMEX and América Móvil was represented by an equal number of shares of each of the three series, without any change in the number of shares comprising the capital stock of TELMEX.

At December 31, 2001, capital stock is represented by 13,165 million common shares with no par value, representing the fixed capital (14,010 million in 2000), issued and outstanding. An analysis is as follows:

(Amounts in thousands of Constant Pesos as of December 31, 2001)

	2001	2000
4,307 million Series "AA" shares (3,266 million in 2000)	P. 13,271,547	P. 11,011,574
313 million Series "A" shares (339 million in 2000)	1,129,292	1,224,666
8,545 million Series "L" shares (10,405 million in 2000)	12,368,865	15,803,411
Total	P. 26,769,704	P. 28,039,651

Series "AA" shares, which may be subscribed only by Mexican individuals and corporate entities, must represent at all times no less than 20% of capital stock and no less than 51% of the common shares. Common Series "A" shares, which may be freely subscribed, must account for no more than 19.6% of capital stock and no more than 49% of the common shares. Series "AA" and "A" shares combined may not represent more than 51% of capital stock. The combined number of Series "L" shares, which have limited voting rights and may be freely subscribed, and Series "A" shares may not exceed 80% of capital stock.

Since January 1, 2001, the Company's bylaws have contemplated the possibility of the holders of Series "L" shares exchanging such shares, in certain circumstances, for Series "AA" shares. In 2001, a total of 1,106 million Series "L" shares were exchanged for Series "AA" shares.

b) In 1994, TELMEX initiated a program to purchase its own shares. For this purpose, in accordance with the Securities Trading Act, the Company appropriated retained earnings to set up a reserve to purchase its own shares. A charge is made to the reserve for the excess cost of the shares purchased over the portion of capital stock represented by the shares acquired.

In March 1999, the stockholders approved an increase of P.27,416,824 in the reserve for the purchase of the Company's own shares to acquire up to 1,600 million additional shares to those previously authorized. In 1999, the Company acquired 500 million series "L" shares, for P.8,610,692 (P. 7,116,910 historical). During 2000, the Company purchased 938.6 million Series "L" shares for P. 24,822,456 (P. 23,159,299 historical) and 761 thousand Series "A" shares for P. 18,440 (P. 17,519 historical) .

In February 2001, the stockholders approved an increase in the reserve to purchase Company's own shares, bringing the balance of the reserve to P. 10,350,222 (P. 10,008,918 historical). During 2001, the Company acquired 843.7 million Series "L" shares for P. 13,692,105 (P. 13,400,776 historical) and 1.5 million Series "A" shares for P. 23,277 (P. 22,715 historical).

Under the Securities Trading Act, amended starting June 1, 2001, it is no longer required to create a reserve for the purchase on one' own shares. The Company's own shares purchased since this change were acquired using the reserve until it was eliminated, after which shares were acquired using unappropriated earnings in the amount the corresponding shares purchased exceeded capital stock.

c) In conformity with the Mexican Corporations Act, at least 5% of net income of the year must be appropriated to increase the legal reserve. This practice must be continued each year until the legal reserve reaches at least 20% of capital stock issued and outstanding.

c) Earnings per share are obtained by dividing net income for the year by the average weighted number of shares issued and outstanding during the period. To determine the average weighted number of shares issued and outstanding in 2001, 2000 and 1999, the shares acquired by the Company have been excluded from the computation.

The diluted earnings per share in 2001, 2000 and 1999, were determined considering the effect of the shares that may be delivered (potentially dilutive shares) as a result of the convertible senior debentures described in Note 9. The computation was made by deducting from net income for the year, the net comprehensive financing income (including interest expense, exchange gain differences and monetary gain), net of income tax and employee profit sharing, derived from the convertible debentures. The adjusted income was divided by the average weighted number of shares issued and outstanding, taking into account the number of shares that could be capitalized.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

An analysis is as follows:

	2001	2000	1999
Income from continuing operations			
Income per basic share:			
Income from continuing operations………………	P. 23,494,117	P. 26,097,495	P. 23,713,332
Weighted average number of shares issued and outstanding (millions)……………………………	13,541	14,669	15,092
Income per basic share (in pesos)…………………	P. 1.735	P. 1.779	P. 1.571
Income per diluted share:			
Income from continuing operations………………	P. 23,494,117	P. 26,097,495	P. 23,713,332
Comprehensive financing income (net of income tax and employee profit sharing)……..………	(339,875)	(265,678)	(206,012)
Adjusted income……………………………………	P. 23,154,242	P. 25,831,817	P. 23,507,320

	2001	2000	1999
Weighted average number of shares issued and outstanding (millions)…………………..	13,541	14,669	15,092
Add:			
Potentially dilutive shares……………………..	676	676	234
Weighted average number of diluted shares issued and outstanding (millions)……………	14,217	15,345	15,326
Income per diluted share (in pesos)…………..	P. 1.629	P. 1.683	P. 1.534

Net income	2001	2000	1999
Income per basic share:			
Net income………………………………………..	P. 23,494,117	P. 27,635,769	P. 28,582,621
Weighted average number of shares issued and outstanding (millions)…………………………..	13,541	14,669	15,092
Income per basic share (in pesos)…………………	P. 1.735	P. 1.884	P. 1.894
Income per diluted share:			
Net income………………………………………..	P. 23,494,117	P. 27,635,769	P. 28,582,621
Comprehensive financing income (net of income tax and employee profit sharing)………………..	(339,875)	(265,678)	(206,012)
Adjusted income…………………………………..	P. 23,154,242	P. 27,370,091	P. 28,376,609
Weighted average number of shares issued and outstanding (millions)…………………….	13,541	14,669	15,092
Add:			
Potentially dilutive shares……………………….	676	676	234
Weighted average number of diluted shares issued and outstanding (millions)………………	14,217	15,345	15,326
Income per diluted share (in pesos)……………	P. 1.629	P. 1.784	P. 1.852

(Amounts in thousands of Constant Pesos as of December 31, 2001)

e) At December 31, 2001, accumulated other comprehensive income items include the effects of labor obligations and the deficit from the restatement of stockholders' equity, net of deferred taxes, of P. 4,733,351 and P. 64,154,245, respectively (P. 3,317,669 and P. 61,628,132 in 2000).

