Algar
Telecom

Annual Sustainability Report

2012

ABOUT THIS REPORT

Algar Telecom has been reporting on a yearly basis since 2006, its performance within the scopes of economic, social and environmental aspects. For the seventh year running, its annual report discloses financial, social and environmental information, in accordance with the international Global Reporting Initiative (GRI) guidelines, version G3 – Level C. This format represents a step forward towards drawing up an increasingly consistent document, capable of conveying Algar Telecom`s future vision in a transparent manner to all of its stakeholders: clients, shareholders, associates, suppliers, the community and the government.

The information contained herein covers the performance of Algar Telecom and its six subsidiaries: CTBC Celular, CTBC Multimídia Data Net, Image, Algar Tecnologia, Engeset and Algar Mídia, over the period between January 1 and December 31, 2012. The compilation of the financial data, audited by KPMG Auditores Independentes, complies with the criteria set out by the International Financial Accounting Standards (IFRS). The social and environmental performance indicators were compiled and validated internally only, that is, not subject to external assessment. Certain indicators, such as EN4, EN8 and EN16 required reclassifications, which led to the re-presentation of the data disclosed in former reports, so as to reflect the change in the measurement criteria. The GRI indicators are provided individually throughout the text and summarized in a specific reference table included in this report.

The Company's commitment to sustainability, encompassing all its distinct aspects - economic, social and environmental - has been evidenced in the disclosure and format of the present report, which has made available both in Portuguese and in English, in an electronic format and in our website downloadable in PDF application. Priority has been given to themes that focus on management systems and operations that are internally considered of utmost interest to all stakeholders. It is worth mentioning that the process of preparation of this report relied on the dedication of both the Company's and its subsidiaries' associates, engaged in the compilation and validation of the data provided.

For further clarification on this report, please contact us through any of the communication channels listed below:

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GRI: 1.2, 2.1, 2.4, 3.1, 3.2, 3.3, 3.4, 3.5, 3.6, 3.7, 3.8, 3.10, 3.11

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ALGAR TELECOM IN NUMBERS

14,000 associates

6,700 students assisted by social projects

896,000 clients

12,000 km fiber optic backbone network

23,000 km of cables managed by Engeset

3 software plants

655,000 directories printed

11 million accesses to the online directory

4 million newspaper copies

MAIN INDICATORS

Operational Indicators ('000)	2010	2011	2012	2012/2011
FIXED TELEPHONY				
Lines in service	799	924	1,070	15.8%
Authorization area	164	231	310	33.9%
Concession area	635	693	760	9.7%
BROADBAND				
Total	277	332	420	26.3%
ADSL	239	276	326	18.4%
Mobile (3G)	38	56	93	65.0%
MOBILE PHONE				
Total number of clients	579	612	674	10.2%
Postpaid	183	205	211	2.7%
Prepaid	396	406	463	13.9%
PAY TV				
Total	79	94	113	20.2%

Financial Indicators (R$ million)	2010	2011	2012	2012/2011
Gross Revenues	1,945	2,157	2,339	8.4%
Net Revenues	1,511	1,682	1,812	7.7%
EBITDA	409	411	452	10.0%
EBITDA Margin	27.1%	24.4%	25.0%	0.6 p.p.
Net Income	133	144	141	-2.1%
Net Margin	8.7%	8.6%	7.8%	-0.8 p.p.
Capex	237	372	351	-5.6%
Gross Debt	667	815	925	13.5%
Net Debt	477	637	739	16.0%
Net Debt/EBITDA (x)	1.2	1.5	1.6	8.9%

Corporate Indicators	2010	2011	2012	2012/2011
Associates	13,935	15,078	14,351	-4.8%
Men	5,422	6,256	6,269	0.2%
Women	8,513	8,822	8,082	-8.4%
Training				
Investment (R$ thousands)	10,631	12,207	12,780	4.7%
Number of training hours	179,594	429,609	352,568	-17.9%
Investment per associate (R$)	736	811	891	9.9%
Greenhouse gases emission (tons)				
Direct Emissions	2,339	1,309	3,660	179.6%
Indirect Emissions	1,569	1,572	2,153	37.0%

For a more readily overview of the sustainability indicators, please refer to the GRI reference table of contents

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VISION, MISSION AND VALUES

Vision

People Serving People

Mission

Serving and integrating people and business in a sustainable manner

Values

Valuing Human Talents

Integrity

Sustainability

Belief in Brazil

Client, Our Reason for Being.*

A quote from the founder, Mr. Alexandrino Garcia

People

CORPORATE PROFILE

Algar Telecom is a Brazilian public limited company, whose shares are not listed in stock exchanges. The Company is controlled by the Algar Group, distinguished for both its effective service and close relationship with its clients. Algar Telecom holds the shareholding control of six subsidiaries, whose operations comprise a portfolio of products and services engaged in three business segments that complement one another.

The Telecom segment includes fixed line phone services, broadband internet access (ADSL I, ADSL II, HFC, GPON e 3G), data communication, mobile phone services, internet services and pay television (DTH and cable). Algar Tecnologia provides services related to Business Process Outsourcing and IT. In the Complementary Business area, Engeset acts in the segment of installation and maintenance of the telecom networks, whereas Algar Mídia produces phone directories and offers other media-related services. In 2012, these three segments accounted respectively for 77%, 18% and 5% of Algar Telecom's consolidated gross revenues.

The Company's portfolio of products and services, supported by a cutting-edge and innovative infrastructure, caters for over 896,000 corporate and retail clients located throughout the country. It is physically present in six states: Minas Gerais, São Paulo, Rio de Janeiro, Goiás, Mato Grosso do Sul and Paraná, as well as in Brasília, the Federal District. The operations developed by this entire set of segments altogether comprised a team of 14,351 associates as at the close of FY 2012, who are committed to the Company's Vision PEOPLE SERVING PEOPLE, a legacy left from Comendador Alexandrino Garcia, who in 1954 founded the company CTBC (presently named Algar Telecom).

Such legacy of beliefs and values inherited from Mr. Garcia also includes relevant attributes such as ethical and transparent business management, culture of innovation, the well-being of its associates, along with the commitment to the country's development, which consist in the set of principles that set the grounds for the creation of a solid corporate governance policy. The set of best practices adopted by the Company has forged the foundation for a corporate management committed to sustainable growth and creation of value to all stakeholders, which contributed to Algar Telecom's positive performance in 2012, by achieving consolidated net revenues in the amount of R$ 1,811 million.

Algar Telecom believes that business is transitory, whereas principles and values are definitive. Such belief is the main driver that bolsters the distinction of the Organization and brings together the various business activities and the team of thousands of associates. Hence, the yielding result sums up in the ongoing effort to maintain the "Algar way of being" within all the locations where the Company operates and, consequently, ensures the conduction of its mission, which is to "develop sustainable businesses and relationships, which generate perceived value".

Algar Group
The Algar Group, one of the strongest corporate groups in Brazil, was established in 1954 with the foundation of CTBC (Companhia de Telecomunicações do Brasil Central), currently Algar Telecom. Algar Holding's name derives from the initials of its founder, Alexandrino Garcia, and it currently comprises nine subsidiaries operating in four business segments: IT/Telecom, Agribusiness, Services and Tourism. So as to ensure the fulfillment of its Vision "PEOPLE SERVING PEOPLE", the Group relies on nearly 21,000 associates, distributed in offices located across over 1,000 cities in the states of Minas Gerais, São Paulo, Rio de Janeiro, Goiás, Mato Grosso do Sul and Paraná, as well as in Brasília, the Federal District.
Access the Algar Group's 2012 Annual Sustainability Report.

GRI: 2.5, 2.6, 2.7, 2.8
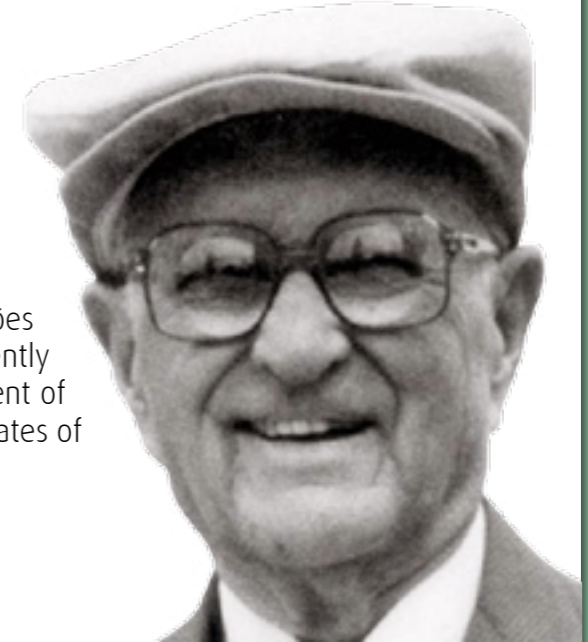
TIMELINE

1954 Comendador Alexandrino Garcia founds CTBC, further on renamed Algar Telecom.

1969 Start-up operations of the graphic editorial business and phone directory publishing.

1991 The Company starts providing telecom network project engineering services.

1993 First company to offer mobile phone services in the Brazilian inland regions.

1995 The business of pay-TV services was added to the portfolio.

1998 Investment in the construction of a fiber optic network and in multimedia services.

1999 Start-up of the contact center operations, with 1,000 workstations in Uberlândia, Minas Gerais State.

2000 Beginning of Data Center services for small and medium-sized companies.

2001 The Company fulfills the universalization goals of ANATEL (Brazilian National Telecommunications Agency) two years before the pre-established deadline.

2002 Long-distance and international calls with carrier selection code 12.

2003 The Company is authorized to extend its fixed telephony and data services to the entire country.

2004 The Company acquires an internet provider in Ribeirão Preto, São Paulo State, and starts offering internet access services.