15. Income Tax, Asset Tax and Employee Profit Sharing

a) The Ministry of Finance and Public Credit authorized TELMEX to consolidate the group tax returns effective January 1, 1995. The Instituto Tecnológico de Teléfonos de México, S.C., Fundación Telmex, A.C., and the subsidiaries acquired during the year are excluded from this tax consolidation.

b) The asset tax is a minimum tax levied on the average value of most assets net of certain liabilities. Income tax may be credited against the asset tax so that the asset tax is payable only to the extent that it exceeds income tax. The asset tax on continuing operations for the years ended December 31, 2001, 2000 and 1999 was P. 2,612,247, P. 2,455,054 and P. 2,453,412, respectively. In all three years TELMEX credited against these amounts the income tax paid in such years.

c) The corporate income tax rate for 2001, 2000 and 1999 was 35%. However, corporate taxpayers had the option of deferring a portion, so that the tax payable for those years represented 30% of taxable income. The earnings on which taxes were deferred must be controlled in a so-called "net reinvested tax profit" account ("CUFINRE"), to clearly identify the earnings on which the taxpayer has opted to defer payment of corporate income tax. Effective January 1, 2002, the above-mentioned option of deferring a portion of income tax was eliminated.

Since the Company opted for this tax deferral, earnings will be considered to be distributed first from the "CUFINRE" account, and any excess will be distributed from the "net tax profit" account ("CUFIN") so as to pay the 5% deferred tax.

Any distribution of earnings in excess of the above-mentioned account balances will be subject to payment of the enacted corporate income tax rate.

In addition, from January 1, 1999 through December 31, 2001, cash dividends obtained by individuals or residents abroad from corporate entities in Mexico, were subject to a 5% withholding tax on the amount of the dividend multiplied by 1.5385 (1.515 for dividends paid from the determined balance of the "CUFIN" account at December 31, 1998).

d) The cumulative effect of the adoption of the new Bulletin D-4 at the beginning of 2000 was P. 9,559,597. Such amount was charged to stockholders' equity. The Company simultaneously recognized a liability for deferred taxes, without restructuring the financial statements of prior years.

Had the requirements of the new Bulletin D-4 been in force in 1999, income from continuing operations for such year would have been increased by P. 1,020,990 and net income would have been decreased by P. 350,529, respectively. Income from continuing operations and net income per basic share would have been P. 1.639 and P. 1.871, respectively, and earnings per diluted share would have been P. 1.600 and P.1.829, respectively.

e) An analysis of income tax provisions is as follows:

	2001	**2000**	**1999**
Current year……	P. 10,577,150	P. 6,321,236	P. 8,310,824
Deferred tax, net of related monetary position gain of P. 1,443,641 (P. 1,231,852 in 2000)	2,702,020	1,859,918	580,170
Total……	P. 13,279,170	P. 8,181,154	P. 8,890,994

(Amounts in thousands of Constant Pesos as of December 31, 2001)

A reconciliation of the statutory Mexican income tax rate and the Company's provision for effective income tax rate is as follows:

	% Year ended December 31, 2001	2000	1999
Statutory income tax rate	35.0	35.0	35.00
Depreciation …………….	(0.5)	(8.5)	(4.6)
Financing costs…………	(2.2)	(4.2)	(4.9)
Other……………………..	0.7	(0.8)	(0.5)
Effective tax rate………..	33.0	21.5	25.0

In 2001, the decrease in the depreciation reconciling item was derived basically from a change in the depreciation method, in conformity with current tax legislation.

f) The temporary differences on which the Company recognized deferred taxes in the years ended December 31, 2001 and 2000, were as follows:

	2001	2000
Deferred tax asset :		
Allowance for doubtful accounts and slow-moving inventories……………………………………	P. 537,158	P. 825,631
Tax loss carry forwards………………………………..	17,306	41,540
Deferred income………………………………………..	124,768	445,754
Liability reserves……………………………………….	247,717	75,117
Excess cost over appraised value of Federal Microwave network………………………………….		14,501
	926,949	1,402,543
Deferred tax liability:		
Fixed assets…………………………………………….	(11,201,916)	(10,956,766)
Inventories………………………………………………	(285,152)	(313,541)
Licenses…………………………………………………	(155,051)	(226,062)
Pensions and seniority premiums……………………	(808,622)	(1,802,771)
	(12,450,741)	(13,299,140)
Net deferred tax (liability)………………………………..	P. (11,523,792)	P. (11,896,597)

On January 1, 2002, an annual one-percentage point decrease in the income tax rate was approved, starting in 2003, so that in 2005 the rate will be 32%. The effect this change will have in succeeding years has not yet been determined, although it is not expected to be material.

g) The Company is required by law to pay employee profit sharing to its employees in addition to their contractual compensation and benefits. The statutory rate for employee profit sharing in 2001, 2000 and 1999 was 10%, based on taxable income of the company for which the employee provides services after eliminating certain effects of inflation and the restatement of depreciation expense.

h) At December 31, 2001, the balance of the restated contributed capital account (CUCA), the net tax profit account (CUFIN) and the net reinvested tax profit account (CUFINRE) was P. 23,109,403, P. 55,828,316 and P. 11,827,098, respectively. These amounts are for Teléfonos de México, S.A. de C.V. computed on a stand-alone basis.

16. Stock Option Plan

Starting in September 2001, TELMEX established a stock option plan for its officers. The plan is for a duration of four years, and 50 million Series "L" shares are to be made available. Each year, plan participants may select between acquiring all shares available or deferring their purchase until the final year. In 2001, options made available totaled 11,673,401 shares and 106,248 were subscribed. The difference between market value and the price given on the respective options was not significant.