2005 The Company acquires a 172-km network in the metropolitan area of São Paulo, renews its fixed telephony service concession for another 20 years and inaugurates a new contact center site with 1,500 workstations in Campinas, São Paulo State.

2007 The Company acquires a 3G license for its operating area for mobile phone services, goes public and carries out its first issue of debentures.

2008 The Company is the first to launch the 3G technology in the Brazilian inland region and repositions its contact center business, which started providing Business Process Outsourcing and IT. In the same year, CTBC is renamed Algar Telecom.

2009 Consolidation of the regional offices in the authorization area: Curitiba, Belo Horizonte, São Paulo, Rio de Janeiro, Campinas, Ribeirão Preto, Brasília, Goiânia and São José do Rio Preto. The Company consistently tops the IDA ranking (Índice de Desempenho de Atendimento, or Service Performance Index), ANATEL's indicator for client service quality.

2010 The Company acquires Band H, the last telephony frequency (3G) in Minas Gerais State, outside of its operating area.

2011 Band H services was extended further to nineteen cities, with the launching of packages including fixed and mobile telephony services, fixed and wireless broadband services and satellite pay-TV.

2012 The Company carries out its second public issue of debentures. The pay-TV package adds up 44 HDTV channels. Data center located in Campinas (São Paulo State) has its capacity area expanded by 30%, aimed at supporting the growth in the services provided to the corporate market.

GRI: 2.9

CORPORATE GOVERNANCE

The Company's commitment to transparency, accountability, evaluation, monitoring and assessment of risks, pave the way for Algar Telecom's conduction of its corporate governance practices. The Company went public in 2007, when it carried out its first public issue of debentures, although its shares are not listed in stock exchanges. Algar Telecom's corporate governance model relies on management tools aimed at ensuring a fair decision-making process, controlling and managing corporate risks, capturing synergies across all business segments, valuing the associates, disseminating the corporate culture internally, in addition to seeking continuous improvement leading the Company to reinforce its commitment and transparent approach towards its stakeholders.
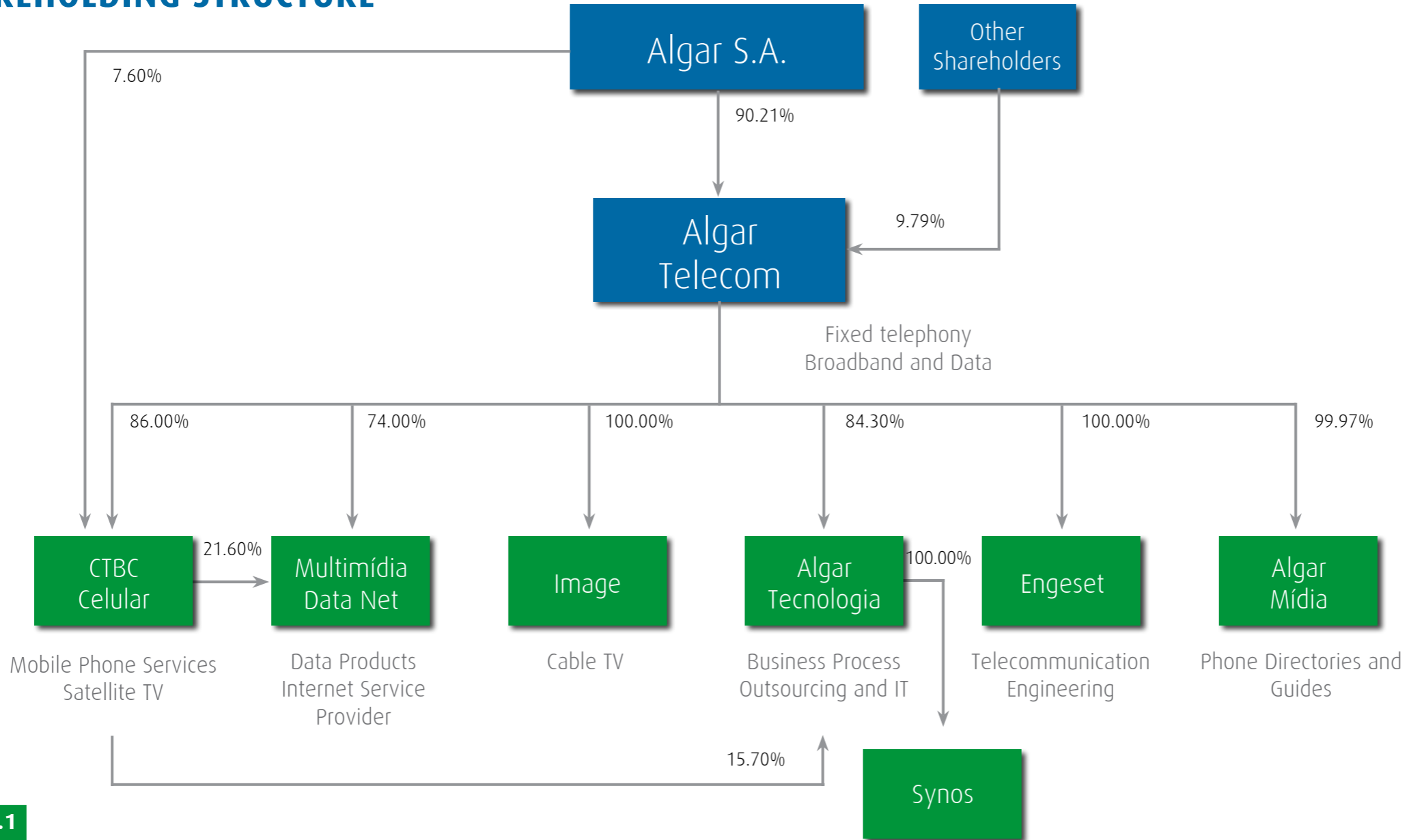
Currently, Algar Telecom has no formal, structured process to engage or define a 'stakeholder', but it seeks to understand its stakeholders' needs by means of an ongoing dialogues. This can be evidenced by a number of different communication channels geared towards its associates, alongside with the " Users Council", an advisory body that for the last 13 years has been in charge of receiving evaluations and suggestions from clients.

Algar Telecom's corporate governance practices are aligned with the corporate governance model adopted by the Algar Group, which aims at harmonizing the interests of the controlling family with the corporate needs, and it has become a benchmark for other Brazilian and international organizations. The effectiveness of this evolving and dynamic model has accredited the Algar Group to take part, since 2010, in the select group of 15 Latin American companies, acknowledged by their excellence in corporate governance practices, which make up the "Companies Circle". This was a joint initiative of the International Finance Corporation (IFC) and the Global Corporate Governance Forum (GCGF), along with the support from the Organization for Economic Cooperation and Development (OECD), these companies meet with the purpose of promoting the enhancement of the corporate governance in Latin America, through the exchanging of experiences.

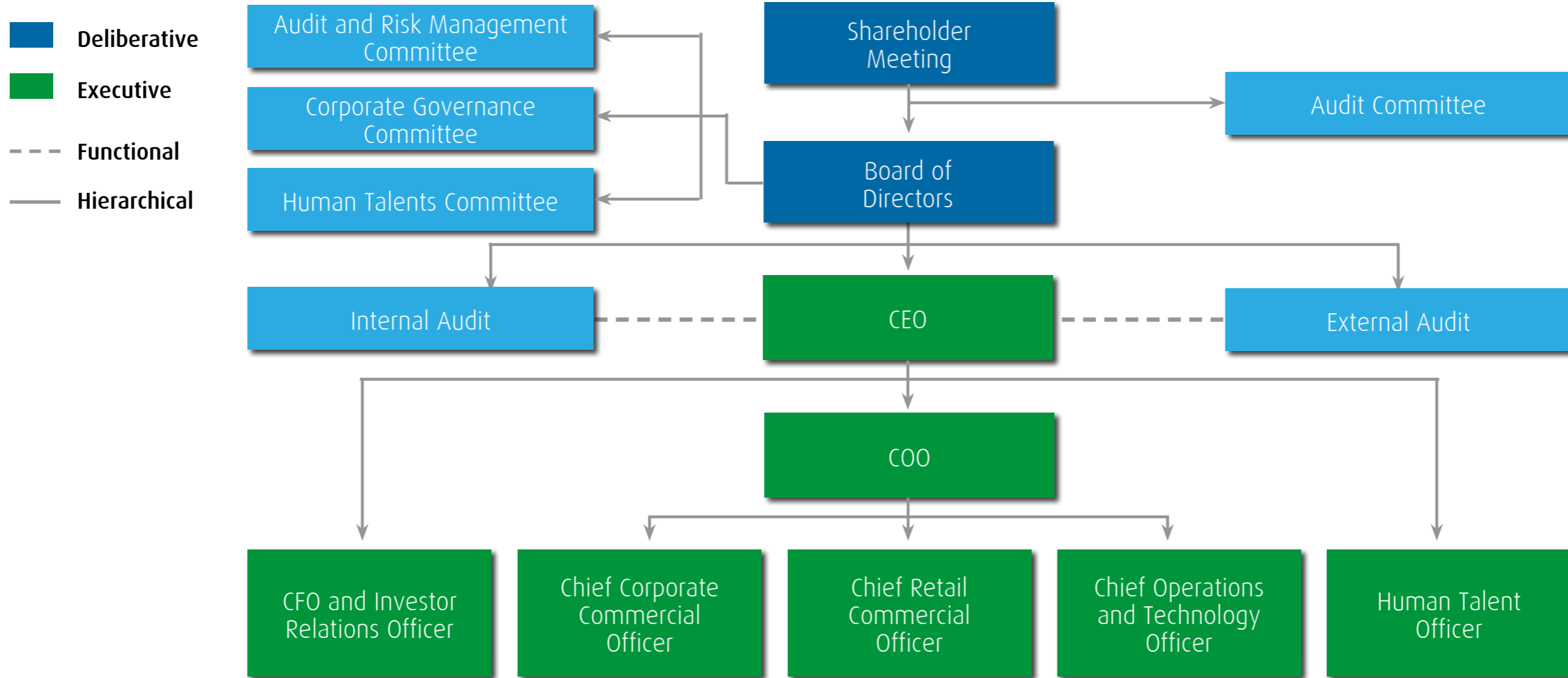Among the corporate governance practices adopted by the Company, special reference is made to:

(a) The Board of Directors is made up by a majority of External members: all the Board's activities follow the guidelines set out by internal policies, which comply with both the Brazilian Corporate Law and the Company's Bylaws, and are based on the recommendations set out in IBCG's Code of Good Corporate Governance Practices;

(b) Advisory Committees to provide support to the Board of Directors: Algar Telecom holds three advisory committees that provide support to the Board of Directors, which consist of External members of the Board of Directors and outside experts;

(c) Executive Board: Algar Telecom relies on highly experienced executive officers, who are broadly skilled in the telecom industry;

(d) Auditing: transparent management, in line with the directives that rule the Company's corporate governance, is reinforced by the activities conducted by an internal audit, which aims to assess and propose improvements with regards to the controlling processes, based on a plan that is reviewed on a yearly basis, in addition to external auditing services, which are provided by an independent specialized firm;

(e) Risk Management: since 2009, Algar Telecom has adopted a formal strategic risk management process;

(f) Investor Relations Division: headed by an Investor Relations Officer elected in accordance with the Company's Bylaws, who is responsible for the relationship with the investors' community, among other related activities;

(g) Code of Ethics: Algar Telecom follows the Code of Ethics adopted by the Algar Group, which lays down the behavior rules and guidelines to be followed by all associates, as well as the corporate conduct towards all stakeholders, within the concept of Sustainability, taking into account the economic, social and environmental dimensions;

(h) Associates' Committee: the body that represents the associates – as the Company's employees are called – which is in charge of listening to and identifying the associates' needs from the various areas and further negotiating with the Company Management.

SHAREHOLDING STRUCTURE

Algar S.A.

Other Shareholders

90.21%

7.60%

Algar Telecom

9.79%

Fixed telephony
Broadband and Data

86.00%   74.00%   100.00%   84.30%   100.00%   99.97%

CTBC Celular

21.60%

Multimídia Data Net

Image

Algar Tecnologia

100.00%

Engeset

Algar Mídia

Mobile Phone Services
Satellite TV

Data Products
Internet Service
Provider

Cable TV

Business Process
Outsourcing and IT

Telecommunication
Engineering

Phone Directories and
Guides

15.70%

Synos

GRI: 4.1

CORPORATE GOVERNANCE STRUCTURE

Deliberative (dark blue)

Executive (green)

- - - **Functional**

——— **Hierarchical**

Audit and Risk Management Committee

Corporate Governance Committee

Human Talents Committee

Shareholder Meeting

Audit Committee

Board of Directors

Internal Audit

CEO

External Audit

COO

CFO and Investor Relations Officer

Chief Corporate Commercial Officer

Chief Retail Commercial Officer

Chief Operations and Technology Officer

Human Talent Officer

On October 8, 2012, the Company carried out a reverse stock split concerning its stake in the capital stock of CTBC Celular and CTBC Multimídia. This initiative was taken with a view to enhancing corporate management, reducing operating and administrative costs, optimizing the shareholding base due to the considerable number of non-trading shareholders, in addition to perfecting the services provided by the Investor Relations Area.

GRI: 2.3, 2.9

BOARD OF DIRECTORS

Incepted in 1999, the Board of Directors' role is to enforce the Company's sustainability policy by laying down its business strategic guidelines, upholding its values and beliefs, and ensuring the harmony between the interests of both the controlling family and those of the whole group of stakeholders.

The Board's major assignments include the evaluation and approval of both the annual budget and the strategic plan proposed by the Executive Board, in addition to supervising the Organization's performance within a long-term horizon.

The Board members are elected at an Annual Shareholders' Meeting for a one-year term, with reelection permitted. As at December 2012, the Board was composed of ten sitting members, of which six are External individuals without any business or professional bond neither with Algar Telecom nor with the family that holds its shareholding control. The Board meets six times a year on a regular basis, according to a pre-established schedule, and at such other times as may be deemed necessary.

The Board members have access to the Governance Portal, an online communication channel that enjoys restricted and exclusive access, which brings together a number of documents and information required for performing their functions. All the Board's activities are ruled by the guidelines set out by internal policies, which comply with both the Brazilian Corporate Law and the Company's Bylaws, and are based on the recommendations set out by the Brazilian Corporate Governance Institute (IBCG)'s Code of Good Corporate Governance Practices. Since 2005, a self-assessment of both the Board as a whole and individually among its members has been undertaken on an annual basis. This process comprises three stages, involving interviews, questionnaires and improvement plans.

Composition of the Board of Directors on 12/31/2012

Luiz Alberto Garcia	Chairman
Luiz Alexandre Garcia	Deputy Chairman
Alexandrino Garcia Neto	Member
Eliane Garcia Melgaço	Member
Darc Antônio da Luz Costa	Member*
Eduardo Moreira da Costa	Member*
Hélio Marcos Machado Graciosa	Member*
Geraldo Sardinha Pinto Filho	Member*
Ozires Silva	Member*
Walter Fontana Filho	Member*

* External member

LUIZ ALBERTO GARCIA

(Chairman)

Shareholder, member of the second generation of the family that holds the Algar Group's shareholding control. Mr. Garcia has a bachelor degree in electronic engineering from Escola Federal de Itajubá (Minas Gerais State), and specializations in Global Business Leadership from Georgetown University Washington, DC, USA; Leading the Family Business from IMD, Lausanne, Switzerland; and Owner/President Management Program from Harvard University, USA. He is a former CEO of the Brazilian National Association of Mobile Phone Service Providers (ACEL), member of ANATEL's Advisory Council, member of the Brazilian Agribusiness Association (ABAG), of Telebrasil and SindiTelebrasil. He also acted as a Board member at the Orsa Foundation. Besides acting as the chairman of the Algar Group, he is the chairman of the Board of Trustees of CPqD Foundation, member of FIEMG's Board, member of the Institute for Industrial Development Studies (IEDI), and of the Research Foundation of the Federal University of Uberlândia (FUNDAP).

LUIZ ALEXANDRE GARCIA

(Deputy Chairman)

Mr. Luiz Garcia holds a bachelor degree in Economics from Universidade Gama Filho (Rio de Janeiro State) and specializations in Marketing from the American University of Paris, France; an MBA from the Catholic University of America, Washington DC, USA; and Leading the Family Business; and Program for Executive Development, both from IMD, Lausanne, Switzerland. He has worked for IFC/World Bank, Washington DC; Ericsson, Dallas, USA and São Paulo; and for Groupe Bull, France. He was a former President of the Uberlândia Commercial and Industrial Association (ACIUB) for two terms and of the Brazilian Mobile Phone Companies Association (ACEL). He is a member of the third generation of the Algar Group's controlling family and has been the Group's CEO since 2006. He also acts as a Board member of the Brazilian Corporate Governance Institute (IBGC), and President of the Companies Circle of the Latin American Corporate Governance.

ALEXANDRINO GARCIA NETO

(Member)

Entrepreneur in the agribusiness segment and a member of the third generation of Algar's controlling group.

ELIANE GARCIA MELGAÇO

(Member)

Ms. Melgaço has a bachelor degree in Business Administration from Pontifícia Universidade Católica (PUC) de Minas Gerais, as well as specializations in MBA from the Catholic University, Washington, DC, USA; Leading the Family Business from IMD, Switzerland; and PGA from Insead, Fontainebleau, France. She has worked for Banco Nacional, Cartão Unibanco and ATL in Relationship and Commercial Marketing. She belongs to the Algar Group's controlling group and currently serves as its Corporate Deputy President of Marketing and Sustainability.

DARC ANTONIO DA LUZ COSTA

(External Member)

Mr. Costa has a bachelor degree in engineering from PUC (Rio de Janeiro State), a master's degree in production engineering from the same university and a doctorate degree in production engineering from COPPE/UFRJ. He was a former Deputy President of the Brazilian Economic and Social Development Bank (BNDES). He is also a member of the Management Board of the Brazilian Strategic Studies Center (CEBRES); advisor for the Brazilian Strategic Studies Center of the War College, where he also acted as a supervisor; President of the Federation of the Chambers of Commerce and Industry of South America (FEBRASUR); member of the Brazilian Academy of Moral and Political Sciences; and a Managing Partner of DLC–Desenvolvimento, Logística e Cenários Simples Ltda.

EDUARDO MOREIRA DA COSTA

(Exernal Member)

He holds a Ph.D degree in electronics from the Southampton University, UK. He acted as the director of the Innovation Area at the Studies and Projects Funding Institution (FINEP), a public company linked to the Science and Technology Ministry, and director and researcher of the Telecommunication Research & Development Center (CPqD). He currently acts as the CEO for ÁgoraLab, Laboratório Internacional Multi-institucional sobre Cidades Inteligentes e Inovação. He acts as a part-time professor for the universities of UFSC and PUC-Rio. He is a Board member of Senior Sistemas, and member of the Brazilian Scientific and Technological Merit Order.