17. Segments

After the spin-off described in Note 2, TELMEX operates primarily in two segments: local and long-distance telephone services. Local telephone service corresponds to fixed local wired service. The long-distance service includes both domestic and international services, exclusive of the long-distance calls originated in public and rural telephones and data transmission, services included in the others, adjustments and elimination column. Additional information related to the Company's operations is provided in Note 1. The following summary shows the most important segment information, which has been prepared on a consistent basis:

(Amounts in millions of Constant Pesos at December 31, 2001)

	Local Service	Long Distance	Others, adjustments and eliminations	Total consolidated
At December 31, 2001				
Revenues:				
External revenues……………..	P. 70,099	P. 25,385	P. 15,483	P. 110,967
Intersegment revenues………..	9,782		(9,782)	
Depreciation and amortization….	11,850	2,095	3,314	17,259
Operating income………………..	27,826	9,118	5,648	42,592
Segment assets (1)……………..	172,504	33,486	30,510	236,500
At December 31, 2000				
Revenues:				
External revenues……………..	64,674	27,058	14,825	106,557
Intersegment revenues………..	14,484		(14,484)	
Depreciation and amortization….	13,061	2,181	2,431	17,673
Operating income………………..	30,501	6,526	4,424	41,451
Segment assets (1)……………..	171,641	31,431	28,319	231,391
At December 31, 1999				
Revenues:				
External revenues……………..	57,383	28,063	11,434	96,880
Intersegment revenues………..	11,866		(11,866)	
Depreciation and amortization….	13,878	2,255	2,357	18,490
Operating income………………..	29,244	9,236	252	38,732
Segment assets (1)……………..	171,990	26,537	22,053	220,580

Additionally, the others, adjustments and elimination's column includes the yellow and white pages directories and other services. Intersegmental transactions are reported at fair value. Comprehensive financing cost and provisions for income tax and employee profit sharing are not assigned to the segments; they are handled at the corporate level.

(1) Segment assets include plant, property and equipment, construction in progress, inventories and advances to suppliers, without including accumulated depreciation.

18. Differences between Mexican and U.S. GAAP

The Company's consolidated financial statements are prepared in accordance with Mexican GAAP, which differ in certain significant respects from generally accepted accounting principles in the United States ("U.S. GAAP").

The reconciliation to U.S. GAAP does not include the reversal of the adjustments to the financial statements for the effects of inflation required under Mexican GAAP (Bulletin B-10), because the application of Bulletin B-10 represents a comprehensive measure of the effects of price level changes in the Mexican economy and, as such, is considered a more meaningful presentation than historical cost-based financial reporting for both Mexican and U.S. accounting purposes.

The principal differences between Mexican GAAP and U.S. GAAP, as they relate to the Company, are described below together with an explanation, where appropriate, of the method used to determine the adjustments that affect operating income, net income, total stockholders' equity and resources provided by operating and financing activities.

Cash Flow Information:

Under Mexican GAAP, the Company presents consolidated statements of changes in financial position, as described in Note 1. The changes in the consolidated financial statement balances included in this statement constitute resources provided by and used in operating, financing and investing activities stated in constant pesos (including monetary and foreign exchange gains and losses). Under Mexican GAAP changes in trading securities are presented as investing activities, while under U.S. GAAP the cash flows from these type of securities should be disclosed as cash provided by (used in) operating activities.

Statement of Financial Accounting Standards No.95 ("SFAS No. 95"), "Statement of Cash Flows," does not provide guidance with respect to inflation adjusted financial statements. In accordance with Mexican GAAP, the changes in current and long-term debt due to restatement in constant pesos, including the effect of exchange differences, is presented in the statement of changes in financial position in the financing activities section. The company has adopted the guidance issued by the AICPA SEC Regulations Committee's International Practices Task Force in its meeting held on November 24, 1998, encouraging foreign registrants that file price level adjusted financial statements to provide cash flow statements that show separately the effects of inflation on cash flows.

If the changes in trading securities, the monetary gain and the exchange gain or loss related to the debt, were treated as components of operating activities, summarized consolidated statements of cash flows derived from information prepared in accordance with U.S. GAAP would be as follows:

(Amounts in thousands of Constant Pesos as of December 31, 2001)

	Year ended December 31,		
	2001	2000	1999
Operating activities:			
Net income	P.20,255,494	P. 25,456,361	P. 26,664,496
Depreciation	21,152,377	20,759,655	21,827,655
Amortization	505,891	340,259	275,056
Deferred taxes	3,179,832	2,356,587	1,467,513
Monetary gain	(2,767,372)	(4,557,970)	(7,931,288)
Equity in results of affiliates	430,082	327,454	121,107
Effect of exchange rate differences on debt	(2,431,280)	291,128	(1,057,113)
Investment in marketable securities	(367,804)	(176,333)	(215,035)
Adjustment to value of equity investments	881,618		
Income from discontinued operations, net		(1,302,506)	(4,072,053)
Change in operating assets and liabilities	865,659	(3,499,464)	(3,835,915)
Resources provided by operating activities of continuing operations	41,674,497	39,995,171	33,244,423
Financing activities:			
New loans	70,283,971	62,557,484	25,789,791
Repayment loans	(72,912,305)	(35,542,956)	(25,733,363)
Purchase of Company's own shares and cash dividends paid	(20,416,354)	(31,682,238)	(15,797,724)
Resources used in financing activities of continuing operations	(23,044,688)	(4,667,710)	(15,741,296)
Investing activities:			
Investment in plant, property and equipment and inventories	(22,762,508)	(19,301,041)	(11,130,716)
Other investments	(304,178)	(1,651,574)	(1,930,431)
Resources used in investing activities of continuing operations	(23,066,686)	(20,952,615)	(13,061,147)
Effect of inflation accounting	(490,434)	(864,171)	923,857
Net change in assets and liabilities of discontinued operations		(6,694,823)	(1,807,035)
Net (decrease) increase in cash and short-term investments	(4,927,311)	6,815,852	3,558,802
Cash and short-term investments at beginning of year	13,741,340	6,925,488	3,366,686
Cash and short-term investments at end of year	P. 8,814,029	P. 13,741,340	P. 6,925,488

Net resources provided by operating activities reflect cash payments for interest, income tax and employee profit sharing as follows:

	Year ended December 31,		
	2001	2000	1999
Interest	P.4,871,010	P. 8,070,924	P. 10,558,002
Income tax	9,669,106	6,660,980	8,559,323
Employee profit sharing	3,265,953	2,600,835	2,542,442

Cash flows from purchases and sales of trading securities during 2001 were P. 299,578 and P.94,471, respectively. Cash flows from purchases and sales of trading securities during 2000 were P.5,543,203 and P. 4,710,612, respectively. Cash flows from purchases of trading securities during 1999 were P. 202,557. During 1999, the company did not make any sales of trading securities.

Capitalized Interest:

Under Mexican GAAP, the Company does not capitalize net financing costs on assets under construction. Under U.S. GAAP, interest on borrowings in foreign currencies or comprehensive financing costs for borrowings in pesos, must be considered an additional cost of constructed assets to be capitalized in property, plant and equipment and depreciated over the lives of the related assets. The amount of interest or net financing costs capitalized for U.S. GAAP purposes was determined by reference to the Company's average interest cost of outstanding borrowings.

Valuation of Inventories and Plant, Property and Equipment:

As previously discussed in Note 5, through December 31, 1996, items comprising the telephone plant were restated based on the acquisition date and cost, applying the factors derived from the specific indexes determined by the Company and validated by an independent appraiser registered with the National Banking and Securities Commission. Since January 1, 1997, the valuation method of plant, property and equipment was modified, as the Bulletin B-10 eliminated the use of appraisals to restate plant, property and equipment.

The alternate restatement method allowed by the Bulletin B-10, which was the one adopted in 1997 by the Company as described in Note 5, is not acceptable for U.S. GAAP purposes; consequently, the difference between this method and the restatement of inventories and plant, property and equipment based on the NCPI was taken to the U.S. GAAP reconciliations subsequently presented.

As a result of this comparison, inventories, plant, property and equipment and stockholders' equity increased by P.17,775,335 (P.14,604,791 in 2000), and the depreciation expense for 2001 increased by P.3,916,754 (P.2,945,293 and P.3,067,370 in 2000 and 1999, respectively).

Accrued Vacation Pay:

For purposes of the attached consolidated financial statements, the expense for vacation pay is recognized when paid rather than during the period in which it is earned by employees. For U.S. GAAP purposes, the Company has determined the accrued liability for vacation pay at December 31, 2001, 2000 and 1999, and accordingly, has adjusted the expense for vacation pay during the periods then ended.

Deferred Income Tax and Deferred Employee Profit Sharing:

As explained in Note 1 and 15, the accounting for deferred income tax was changed in 2000 with the issuance of the new Bulletin D-4. Through December 31, 1999, under Mexican GAAP, deferred income tax was determined by the partial liability method of accounting, under which deferred income tax is provided for identifiable, non-recurring temporary differences (i.e., those that are expected to reverse over a definite period of time) at rates expected to be in effect at the time those temporary differences reverse.

The new Bulletin D-4 requires that deferred income tax be determined on virtually all temporary differences in balance sheets accounts for financing and tax reporting purposes. The cumulative effect derived from the adoption of Bulletin D-4 at the beginning of 2000 for P. 9,559,597 was charged to stockholders’ equity.

Statement of Financial Accounting Standards No. 109 ("SFAS No. 109") "Accounting for Income Taxes,” requires deferred income tax be determined using the liability method for all temporary differences between financial reporting and tax bases of assets and liabilities and that such difference be measured at the enacted income tax rates for the years in which such taxes will be payable or refundable.

The Company is required to pay employee profit sharing in accordance with Mexican labor law. Deferred employee profit sharing under U.S. GAAP has been determined following the guidelines of SFAS No.109. The new Bulletin D-4 did not significantly change the accounting for employee profit sharing, of which the deferred portion is determined by the partial liability method of accounting referred to above .

The deferred tax adjustment included in the net income and stockholder’s equity reconciliations, also include the effect of deferred taxes on the other U.S. GAAP adjustments reflected in the respective summaries.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

The differences in the recognition of deferred income tax and deferred employee profit sharing (for purposes of this note, collectively "deferred taxes") between Mexican and U.S. GAAP for purposes of the income statement were as follows:

1999……………………P.	(887,342)
2000……………………P.	(496,669)
2001……………………P.	(477,812)

The effect of income tax and employee profit sharing on the difference between the indexed cost and the specific indexation factor valuation of fixed assets and inventories, and additionally on the minimum pension and seniority premium liability adjustment, is applied as an adjustment to stockholders' equity. The related accumulated amounts at December 31, 2001 and 2000 that decreased equity were P.(6,088,601) and P.(5,453,801), respectively.