GERALDO SARDINHA PINTO FILHO

(Exernal Member)

Mr. Sardinha holds a bachelor degree in Economics from Faculdade de Ciências Econômicas da Universidade Federal de Minas Gerais (UFMG), with specialization in Finances from J.L.Kellogg Northwestern University (USA), as well as from The Business School for the World (Insead), France. He is a director of Sardinha & Sant'Ana Consultoria Empresarial, in which he is a corporate finance consultant for large corporations, with an emphasis on implementing management processes aimed at value creation. He is a visiting professor at Sauder School of Business – University of British Columbia, Canada, and in The Business School for the World (Insead), France. He is also an associate professor at Fundação Dom Cabral, Brazil. Besides being a member of Algar's Board, he is a member of the Board of Directors for the Seculus, Raimundo da Fonte Group, Mater Dai Hospital and Kyli Group.

HÉLIO MARCOS MACHADO GRACIOSA

(Exernal Member)

Mr. Graciosa has a bachelor's degree in telecom engineering and a master's degree in electric engineering from PUC (Rio de Janeiro State). He was the former Research & Development Officer at Telecomunicações Brasileiras S/A – Telebrás, President of Sociedade de Telecomunicações (SBrT) and Chairman of the Board of Directors of Telesc and Telebahia. He is currently the Chairman of the Telecommunications Research & Development Center (CPqD) (São Paulo State), and of CPqD Technologies & Systems Inc., in Fort Lauderdale, Florida (USA). He is also a director for Telebrasil, chairman of the Board of Padtec, Board member of Cleartech and Telebrasil, as well as member of the Board of Trustees of Campinas Forum Foundation, São Paulo State.

OZIRES SILVA

(Exernal Member)

Mr. Silva has a bachelor degree in aeronautic engineering from Instituto Tecnológico da Aeronáutica (ITA) and a post-graduation degree in aeronautics from California Institute of Technology (CALTECH), California, USA. He headed the group that created Empresa Brasileira de Aeronáutica S.A. (EMBRAER), which he managed since its foundation, in 1970, until 1986, as well as over the 1991-1995 period, when he led the company's privatization process. He acted as the CEO of Petróleo Brasileiro S.A. (Petrobras), Brazilian Infrastructure Minister and CEO of Varig S.A. He is currently a member of several trade and civil servant associations and of the Board of Directors of renowned companies.

WALTER FONTANA FILHO

(Exernal Member)

Mr. Fontana has a bachelor degree and a post-graduation degree in Economics from PUC (São Paulo) and specialization in Marketing Management from Fundação Getúlio Vargas. He acted as the CEO and Chairman of the Board of Directors of Sadia. At present, he is a member of the Board of BRF Brasil Foods, of Repom S.A., and member of the Advisory Committee for the Estado de São Paulo newspaper.

ADVISORY COMMITTEES

The Advisory Committees are non-decision-making bodies aimed at providing support to the decisions taken by the Board of Directors, by delivering recommendations in light of expert analyses of selected themes, with the purpose to bring about greater efficiency and promptness with regards to the decisions taken. Incepted in 2005, the three existing Advisory Committees are made up of Board members and both internal and external experts, who are appointed on an annual basis by the Board of Directors itself, to which they report. These bodies are regulated by internal policies and procedure guidelines, which set up rules for their functions, as well as their duties and responsibilities.

Audit and Risk Management:
This committee aims to ensure that the Company's financial statements are prepared in an appropriate, comprehensive, transparent and trustworthy manner. It also ensures the effectiveness of internal and independent audit processes, as well as internal controls and compliance with the applicable legislation. It also supervises the management of corporate risks. It is made up of five members, three of whom are experts, and meets on a quarterly basis.

Human Talents:
This committee focuses on ensuring the proper valorization and development of Human Talents, within the best people management practices, in accordance with the Algar Group's different business segments. Among the regular issues that are covered by this Committee, of particular reference are the organizational climate, the development program for potential successors, leadership development, remuneration, dissemination of the Company's values and the Brazilian labor market scenario. It is composed of four members, which include a Board member and an outside expert, who meet on a yearly basis.

Corporate Governance:
This committee is made up of five members, two of whom are External members of the Board, whereas the others are members of each one of the three branches of the controlling family, and they meet once a year. This committee examines, assesses, monitors and makes proposals aimed at consistently seeking to enhance the effectiveness of the Company's corporate governance practices, on the grounds of the principles of transparency, fairness, accountability and corporate responsibility.

Executive Board

The Executive Board is composed of highly skilled professionals, who perform their functions geared towards the Company's daily operations. It is responsible for enforcing the corporate management policies, in line with the directives laid down by the Board of Directors, alongside with the applicable legislation and the Company's Bylaws. The Executive Board is composed of seven members, namely the CEO, the Deputy CEO, and six officers allocated in specific areas, who meet once a week on a regular basis, and at such other times as may be deemed necessary, with the purpose of aligning and taking decisions concerning strategic corporate matters.

Composition of the Executive Board on 12/31/2012

Divino Sebastião de Souza	Chief Executive Officer (CEO)
Jean Carlos Borges	Chief Operations Officer (COO)
Tatiane de Souza Lemes Panato	Chief Financial Officer and Investor Relations Officer
Marineide da Silva Peres	Chief Human Talent Officer
Luis Antônio Andrade Lima	Chief Operations and Technology Officer
Osvaldo César Carrijo	Chief Retail Commercial Officer
Márcio Estefan	Chief Corporate Commercial Officer

Tatiane Panato - Chief Financial Officer and Investor Relations Officer

Marcio Estefan - Chief Corporate Commercial Officer

Divino Sebastião - CEO

Jean Carlos Borges - COO

Luis Lima - Chief Operations and Technology Officer

Marineide Peres - Chief Human Talent Officer

Osvaldo Carrijo - Chief Retail Commercial Officer
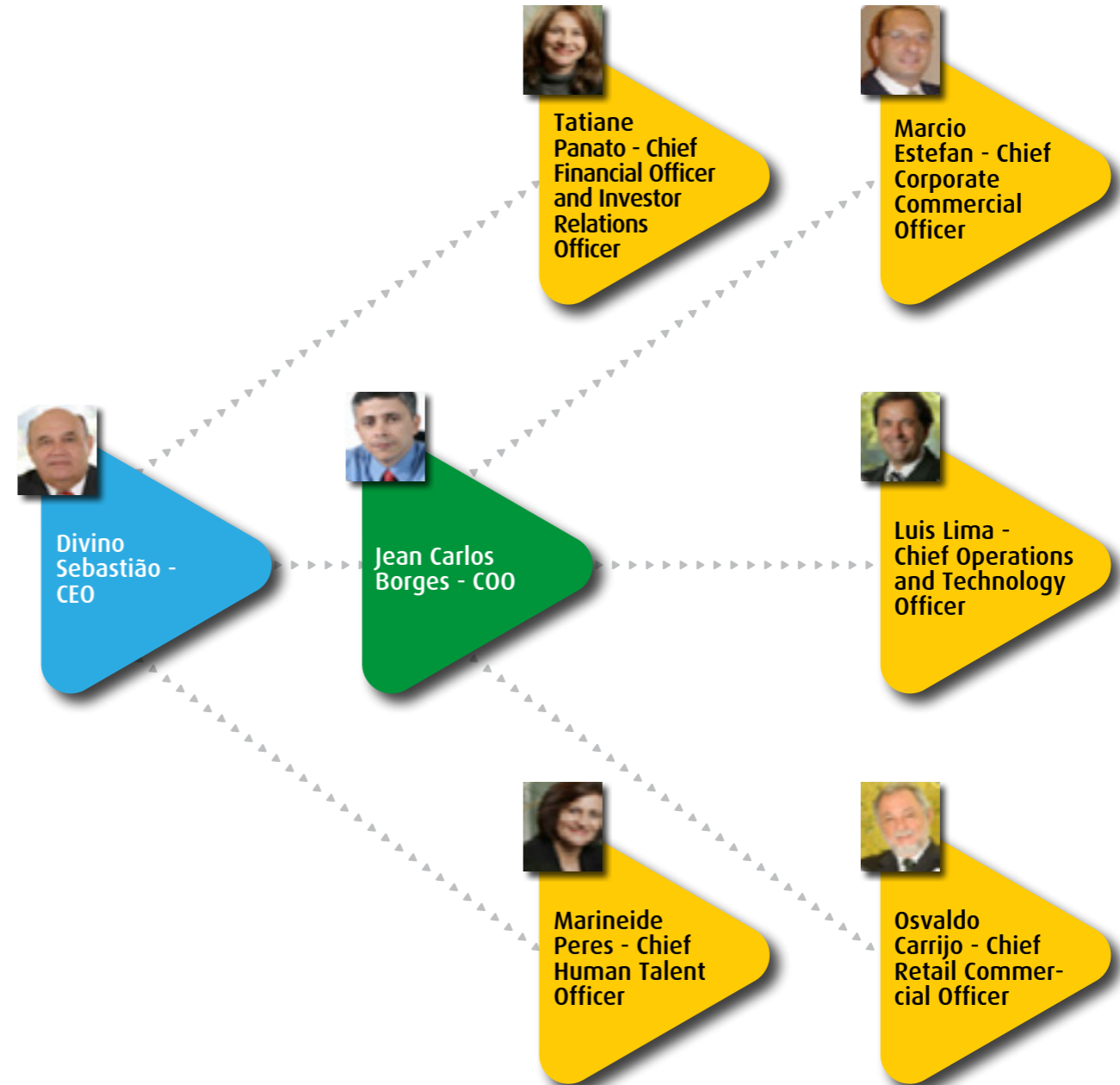
DIVINO SEBASTIÃO DE SOUZA

(CEO)

Mr. Souza holds a 35-year professional experience in the field of Information Technology, with particular emphasis on telecommunications. He was involved in the first implementation of mobile phone services in the inland region of the states of Minas Gerais, São Paulo and Mato Grosso do Sul. He was involved in the conception and creation of the Company's Contact Center (ACS), later renamed Algar Tecnologia (a provider of Business Process Outsourcing and IT), where he acted as the Superintendent Director for 8 years. He holds a bachelor degree in electrical engineering from Faculdade de Engenharia Elétrica de Ituiutaba (Minas Gerais State), in addition to post-graduation degrees in (i) Corporate Management, from Universidade Federal de Uberlândia; (ii) Strategy Management, from Insead, France, and (iii) Strategic Management, from Wharton University, USA.

JEAN CARLOS BORGES

(Chief Operations Officer)

With a 23-year professional experience, Mr. Borges started his career as an engineer at IBM Brasil, where he acted as a Commercial Manager in the states of Minas Gerais and Mato Grosso. He worked for Algar Tecnologia for five years, two of which as a Chief Financial Officer. He has been in the Company since 2003 and has held the positions of Chief Financial Officer, Technical-Operational Officer and Chief Governance and Strategy Officer. He holds a bachelor degree in mechanical engineering from Universidade Federal de Uberlândia, as well as post-graduation degrees in (i) Corporate Management, (ii) Controlling and Accounting, both from the same university, and (iii) Business Administration and Marketing from Universidade do Triângulo (Unitri). He also attended the Program For Executive Development (IMD) for two months, in Lausanne, Switzerland.

TATIANE DE SOUZA LEMES PANATO

(Chief Financial and Investor Relations Officer)

With a 12-year experience in finances, she has acted as the Administrative-Financial Coordinator at Algar Tecnologia, Controllership Coordinator and head of the Controlling and Planning Division at both companies. Ms. Panato has a bachelor degree in Accounting Sciences from Universidade Federal de Uberlândia and a post-graduation degree in Finances and Corporate Planning from the same university, an MBA in Corporate Management from Fundação Getúlio Vargas (São Paulo) and an MBA in Finance, Communications and Investor Relations from FIPECAFI.

MARINEIDE DA SILVA PERES

(Human Talent Officer)

Ms. Peres has a 32-year professional experience in the fields of Finance, Trading and Strategic Planning. She has acted as the Chief Operations Officer at PWC BPO Brasil (a provider of finance, accounting, human talent and procurement outsourcing services). She was the Chief Financial Officer for the Company for 10 years and, later, a Business Director at the Uberlândia Regional Office. Ms. Peres holds a bachelor degree in Business Administration from Universidade Federal de Uberlândia and a post-graduation degree in Corporate Management from the same university, She has attended professional development programs in the areas of Leadership, Marketing, Finance and Sales for Executives, with special reference for the Harvard Business School's Case Studies program and IMD's Executive Development Program, in Switzerland.

LUIZ ANTÔNIO ANDRADE LIMA

(Chief Operations and Technology Officer)

Mr. Lima has a 29-year professional experience in the telecom industry and has been involved in projects, implementation, operations and maintenance of telecommunication networks for fixed-line and mobile telephony, in addition to data communication. He has held several positions at the Company, such as project engineer, technical advisor of the Regional Operations Division in Franca (São Paulo State), General Operations Coordinator and head of the Strategic Project Division. He holds a bachelor degree in electronic engineering and an MBA in Advanced Business Management from Fundação Getúlio Vargas (São Paulo State). He also has attended specialization courses in Computer Networks at Universidade Federal de Uberlândia and holds a post-graduation degree in Business Administration from Universidade Algar. He has also attended a refresher course in Industrial Electrical Systems at Universidade Federal de Uberlândia, Minas Gerais State.

OSVALDO CESAR CARRIJO

(Chief Retail Commercial Officer)

With a 30-year professional experience in Retail and Technology, Mr. Carrijo founded and headed Universidade Martins do Varejo (UMV), as well as introduced and coordinated Grupo Martins's client relationship programs. He created and implemented Rede de Valor brand and Grupo Martins's Rede Smart de Supermercados. He has been a member of the Board of Directors for Le Postiche, as well as of the Academic Board of ENS and Universidade Cândido Mendes (Minas Gerais State). He has also developed several franchising and relationship marketing projects, including those of Le Postiche, Leo Madeiras, Marisol, Agora Sênior and Milenia. He holds a bachelor degree in civil engineering and specializations in Information Systems from IBM, in White Plains, USA; Food Retail from Fleming Retail University, Oklahoma, USA; and Advanced Management from Insead/FDC (Brazil/France).

MÁRCIO ESTEFAN

(Chief Corporate Commercial Officer)

With a 21-year professional experience in the telecom industry, Mr. Estefan has worked in Sales, Pre-Sales and Marketing at large telecom corporations, such as Telefônica, MetroRED, Comsat and Vicom. He holds a bachelor degree in electronic engineering from Universidade Federal do Rio de Janeiro, with extension courses in Marketing and Knowledge Management from Fundação Getúlio Vargas, Management from IESE, Spain, and Innovation from Wharton Business School, USA.

Evaluation of the Executive Management

The annual 360-degree evaluation process applicable to all of the Company's executives was incepted over 20 years ago. This approach allows for the assessment of both Algar's key competences and the specific ones attributed to each distinct position and the person holding the post, by means of analyses conducted by his/her peers, subordinates and superiors. This evaluation approach reveals the strengths and the aspects to be improved, and enables to outline an action plan, including the professional development of each executive.

Remuneration

The remuneration system adopted by the Company aims at aligning and uniting the efforts to enhance its performance. It entails both fixed and variable amounts, in addition to the package of benefits. The fixed portion includes the regular monthly salary, the proportional amount attributed to the vacation period, as well as the amount corresponding to the annual 13th salary.

The variable portion, which has become increasingly relevant, aims at stimulating and promoting financial reward to all executive and non-executive associates, and consists of two portions. The first one relates to the Result Sharing Program, representing an individual bonus based on meritocracy, in view of the associate having achieved any extra result, that is, which exceeds the expected targets for his/her area of activity. The second portion refers to the Profit Sharing Program, through which the Company distributes a percentage of the net income recorded each year, limited to a 12% share of total net earnings.

Furthermore, in line with the principles of consistency and fairness, the Variable Remuneration System takes into account the effect from deflators, by using the indicators deriving from the expected ensuing scenario based on pre-established assumptions, such as the annual growth rate, profitability and financial conditions.

GRI: 4.2

Audit

Algar Telecom is submitted to both internal and independent auditing teams, which report directly to the Board of Directors, through the Audit and Risk Management Committee, and in functional terms, report to the Holding Company, with a view to assuring autonomy in performing their tasks.

The Internal Audit consists of five people, whose mission is to promote independent assessment of internal controlling processes and the Group's performance, with a view to provide assistance to Management in fulfilling the corporate goals and in seeking maximization of the return to shareholders.

In addition to the Internal Audit Committee, Algar Telecom hires an independent audit company to perform the auditing activities on a quarterly basis, with the purpose to assess information standards and compliance with the current accounting legislation. Since 2009, this service has been performed by KPMG Auditores Independentes.

Code of Ethics

Within the global framework, corporations play a relevant role in the process of sustainable growth, by placing particular emphasis on the ethical conduct of business activities.

Algar Telecom has adopted a Code of Ethics that lays down the ethical principles and behavior conduct that must be followed by all associates with regards to their relationship with both the internal and external publics, regardless of their attributions and responsibilities, based on the concept of Sustainability, within the economic, social and environmental aspects. The Code of Ethics has been accessible on the Company's website to all related parties, and is an integral part of the Human Talent's General Policy, having been officially approved by all relevant bodies, including the Associates' Committee, the Executives' Meeting and the Board of Directors. For Algar Telecom, being a responsible company means upholding an ethical behavior on the part of its staff, throughout all aspects of the business, in addition to preserving the environment and keeping high standards of relationship with all stakeholders, by complying with the rules and guidelines established by the organization.

Users Council

Algar Telecom was a pioneer in the Brazilian telecom industry in 1999, by creating a Council that included the participation of clients. In 2008, when ANATEL, the regulatory body for the Brazilian telecom industry, introduced the requirement to organize a Council that included the clients' participation, by means of the Regulation ruling Councils of Users of the Fixed Switched Telephone Services, Algar Telecom only had to make a few adjustments to its ongoing practices. The Users Council acts as an advisory body, aimed at guiding, analyzing and assessing the quality of the services rendered, in addition to providing suggestions for improvements.

HUMAN TALENTS

Algar Telecom's professionals are called associates and the area that manages the policies geared towards the internal stakeholders is named Human Talents Area. More than mere words, the designations chosen express the deep respect for the people who are the soul of the Company and the other companies of the Group. This attitude comes in line with the concept of "Network Company" management.

The Group founder, Comendador Alexandrino Garcia, has always seen each employee as an agent of transformation of vital importance to a long-lasting business. After all, the willingness to fulfill their functions in the best possible way and the care and dedication in serving clients are very personal attributes. Based on this concept and with the purpose of boosting each one's natural talents, the culture of valuing people's talents was spontaneously developed in the Company.

In order to preserve the spirit of motivation and passion in serving the clients, which is well translated in the statement of the Company's Vision - PEOPLE SERVING PEOPLE, the Human Talents area works jointly with UniAlgar, the Algar Group's corporate university, in the quest for tools to foster the professional development of each member in the Organization, both in the personal and professional dimensions, promoting life quality, wellbeing and career development.

In 2012, Algar Telecom policy of fostering talents was once again acknowledged with the granting of awards. The Company was listed in the ranking of the best companies to work in Brazil, sponsored by Época Magazine, and of the best IT and Telecom companies to work in Brazil by Computerworld Magazine.