The yearly changes in the accumulated amount for deferred taxes applied to equity as a result of this effect corresponding to continuing operations from 1999 through 2001 are the following:

1999……………………P.	(936,524)
2000……………………P.	(3,537,723)
2001……………………P.	(634,800)

In 2001, 2000 and 1999, monetary gains of P.17,161, P.149,888 and P.154,735, respectively, on the deferred taxes balance related to the difference between the indexed cost and replacement cost valuation of fixed assets and inventories and additionally on the minimum pension and seniority premium liability adjustment, were taken to equity, as part of the change of the year.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

Significant components of deferred taxes under U.S. GAAP at December 31, 2001 and 2000 are as follows:

	2001			2000		
	Income Tax	Employee Profit Sharing	Deferred Taxes	Income Tax	Employee Profit Sharing	Deferred Taxes
Deferred tax assets:						
Allowances for bad debts and slow moving inventories....	P. 607,157	P. 173,473	P. 780,630	P. 825,631	P. 235,895	P. 1,061,526
Tax loss carry forwards..........	17,306	-	17,306	41,541	-	41,541
Deferred revenues..........	124,768	35,648	160,416	445,754	125,159	570,913
Deferred Assets..........	-	-	-	14,500	926	15,426
Accrued liabilities..........	594,595	123,629	718,224	376,752	107,645	484,397
Debt obligations exchange loss..........	-	114,856	114,856	-	226,777	226,777
Pensions and seniority premiums..........	630,660	180,189	810,849	-	-	-
Total deferred tax assets..........	1,974,486	627,795	2,602,281	1,704,178	696,402	2,400,580
Deferred tax liabilities:						
Fixed assets..........	(17,512,284)	(6,568,319)	(24,080,603)	(16,038,310)	(6,952,392)	(22,990,702)
Inventories..........	(308,314)	(104,769)	(413,083)	(337,755)	(124,363)	(462,118)
Capitalized interest or net financing cost..........	(1,104,942)	(315,698)	(1,420,640)	(1,060,752)	(303,072)	(1,363,824)
Licenses..........	(155,051)	(44,295)	(199,346)	(226,061)	(64,589)	(290,650)
Pensions and seniority premiums..........	-	-	-	(317,684)	(59,980)	(377,664)
Total deferred tax liabilities..........	(19,080,591)	(7,033,081)	(26,113,672)	(17,980,562)	(7,504,396)	(25,484,958)
Net deferred tax liabilities..........	P. (17,106,105)	P. (6,405,286)	P. (23,511,391)	P. (16,276,384)	P. (6,807,994)	P.(23,084,378)

For Mexican GAAP purposes, as earlier discussed in Note 15, deferred income tax liabilities of P.11,523,792 and P.11,896,597 were recognized at December 31, 2001 and 2000, respectively.

Employee Benefits Obligations:

In 2001, 2000 and 1999, pension and seniority premium plans expense under U.S. GAAP totaled P.2,979,223, P.2,936,006, and P.2,871,330, respectively. The components of these employee benefit obligations, calculated in accordance with the provisions of Statement of Financial Accounting Standards No. 87 (SFAS No. 87), consist of the following:

	December 31,		
	2001	**2000**	**1999**
Service cost..........	P.1,841,576	P. 2,017,542	P. 1,781,553
Interest cost..........	3,749,080	3,682,518	3,157,416
Return on plan assets..........	(3,175,440)	(3,248,837)	(2,525,457)
Amortization of past service costs..........	484,783	484,783	457,818
Amortization of variances in assumptions..........	79,224		
Net cost under U.S. GAAP..........	2,979,223	2,936,006	2,871,330
Net cost under Mexican GAAP..........	3,556,858	3,536,433	3,427,027
Cost reduction under U.S. GAAP..........	P. (577,635)	P. (600,427)	P. (555,697)

The Company has adopted a select and ultimate approach to establish economic assumptions used to determine the actuarial present value of pension plan obligations under U.S. GAAP. In determining the various economic assumptions used in the computation, the Company estimates specific rates for each of the next 15 years and assumes a constant ultimate rate for each year thereafter. Each economic assumption is evaluated annually and revised as necessary. Assumptions used in the computation of the net cost under U.S. GAAP for each of the years presented in the above table are those used to determine employee benefit obligations disclosed below as of December 31 of the prior year.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

The pension and seniority premium plans liability is as follows:

	December 31,	
	2001	**2000**
Actuarial present value of benefit obligations:		
Vested benefit obligation	P.29,714,635	P. 26,765,816
Non-vested benefit obligation	29,665,582	26,174,260
Accumulated benefit obligation	59,380,217	52,940,076
Additional benefits related to future compensation Increases	3,748,598	3,413,054
Projected benefit obligation	P.63,128,815	P. 56,353,130

The change in the pension plan benefit obligation is as follows:

	December 31,	
	2001	**2000**
Projected benefit obligation at the beginning of year	P. 56,353,130	P. 54,722,195
Service cost	1,841,576	2,017,542
Interest cost	3,749,080	3,682,519
Actuarial loss (gain)	4,226,043	(1,463,425)
Benefits paid	(3,041,014)	(2,605,701)
Projected benefit obligation at end of year	P. 63,128,815	P. 56,353,130

The change in employee benefit plan assets and plans' funded status is as follows:

	December 31,	
	2001	**2000**
Fair value of plan assets at beginning of year	P. 46,160,465	P. 46,134,266
Actual return on plan assets	3,001,057	(1,860,896)
Employer contribution	4,894,966	1,887,095
Fair value of plan assets at end of year	P. 54,056,488	P. 46,160,465

	2001	**2000**
Funded status	P. 9,072,327	P.10,192,665
Unrecognized net actuarial loss	(11,127,907)	(6,807,827)
Unrecognized net transition obligation and intangible asset.	(3,521,843)	(4,006,626)
	(5,577,423)	(621,788)
Additional minimum liability	10,901,152	7,401,399
Accrued benefit cost	P. 5,323,729	P. 6,779,611

The equity adjustment is as follows:

	December 31,	
	2001	**2000**
Additional minimum liability	P. 10,901,152	P. 7,401,399
Intangible asset	(3,521,843)	(4,006,626)
Equity adjustment under U.S. GAAP	7,379,309	3,394,773
Equity adjustment under Mexican GAAP	7,282,079	3,317,669
Additional equity adjustment to be recognized Under U.S. GAAP	P. 97,230	P. 77,104

(Amounts in thousands of Constant Pesos as of December 31, 2001)

Starting 1997, the actuarial computations are based on actuarial assumptions net of inflation. In the last quarter of 2000, the Company decided to review and modify the actual assumptions used for several years to make the actuarial computation of the projected benefit obligation and the accumulated benefit obligation at December 31, 2000, as well as the net period cost for 2001.

The net of inflation rates used to determine the actuarial present values of the benefit obligations at December 31, 2001, 2000, and 1999 are presented below for each of the economic assumptions.

	2001	2000	1999
Discount of labor obligations:			
First year……………………	6.84%	6.84%	6.90%
Long-term average………..	5.85%	5.85%	4.91%
Increase in salaries:			
First year…………………..	1.85%	1.85%	0.88%
Long-term average………..	0.96%	0.96%	1.42%
Return of plant assets……………...	6.84%	6.84%	6.90%

The changes in financial assumptions resulted in a decrease of approximately P. 1,200,000 in the net period cost of 2001, compared to the cost that would have been determined on the basis of the previous actuarial assumptions. The change represented a decrease of approximately P.6,160,000 in the projected benefit obligation, the accumulated benefit obligation, and in the charge to stockholders' equity for labor obligations at December 31, 2000.

The unrecognized net transition obligation under SFAS No. 87 of P.5,493,845 at January 1, 1997, is being amortized over the average future working lifetime of the employee group, which has been determined to be 12 years. The portion of the unrecognized net (loss) gain that exceeds 10% of the projected benefit obligation will also be recognized over 12 years.

In 1995, consistent with the deferral of the unrecognized net (loss) gain, TELMEX included in income of such year an amount of P.642,484 as monetary gain on the unfounded liability and deferred P.3,382,649 which represented the difference between the amount credited to income and the full monetary gain on the unfounded liability. For 1996, the Company did not defer the monetary gain for such year, as the rates used in the actuarial study were similar to actual inflation for 1996, and amortized P.177,101 of the monetary gain deferred in 1995. The monetary gain deferred in 1995 is being amortized in 12 years. In 2001, 2000 and 1999, the Company amortized P.291,414 each year, on the monetary gain deferred in 1995.

Effects of Inflation Accounting on Approximate U.S. GAAP Adjustments:

To determine the net effect on the consolidated financial statements of recognizing the adjustments described above, it is necessary to recognize the effects of applying the Mexican GAAP inflation accounting provisions (described in Note 1) to such adjustments. These effects are taken into consideration in the preparation of U.S. GAAP reconciliations of net income, operating income and equity.

Disclosure about Fair Value of Financial Instruments:

In accordance with Statement of Financial Accounting Standards No. 107 ("SFAS No. 107"), "Disclosures about Fair Value of Financial Instruments," under U.S. GAAP it is necessary to provide information about the fair value of certain financial instruments for which it is practicable to estimate that value.

The carrying amounts of cash and short-term investments, accounts receivable and accounts payable and accrued liabilities approximate fair values due to the short maturity of these instruments.

The fair value of total debt, excluding capital leases, is estimated using discounted cash flow analyses based on current borrowing rates offered to the Company for debt of the same remaining maturities and the market value for the convertible senior debentures at December 31, 2001 and 2000. As of December 31, 2001, the carrying value of total debt is P.67,201,015 (P.76,114,990 at December 31, 2000) and the fair value is P.70,465,978 (P.77,021,090 at December 31, 2000).

Impairment of Assets:

Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," requires impairment losses to be recorded on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. Statement 121 also addresses the accounting for long-lived assets that are expected to be disposed of. Based on current circumstances, it was not necessary to record any adjustment to the carrying value of these assets.

Business Combinations and Goodwill and Other Intangible Assets:

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, Business Combinations, and No. 142, Goodwill and Other Intangible Assets, effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill and intangible assets deemed to have indefinite lives will no longer be amortized but will be subject to annual impairment tests in accordance with the Statements. Other intangible assets will continue to be amortized over their useful lives.

The Company will apply the new rules on accounting for goodwill and other intangible assets beginning in 2002. Application of the nonamortization provisions of the Statement is not expected to have a material effect on net income. During 2002, the Company will perform the first of the required impairment tests of goodwill and indefinite lived intangible assets as of January 1, 2002 and has not yet determined what the effect of these tests will be on the earnings and financial position of the Company.

Translation of Financial Statements of Foreign Subsidiaries:

Under Mexican GAAP, the financial statements of foreign subsidiaries and affiliates for periods prior to the most recent period, are translated following the guidelines of Bulletin B-15. This bulletin requires that the financial statements of foreign subsidiaries and affiliates for periods prior to the most recent period, be translated into constant Mexican pesos by restating the balances to constant units in the local currency, using the inflation rate of the country in which the subsidiary or affiliate is located, before being translated into Mexican pesos at the rate of exchange at the end of the reporting period .

In the Company's financial statements for each of the three years in the period ended December 31, 2001, including the financial statements of foreign subsidiaries that were transferred to América Móvil, such restatements were made based on the inflation in Mexico because the Company's investments in foreign subsidiaries and affiliates were not material in any of these periods.

Under Mexican GAAP the statement of income amounts were translated at the prevailing exchange rate at the end of the reporting period. Under U.S. GAAP, statement of income amounts are translated at the average exchange rate for the period. In the Company's financial statements for each of the three years in the period ended December 31, 2001, the effects of this translation difference were not material.

Reporting Comprehensive Income:

Statement No. 130 establishes rules for the reporting and disclosure of comprehensive income and the related components. Statement No. 130 requires the deficit from restatement of stockholders' equity, deferred taxes on the difference between indexed cost and replacement cost and minimum pension and seniority premium liability adjustment, which prior to the adoption were reported separately in stockholders' equity, to be included in other comprehensive income. The company has restated prior years financial statements, reclassifying deferred taxes in the amount of P. (4,060,632) from retained earnings to accumulated other comprehensive income.