GRI: 2.10

ASSOCIATES' PROFILE

Algar Telecom's team is composed of professionals, whose characteristics are in line with the Company's DNA (Innovation, Empathy and Simplicity) and with Algar Group's essential competences, showing identity with the Organization's strategic plan and operations. Guided by the vision PEOPLE SERVING PEOPLE, the Company values people who are keen to develop relationships, who demonstrate their willing to help, besides showing a spirit of teamwork and a natural talent for innovation. These criteria enable both the Company and its subsidiaries to form efficient teams, geared towards the creation and development of innovative solutions, while keeping focus on both the client and quality, in addition to being concerned about sustainability.

Algar Telecom, in all of its segments, adopts the practice of hiring people with special needs. In the contact centers, for example, there are visually impaired professionals hired to work as masseuses, thus contributing to the initiatives intended to improve the associates' wellbeing.

Telecom
This segment encompasses fixed and mobile telephony, broadband, data transmission and pay-TV services, and closed FY 2012 with 1,816 associates.

Business Process Outsourcing and IT
The number of professionals in this segment at the close of 2012 stood at 10,096, versus 10,913 associates at the end of FY 2011.

Complementary Business
Engeset – Telecom Engineering closed FY 2012 with 2,139 associates. In turn, the segment of Phone Directories and Guides (Algar Mídia) ended FY 2012 with 300 associates.

ASSOCIATES (as at Dec/31)

FULL-TIME ASSOCIATES	2010	2011	2012
Permanent or Indefinite-Term Contract	4,989	6,224	6,385
Temporary or Fixed-Term Contract	31	22	8
Permanent Outsourced Contract	0	0	1
Pre-fixed or Temporary Outsourced Contract	21	41	40
TOTAL number of full-time associates	**5,041**	**6,287**	**6,434**

PART-TIME ASSOCIATES	2010	2011	2012
Permanent or Indefinite-Term Contract	8,921	8,812	7,955
Temporary or Fixed-Term Contract	1	2	3
Permanent Outsourced Contract	0	0	0
Pre-fixed or Temporary Outsourced Contract	4	1	93
TOTAL number of part-time associates	**8,926**	**8,815**	**8,051**

TOTAL (full-time + part-time associates)	**13,967**	**15,102**	**14,485**

Part-Time   Full-Time
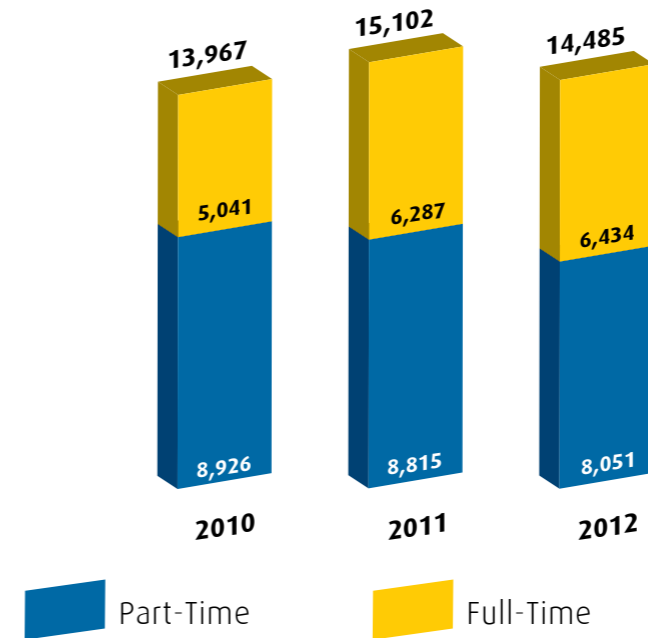
Age group (own associates)	2010	2011	2012
>50	411	509	499
30 to 50	4,590	5,272	5,537
<30	8,941	9,279	8,315
Total	13,942	15,060	14,351

GRI: LA1

Turnover

As described throughout this chapter, the Company promotes a number of initiatives intended to value human talents, which contributes significantly to decrease the consolidated turnover, which stood at 61.1% in 2012. This result predominantly reflects the turnover of 59.1% posted by the Business Process Outsourcing and IT segment, due to the nature of the contact center area. This ratio came to 20.0% in the Telecom segment. The turnover ratio is even lower in the Complementary Business Units -- 2.9% for Engeset and 21.0% for Algar Mídia. Algar Telecom holds no information on the turnover ratio per region.

ASSOCIATES – as at Dec.31/2012

	Indefinite-Term Contract		Permanent or Indefinite-Term Contract	
	Total Number of Dismissals	%	Total Number of Dismissals	%
Per Gender				
Male	2,759	19.2%	3	0.0%
Female	6,014	41.9%	8	0.1%
Total	8,773	61.1%	11	0.1%
Per Age Group				
>50	141	0.9%	1	0.0%
30 to 50	2,449	17.1%	2	0.0%
< 30	6,183	43.1%	8	0.1%
Total	8,773	61.1%	11	0.1%

GRI: LA2

Corporate University

The Algar Group's Corporate University – UniAlgar - is the main ally to the Human Talents Area of Algar Telecom. This strategic tool to the human and professional development of all associates is located in Uberlândia (Minas Gerais State), in a green space that covers 32,600 m². UniAlgar was created in 1998, with the mission to develop internal human talents, thus contributing to the sustainable growth of all the Algar companies.

The institution distinguishes itself from conventional universities, since its academic programming is based on real corporate concepts and practices, focused on the needs of Algar companies. In addition to on-site programs, the teaching approach is supported by tools such as online training, chats, discussion forums, hot-sites featuring relevant content and social networks.

UniAlgar is also dedicated to themes such as dissemination of corporate culture, performance evaluation, and climate survey, emotional and physical health management of the associates, personal and professional development and carrier plan. In other words, it aims at fostering all initiatives to ensure a pleasant workplace environment, with real perspectives for building successful careers. Consequently, it is also the repository of the knowledge accrued by Algar Group Companies.

For the performance its activities, UniAlgar enjoys an excellent physical infrastructure. UniAlgar's three buildings host 17 training rooms and other five rooms intended for meetings, an auditorium with capacity for 600 people, a library with over 4,500 titles, a restaurant, a cybercafé and a bookshop.

The work developed by the corporate university contributes to the recognition that Algar professionals enjoy in the marketplace and is acknowledged by awards. In 2012, UniAlgar was elected the best Brazilian Corporate University by the International Quality & Productivity Center (IQPC), an international organization of corporate information, which assessed other national and international corporations that operate in the country.

GRI: 2.10

Relationship with Internal Stakeholders

Training and Development

The Company's ongoing program of professional training and development made available to associates is one of the driving forces in promoting Algar Telecom's growth. Knowledge updating enhances professional quality of the staff, thus contributing to raise their levels of employability. To that end, the Group has been increasing the number of hours and the amount of funds allocated to training programs every year. A total investment of R$ 12.8 million and a number of 353,000 class/hours were registered in 2012. These figures include all Company's segments and correspond to an average investment of R$ 890.51 per associate. In the Telecom segment alone, the average investment per associate climbs to R$ 4,078.22.

Segment	Amount invested (R$`000)	Class/hours	Amount invested per Associate
Telecom	7,406.0	122,125	4,078.22
Business Process Outsourcing and IT	3,859.3	195,456	382.26
Telecom Engineering	1,094.7	28,582	511.78
Directories and Guides	419.7	6,405	1,399.02
Consolidated Total	12,779.7	352,568	890.51

In 2012, the training programs were engaged by professionals of all Algar Telecom's levels (Officers, Directors, Coordinators, Consultants and non-executive associates), covering technical (74%) and behavioral (26%) topics. The access to online tools intended to strengthen professional skills has also gained in relative importance. In 2012, the Company offered 9,190 programs in this format, which were attended by 64,400 associates.

A major share of the training initiatives is made feasible by UniAlgar, whereas specific courses are held outside the Organization. In 2012, the corporate university and the Human Talents area joined efforts to create a development program designed to meet Algar Telecom's strategic needs stemming from its mission "Serve and integrate people and business in a sustainable way". That was the main driver behind "Programa Integrar" (Integrating Program).

It consists in a continuous educational program, featuring cycles of up to 36 months, which not only contribute to the development of talents with a view to enhancing the Company's results, but it also aims at retaining and transferring key knowledge, whose task is conducted by professionals who act as multipliers. It also allows for the accrual of statistics to back up the monitoring of the Company's goals.

In the initial stage, held during the August-December 2012 period, "Programa Integrar" covered 83.3% of associates. A total number of 47 multipliers were trained and 15,326 certificates were granted to 1,685 different associates who took part in at least one of the training programs.

The partnership between UniAlgar and the Human Talents area has developed further programs. One of them, in the area of commercial culture, involved a training program intended to promote professional development to the consultants of Key Account Managers (KAM), who act in the Prime Corporate Club, created to serve a distinguished group of clients, with potential to consume the Company's products

and services from different business segments. In 2012, the Company also formed the first group of 30 trainees under the Jovem Empreendedor (Young Entrepreneur) Program, aimed at attracting, developing and retaining young talents, in preparation to perform functions in the future within the Group's different segments. Algar Telecom also offers professional development opportunities abroad, which are subsidized by the educational aid granting policy. Benefit program. Supervised by the Associates' Committee, this program grants subsidized funds that can reach up to 50% of the monthly tuition for undergraduate, graduate, MBA and masters degrees.