Cumulative effects of the deficit from restatement of stockholders' equity, deferred taxes on the difference between indexed cost and replacement cost and minimum pension and seniority premium liability adjustment included in comprehensive income at December 31, 2001, that (decreased) increased stockholder's equity are P.(41,297,952), P.4,551,169 and P. (7,379,309), respectively.

Accounting for the Cost of Computer Software Developed or Obtained for Internal Use:

In March 1998, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position 98-1 ("SOP 98-1"), "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use." SOP 98-1, which was effective beginning on January 1, 1999, requires the capitalization of certain costs incurred after the date of adoption in connection with developing or obtaining software for internal-use. Because the Company capitalizes such costs, the adoption of SOP 98-1 in 1999 did not have any significant effect on U.S. GAAP earnings or financial position.

Accounting for the Costs of Start-Up Activities:

In April 1998, the AICPA issued SOP 98-5, "Reporting the Cost of Start-Up Activities." The effective date of the SOP was January 1, 1999. It requires that start-up costs capitalized prior to January 1, 1999, be written-off and any future start-up costs be expensed as incurred. Because the Company is expensing such costs as incurred, the adoption of this guideline in 1999 did not effect U.S. GAAP earnings or financial position.

Accounting for Derivative Instruments and Hedging Activities:

In June 1998, the Financial Accounting Standards Board issued Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended, which was required to be adopted in years beginning after June 15, 2000. Because of the Company's limited use of derivatives, the adoption of this Statement did not have a significant effect on earnings or the financial position of the Company.

SAB-101 Revenue Recognition:

Staff Accounting Bulletin No. 101, "Revenue Recognition" ("SAB 101") was released on December 3, 1999, and provides the staff's view in applying generally accepted accounting principles to

selected revenue recognition issues. Such adoption had no impact on the Company's net income or stockholders' equity.

Under U.S. GAAP, revenues from internet service plans and from installation charges for data transmission equipment are deferred and recognized over the estimated duration of the customer relationship. Under Mexican GAAP, these revenues are recognized when they are billed. The amount of the resulting difference between Mexican GAAP and U.S. GAAP is not material.

Under U.S. GAAP, revenues from installation charges for local service and related costs not exceeding such revenues are deferred and recognized over the estimated duration of the customer relationship. Under Mexican GAAP, these revenues and costs are recognized when the installation is performed. The difference between Mexican GAAP and U.S. GAAP has no effect on operating income, net income or stockholders' equity, and the effect on revenues is not material.

U.S. GAAP Adjustments on Discontinued Operations:

U.S. GAAP adjustments on discontinued operations shown in the net income and stockholders' equity reconciliations presented below, are mainly comprised of deferred taxes, accrued vacation costs, minority interest, and the difference between the indexed cost and specific indexation factor valuation of fixed assets and inventories.

Asset Retirement Obligations:

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations, which is effective for fiscal years beginning after June 15, 2002. The Statement requires legal obligations associated with the retirement of long-lived assets to be recognized at their fair value at the time that the obligations are incurred. Upon initial recognition of a liability, that cost should be capitalized as part of the related long-lived asset and allocated to expense over the useful life of the asset. The Company will adopt Statement 143 on January 1, 2003, and, based on current circumstances, does not believe that the impact of adoption of Statement 143 will have a material impact on the Company's financial position or results of operations.

Impairment or Disposal of Long-Lived Assets:

In August 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets (FAS 144), which addresses financial accounting and reporting for the impairment or disposal of long-lived assets and supersedes SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of, and the accounting and reporting provisions of APB Opinion No. 30, Reporting the Results of Operations for a disposal of a segment of a business. FAS 144 is effective for fiscal years beginning after December 15, 2001, with earlier application encouraged. The Company expects to adopt FAS 144 as of January 1, 2002 and it does not expect that the adoption of the Statement will have a significant impact on the Company's financial position and results of operations.

Summary

Income from continuing operations, net income, operating income and total stockholders' equity, adjusted to take into account the material differences between Mexican GAAP and U.S. GAAP, are as follows:

	Year ended December 31,		
	2001	2000	1999
Income from continuing operations as reported under Mexican GAAP	P.23,494,117	P.26,097,495	P.23,713,332
U.S. GAAP adjustments:			
Capitalized interest or net financing cost	601,832	530,462	466,598
Depreciation of capitalized interest	(482,762)	(481,386)	(545,333)
Accrued vacation pay	(126,441)	(127,482)	(149,017)
Deferred income tax under U.S. GAAP included in this reconciliation	(53,243)	(97,795)	17,632
Deferred income tax		(613,988)	(409,783)
Deferred employee profit sharing under U.S. GAAP included in this reconciliation	(24,652)	(66,153)	167,534
Deferred employee profit sharing	(399,917)	281,267	(662,725)
Pension and seniority premium plan cost	577,635	600,427	555,697
Difference between the restatement of depreciation expense based on specific indexation factors and on the basis of the NCPI	(3,916,754)	(2,945,293)	(3,067,370)
Effects of inflation accounting on U.S. GAAP adjustments	610,991	976,301	2,505,878
Other	(55,312)		
Total U.S. GAAP adjustments in income from continuing operations	(3,268,623)	(1,943,640)	(1,120,889)
Income from continuing operations under U.S. GAAP	20,225,494	24,153,855	22,592,443
Income from discontinued operations under U.S. GAAP		1,302,506	4,072,053
Net income under U.S. GAAP	P. 20,225,494	P.25,456,361	P.26,664,496
Weighted average common shares outstanding (in millions):			
Basic	13,541	14,669	15,092
Diluted	14,217	15,345	15,326
Income per share under U.S. GAAP (in pesos) from continuing operations			
Basic	P. 1.494	P. 1.647	P. 1.497
Diluted	P. 1.399	P. 1.557	P. 1.461
Net income per share under U.S. GAAP (in pesos)			
Basic	P. 1.494	P. 1.735	P. 1.767
Diluted	P. 1.399	P. 1.642	P. 1.726

After giving effect to the foregoing adjustments for pension plan costs, accrued vacation pay, depreciation of capitalized interest, the difference between the restatement of depreciation expense based on specific indexation factors and on the basis of the NCPI and other; as well as to the reclassification of the employee profit sharing expense and the deferred employee profit sharing expense, operating income under U.S. GAAP totaled P.35,178,278, P. 35,260,323 and P.32,195,782, in 2001, 2000 and 1999, respectively.

(Amounts in thousands of Constant Pesos as of December 31, 2001)

	December 31	
	2001	**2000**
Total stockholders' equity under Mexican GAAP	P. 50,762,116	P.51,626,148
U.S. GAAP adjustments, net of effects of inflation on monetary items:		
Capitalized interest or net financing cost	9,453,304	8,851,472
Accumulated depreciation of capitalized interest or net financing cost	(6,303,515)	(5,820,752)
Accrued vacation pay	(949,409)	(861,818)
Deferred income tax on U.S. GAAP adjustments included in this reconciliation	704,775	725,972
Deferred income tax		
Deferred employee profit sharing on USGAAP adjustments included in this reconciliation	174,625	207,531
Deferred employee profit sharing	(6,778,398)	(6,667,483)
Deferred taxes on the difference between the indexed cost and specific indexation factor valuation of fixed assets and inventories, and on minimum pension and seniority premium liability adjustment	(6,088,601)	(5,453,801)
Pension and seniority premium plan cost	(5,696,882)	(6,565,930)
Minimum pension and seniority premium liability adjustment	(97,230)	(77,104)
Difference between the restatement of fixed assets and inventories based on specific indexation factors and on the basis of the NCPI	17,775,335	14,604,791
Other	(54,944)	
Total U.S. GAAP adjustments from continuing operations, net	2,139,060	(1,057,122)
Total stockholders' equity	P. 52,901,176	P.50,569,026

(Amounts in thousands of Constant Pesos as of December 31, 2001, except for dividends per share)

Consolidated statements of changes in stockholders' equity under U.S. GAAP at December 31, 1999, 2000 and 2001, are as follow:

	Capital stock	Premium on sale of shares	Retained earnings: Legal reserve	Retained earnings: Reserve for purchase of Company's own shares	Retained earnings: Unappropriated	Retained earnings: Total	Accumulated other comprehensive income	Comprehensive income	Total
Balances at January 1, 1999	P. 59,037,317	P. 12,059,923	P.14,271,061	P. 17,524,070	P. 58,241,038	P. 90,036,169	P. (42,484,377)		P. 118,649,032
Appropriation of earnings approved at stockholders' meetings held in March and April, 1999:									
Cash dividends paid at P.0.457 per share (P. 0.388 historical)					(6,865,146)	(6,865,146)			(6,865,146)
Increase in reserve for purchase of Company's own shares				27,416,824	(27,416,824)				
Increase in legal reserve			11,648		(11,648)				
Cash purchase of Company's own shares	(130,619)			(8,480,073)	(321,886)	(8,801,959)			(8,932,578)
Comprehensive income:									
Net income for the year					26,664,496	26,664,496		P. 26,664,496	26,664,496
Other comprehensive income items:									
Deferred taxes allocated to equity, net of effect of inflation							(1,118,210)	(1,118,210)	(1,118,210)
Minimum pension and seniority premium liability adjustment							903,468	903,468	903,468
Deficit from holding nonmonetary assets							(605,322)	(605,322)	(605,322)
Comprehensive income								P. 25,844,432	
Balances at December 31, 1999	58,906,698	12,059,923	14,282,709	36,460,821	50,290,030	101,033,560	(43,304,441)		128,695,740
Appropriation of earnings approved at stockholders' meeting held in April, 2000:									
Cash dividends paid at P.0.479 per share (P. 0.445 historical)					(7,010,051)	(7,010,051)			(7,010,051)
Increase in legal reserve			84,098		(84,098)				
Cash purchase of Company's own shares	(2,096,997)			(22,743,899)	168,709	(22,575,190)			(24,672,187)
Comprehensive income:									
Net income for the year					25,456,361	25,456,361		P. 25,456,361	25,456,361
Other comprehensive income items:									
Deferred taxes allocated to equity, net of effect of inflation							44,094	44,094	44,094
Minimum pension and seniority premium liability adjustment							(2,806,870)	(2,806,870)	(2,806,870)
Deficit from holding nonmonetary assets							1,126,281	1,126,281	1,126,281
Comprehensive income								P. 23,819,866	
Spun-off stockholder's equity	(28,770,050)		(44,228)	(8,622,874)	(31,119,024)	(39,786,126)	(1,708,166)		(70,264,342)
Balances at December 31, 2000	28,039,651	12,059,923	14,322,579	5,094,048	37,701,927	57,118,554	(46,649,102)		50,569,026
Appropriation of earnings approved at stockholders' meetings held in February and April, 2001:									
Cash dividends paid at P.0.498 per share.(P.0.490 historical)					(6,700,972)	(6,700,972)			(6,700,972)
Increase of reserve for purchase of Company's own shares				5,256,174	(5,256,174)				
Increase in legal reserve			51,373		(51,373)				
Cash purchase of Company's own shares	(1,269,947)			(10,350,222)	(2,095,213)	(12,445,435)			(13,715,382)
Comprehensive income:									
Net income for the year:					20,225,494	20,225,494		P. 20,225,494	20,225,494
Other comprehensive income items:									
Deferred taxes allocated to equity, net of effect of inflation							1,376,060	1,376,060	1,376,060
Minimum pension and seniority premium liability adjustment							1,146,950	1,146,950	1,146,950
Comprehensive Income								P. 22,748,504	
Balances at December 31, 2001	P.26,769,704	P. 12,059,923	P.14,373,952	P.	P. 43,823,689	P. 58,197,641	P. (44,126,092)		P. 52,901,176

See accompanying notes.