GRI: LA10, LA11

Health and Wellbeing

At Algar Telecom, the concern with life quality and wellbeing of associates is evidenced in a number of practices that exceed by far the legal requirements. In this sense, the highlight in 2012 was the extension of "PDI da Saúde" – a program to promote life quality that was initially meant only for executives – for all the Company's associates.

Within this program, after clinical, physical and nutritional evaluation, these professionals receive guidance and constant motivation to fight sedentary lifestyle, obesity, stress and other factors that affect life quality. In the case of executives, the fulfillment of targets affects the calculation of the variable remuneration. In 2012, 100% of the executives were considered to have an active lifestyle. Ten years ago, that figure stood at 34%. Among the associates, this program covered 74% in 2012. The Company expects to extend it to 100% of the associates by 2015. Still in the area of health and life quality, Algar Telecom maintains a multidisciplinary team in its headquarters, consisting of a doctor, a nurse, social assistant, a safety technician and a safety engineer. In addition, it develops a series of specific initiatives within the Life Quality Program, such as labor gymnastics and massage facilities spread across the company.

The Company also maintains an Internal Committee for Accident Prevention (CIPA)

in all of its operational units with at least 51 associates, in compliance with the Brazilian legislation. The committee is formed by representatives appointed by the Company, whereas the members elected by the associates have the role of monitoring and reporting risk conditions in the work environments, as well as of requesting measures to reduce and/or eliminate existing risks. In 2012, 92% of the associates were represented by this type of formal health and safety committee.

GRI: LA6

Algar Telecom benefits policy entails the subsidy of a private pension plan (with co-participation of the Company in the executive positions), day care aid, meal allowance and differentiated health plans for each region, with the intent of providing the best framework conditions to all associates, regardless of the geographical area where they work. Moreover, Algar Telecom holds a partnership with mobile ICU services for situations that demand on-site assistance, in addition an optional integration plan as a complement for medical procedures that are not covered by the regular health plan.

In case of sick leave that lasts more than fifteen days, Algar Telecom complements up to 40% of the associate's salary. The health assistance aims at allowing the associate to maintain his/her level of income for a period as long as two years. The Company also offers monetary assistance for associates who are parents of children with special needs.

Created by the associates, the Algar Telecom Credit Cooperative grants personal loans at subsidized interest rates, lower than the rates practiced by the financial market, contracted upon the associate's request, with payments ranging from 1% to 10% discount in the payroll (at the associate's discretion), intended to the acquisition of consumer goods. The associates are also entitled to special discounts for the purchase of Algar Telecom products and services.

Another differential of the Company's benefit policy is the vacation bonus, which is equivalent of the base-salary (the value includes the 33%-additional payment provided by law). With a focus on the associates' wellbeing and satisfaction, the Company also takes initiatives such as movie and theatre sessions during the lunch break, organization of soccer championships, tracking and other events. Flexible schedules and the home office schemes are also an option, provided that the associate's function so allows.

RATES OF INJURY, OCCUPATIONAL DISEASES, LOST DAYS AND ABSENTEEISM, AND TOTAL NUMBER OF WORK-RELATED FATALITIES PER REGION

	2010	2011	2012
Total Headcount (Own + Outsourced) => Same Figures as in LA1	12,212	12,781	12,253
Injuries			
Injury Rate (IR)	0.06%	0.06%	0.11%
# of Injuries	7	8	14
Occupational Diseases			
Occupational Disease Rate (ODR)	1.11%	0.77%	0.19%
# of Occupational Diseases	136	98	23
Days Lost			
Lost Day Rate (LDR)	ND	ND	ND
# of Lost Days	ND	ND	ND
Absenteeism			
Absenteeism Rate (AR)	ND	ND	ND
Scheduled Work Days	ND	ND	ND
Fatalities			
# of Fatalities*	0	0	0

As regards occupational safety, the Company's initiatives have been yielding a sharp decrease in the number of occupational diseases. In 2012, 23 cases were registered, which corresponds to a 0.19% ODR (Occupational Disease Rate). In contrast, there were 98 cases in 2011, a 0.77% ODR. As for injuries, there were 14 cases in 2012 versus 8 in the previous year, representing a 0.11% increase in the IR (Injury Rate). The data above do not include the Engeset figures.

GRI: LA7

For the calculation of both IR and ODR, Algar Telecom does not include outsourced workers who are responsible for the installation and maintenance of antennas, base stations and other facilities. In this case, the Company's policy is to require that service providers require their employees to use safety equipment, undergo medical examinations and have proof of completion of the "Height Work Safety Training Course" pursuant to NR8. The work sites are visited and audited to ensure compliance with such requirements.

GRI: IO3

With regards to the policies and practices related to antenna installation, including stakeholder consultation, shared facilities and visual impact-related initiatives, Algar Telecom take as a base the applicable legislation in force in each municipality. Whenever it is necessary to build a vertical structure, the Company previously checks the possibility of sharing an existing structure (tower), always making sure that it meets the project height and soil-related requirements. When it is really necessary to build a new tower (for mobile technology), the Company hires a qualified supplier, which becomes liable for the whole licensing and construction process of the new structure, in compliance with the applicable legislation in force in the municipality.

GRI: IO7

Career building

Attracting and retaining Human Talents is one of the main challenges faced by the companies that operate in the segments of Telecom and Business Process Outsourcing and IT. With a view to stand out in such a competitive market, differentiating itself by relying on a highly qualified team of professionals, Algar Telecom has structured a fair remuneration policy, tied to a meritocracy scheme and a transparent career plan, which enables associates to envisage their possibilities for further growth.

One of the most effective tools geared towards the Company's career plan is the performance evaluation, which is formally undertaken at least once a year. This evaluation, while assessing the individual performance, results in a target-related development plan, intended to stimulate each associate to accomplish his/her goals. In 2012, 10,367 associates underwent performance evaluation, accounting for 72.2% of the total headcount, not including the associates of the segments of Telecom and network engineering business, whose evaluation programs are scheduled to finish by May 2013. The goal is to complete 100% of the performance evaluations during the course of 2013.

GRI: LA12

Another procedure to value the human capital is to search, within the Company's own base of associates, for qualified people to occupy the new positions that emerge, prior to announcing them to the market. In 2012, 2,339 associates were promoted at the Company, 168 of whom in the Telecom segment, 1,709 in the Business Process Outsourcing and IT segment and 462 in Complementary Businesses.

Promotions contribute positively to the Company's climate and, at the same time, enable to close one of the largest gaps in the sector, which is the scarcity of skilled workforce at all levels. Identifying and training talented professionals

to take on key positions in the Company are initiatives covered by a specific program, "Talentos em Desenvolvimento" (Talents under Development). Since 2011, when the program was launched, fifteen talents from the segments of Telecom e Business Process Outsourcing and IT have been promoted, representing 20% of all associates who took part in the program. In October 2012, this same program was implemented in the network engineering business, and relies on the participation of 25 professionals.

Algar Telecom also develops differentiated initiatives that contribute to both the associates' employability and their retirement planning. Among these actions, of special reference are the support to outplacement services, professional development and assistance during the transition to retirement.

The Company keeps a good relationship with unions - in 2012, 98% of the associates were benefited by collective bargaining agreements. At Algar Telecom, professionals in management positions did not benefit from the negotiation, since they enjoy specific remuneration policies. In April 2012, Algar Telecom distributed a total bonus amount of R$ 13.9 million related to the profit sharing program based on the previous year. The distribution benefitted 89% of the associates.

GRI: LA4

Communication Channels

The Algar Group, of which Algar Telecom is a subsidiary, provides different communication channels to interact with its associates. One of them is TV Algar, an exclusive corporate TV show that can be viewed on computers, mobile devices or televisions installed in regional offices. Algar Telecom takes part in all the show episodes, with topics of interest to its associates.

The main facts and achievements related to Algar Group are also reported by Toda Hora (Every Hour), formed by frames of short and informational texts accessed by computers and broadcasted in the screens available in the Company's convenience sites.

Algar Telecom associates' intranet was fully reformatted in 2012 to include information such as internal contact lists, agenda, Library of Procedures and Processes, useful links and the Human Talents Portal, an exclusive channel to the Human Talents area, used to disseminate the Company's culture, benefits, new posts opportunities, compensation policy and other related topics.

The Group's associates may also access the Algar Net, a corporate communication channel that features services such as vacation leave application, salary and remuneration statements, in addition to Conect@ - a Distance Learning training channel, offering training programs customized to each associate.

Human Rights

Algar Group rejects any kind of discrimination and adopts all applicable measures to prevent this type of conduct in its business. In 2012, two cases of sexual harassment in Algar Tecnologia were reported to the Ombudsman. The Ombudsman team investigated the reports, examined both evidences and recommended the dismissal of the leaders responsible for such acts, which was executed by the Company. In addition, as an improvement measure, workshops addressing themes such as moral damages and sexual and moral harassment were scheduled to be offered to all leaders, to be held during the first half of 2013.

Since its inception in 1994, the Algar Tecnologia's Ombudsman area has received, recorded and examined over 17,000 complaints, charges and criticisms, related not only to discrimination, but also to several issues relevant to associates. With a workflow that allows for listening to internal stakeholders, investigating their claims and recommending improvements in processes, procedures and leadership development, the Ombudsman has made many contributions to Algar Tecnologia and its associates. Its permanent goal is to constantly decrease the number of complaints forwarded to the unions, the Ministry of Labor, postings on social networks, as well as to consumer protection bureaus, by fostering an environment that makes associates feel valued and proud of belonging to the Organization.

Also concerning Human Rights, the Code of Ethics adopted by all the Algar Group's companies set out that no partners or suppliers that use slave or child labor be accepted. In 2012, no cases of child labor were identified at Algar Telecom. To avoid partners and suppliers that employ slave or child labor, the area of labor safety requires specific documentation from the outsourced companies (employment card, associates' information sheet, health exam and proof of payment of all labor taxes – FGTS, PIS and COFINS), and performs regular inspection visits to partners and suppliers, with a view to confirming the absence of such conditions.

GRI: HR4, HR6, HR7

Serving

MESSAGE FROM MANAGEMENT

Algar Telecom will always remember 2012 as a year of intense work, overcoming challenges and making great strides. It was a period in which it faced a challenging economic and industry environment. In the international arena, the lingering crisis in Europe, the slowdown in China and the sluggish recovery in the U.S. all contributed to a drop in exports and, consequently, in the inflow of U.S. dollars into Brazil. In Brazil, economic activity was affected by low investment levels due to these uncertainties, mainly in the first half of the year; as a result, GDP grew a disappointing 0.9% in 2012. In addition, the service industry continued to face cost pressure from talent maintenance and retention.

This adverse situation was even more challenging for Algar Telecom, the only telecom company fully owned by Brazilian investors. The Company relied on efficient strategic planning to make wise decisions, in order to become more competitive, increase liquidity, sustain investments and continue expanding geographically and attracting clients. As a result, it had 2.3 million Revenue Generating Units, and recorded consolidated net revenues of R$1.8 billion and net income of R$141 million at the close of 2012.

On the financial front, the Company had a major success. The market responded very positively to its second issue of debentures, which exceeded the minimum levels required by the Novo Mercado de Renda Fixa (New Fixed Income Market) rules and amounted to R$358 million. However, we restricted ourselves to R$294 million, which corresponds to the 35% additional amount permitted by regulations. At the end of the process, we had a very diverse group of investors. The new capital inflow allowed the Company to pay in advance 97% of the outstanding balance of the first issue debentures, issued in 2007 and maturing up to 2014. As a result, the Company was able to extend its average debt maturity while sustaining its cash reserves, needed to continue expanding its businesses focused on the corporate sector.

There were also changes in the operational environment of our business. Always at the forefront of new technologies, Algar Telecom continued to offer ultra-broadband services to the retail market and expanded its pay TV package, which currently comprises over 170 channels, 44 of which in high-definition. Concerning client relations, we expanded SAC 2.0, which is now part of other social networks, and introduced Clube Corporativo Prime (Prime Corporate Club), created to cater to a group of special clients that may buy products and services from the Company's different business segments.

In the Minas Gerais State expansion area, in which Algar Telecom started operating in late 2011 when it obtained the Band H license, we consolidated our position in the 19 new cities where we offer fixed-line phone, 3G mobile phone, broadband internet and pay TV combo packages.

The efforts to strengthen the Algar brand greatly contributed to the great expansion in the corporate market, one of the Company's key target markets for expansion. The strategic initiatives focusing on this niche comprise top-quality cost-effective solutions and close relationships with clients. In addition, we opened Casa Algar in São Paulo City in 2012 and are planning to open more of these facilities in 2013. That will bring us closer to our current and prospective clients, thus making the Company even more competitive and strengthening Algar Telecom's presence in state capitals.

We confidently stress that our achievements in 2012, as well as others that have always marked the Company's history, resulted from the unique way we serve our clients on a daily basis, regardless of where they are based. Algar Telecom, as well as all other Algar companies, follows its vision PEOPLE SERVING PEOPLE in all its initiatives. These words concisely describe our unique way of doing business, in which all investments in infrastructure and human capital focus only on offering quality and good services to satisfy our clients.

All this dedication and focus were essential for the Company to overcome the challenges and improving client satisfaction. In fact, satisfaction rates came to 86% among corporate clients and 72% among retail clients, considered high in the industry. In addition to Algar Telecom's professionals' performance, this recognition was also due to our competitive intelligence initiatives, risk management policies and improved Innovation Program, which pervades and is expanding throughout the organization and is a key component in our search for product and service quality.

We are immersed in a culture of innovation. Proof to that is the R$43-million profit that Algar Telecom has achieved since 2007 by developing new platforms, processes and equipment, in addition to the gains that it made by insourcing knowledge and remaining independent from international suppliers. To make even greater strides in innovation, we invested in innovative ideas and projects that may help the Company reduce costs and become more competitive. As a result, the Company was ranked the most innovative telecom company in 2012 by consulting firm A. T. Kearney, in a ranking published by Época Negócios magazine.

Our policy of valuing human talents is widely recognized as well. We offer a career path with clear opportunities for growth, adopt a merit-based management model and are committed to our professionals' quality of life and well-being in and out of the Company. Our most significant advance in this regard in 2012 was extending PDI da Saúde, a life quality program initially offered to executives only, to all associates.

We also invested heavily in job training programs in 2012. It is worth noting the Integrar (Integrate) Program, designed by UniAlgar, the Group's corporate university, especially to bring all Algar Telecom's associates closer to the Company's strategic goals. In 2012, investing in professional development helped improve services in the segments of Business Process Outsourcing and IT, mainly concentrated at Algar Tecnologia, whose data center in Campinas, São Paulo State, was enlarged by 30% to cope with the expansion of operations, and of Engeset, which is in telecommunications engineering. Likewise, Algar Mídia focused on training sales professionals in the specifics of digital media, which have a great growth potential in the near future.

The expansion of our operations and other developments described in this Annual Report resulted from our good corporate governance practices as well, including the involvement of the Board of Directors, a risk management policy that improved considerably in 2012 and our commitment to sustainability at all levels.

In addition to business perpetuity, Algar Telecom's management model seeks to promote value creation throughout its relationship chain. As a result, our environmental policy goes far beyond the effort to mitigate environmental impact. Our main purpose is to enable and encourage our associates, clients, suppliers and communities to contribute to the future of the planet. This effort, which we call internally Influência Verde (Green Influence), is supported by a series of practices designed to increase energy efficiency, promote correct waste disposal and reduce greenhouse gas emissions, for example. On the social front, Algar Telecom invested over R$5 million in 2012. The direct investments from the Company and those from tax incentive laws were allocated to educational initiatives developed by Instituto Algar and cultural events held in the fifteen cities in which the Company is present.

We started 2013 ready to face the future challenges. We believe in a more favorable economic environment, which will lead to increased demand from the corporate market niche, to which our expansion strategy is directed. We also believe that the new investments, coupled with ANATEL's regulatory measures, will allow Algar Telecom to compete more aggressively in the mobile phone market. However, we have no doubt that the Company's success will always be related to its ability to provide a unique experience for clients. Therefore, we are going to continue investing heavily in innovation and human talent management, in addition to infrastructure.

We take this opportunity to thank all the people who are part of Algar Telecom's history—clients, board members, regulators, governments, creditors, associates and suppliers—and reaffirm our commitment to being a unique Company where everyone is glad to help build a better world.

Divino Sebastião de Souza
Algar Telecom's CEO

Luiz Alberto Garcia
Chairman of the Board of Directors

GRI: 1.2, 2.9

STRATEGY

Over the last years, Algar Telecom has been standing out in the Brazilian market, due to its consistent achievement of the maximum grade of the "Customer Care Performance Index" (IDA), created by the Brazilian Telecommunications Agency (ANATEL) intended to measure the companies' quality of customer care. This relevant acknowledgement evidences the correctness of the Company's strategic goal: to become a benchmark in customer care and relationship.

The Company's distinguished quality of customer care and relationship has been fulfilled primarily due to the constant investments in human talents, coupled with the disseminations of the culture laid down by the founder of the Algar Group, Alexandrino Garcia, whose motto has been perpetuated across all of the Group companies through both the Value "Client, Our Reason for Being" and the Vision "PEOPLE SERVING PEOPLE". Such guiding principles have enabled Algar Telecom to form a highly skilled team, who show a passionate focus on people.

The Company's strategic planning also considers the development of sustainability initiatives, the enhancement of corporate governance practices, and the complementarity of operations. The synergy captured between the three business segments - Telecom, Business Process Outsourcing and IT and Complementary Business – is crucial to enable Algar Telecom to consistently enhance competitiveness, in addition to surprising the clients with efficient and innovative solutions, alongside a friendly, close and pleasant relationship, based on both the way of being and conducting business of Algar.

Algar Telecom's bold and confident approach, which has paved the way to become the most effective company in the telecommunication services segment. This achievement is also backed up by the Company's distinguished management model, which bolsters the attainment of goals, engaged by the whole team of associates, coupled with the culture of innovation that fosters the development of solutions that yield creation of value to all stakeholders.

Network Company Management Model

Algar Telecom believes that achievements result from each associate's effort and ability to innovate. This belief led to the challenge of introducing participative business management at all levels. Since 1990, the Company has adopted the Algar Group's management model, called Network Company.

This model has clear processes announced widely and involving all associates, regardless of their positions. It also has tools to foster commitment and autonomy with responsibility, thus allowing each professional to follow and play an active role in the decisions that guide the Company.

In practice, each business segment of Algar Telecom is considered a Results Center and has its own budget and goals. The Board of Executive Officers manages all of them strategically by aligning them with the goals set jointly with the Board of Directors. However, after budgets are approved, each Results Center has full autonomy to execute its planning, which results in greater promptness in the decision-making processes.

Applied for over two decades, this management model has proven efficient in motivating associates, since it fosters a culture in which all are ready to make suggestions, listen to criticisms and, above all, learn. This participative process strengthens associates' sense of belonging and commitment, and makes them proud of the results achieved by the teamwork.

The efficiency of Algar Telecom's management model has enabled the Company to capitalize its businesses, within a market environment characterized by fierce competition, by enjoying a track record of consistently solid operating cash flow generation, coupled with low financial leverage. In this sense, in early 2013, the ratings agencies Standard & Poor's and Fitch upgraded the Company's rating to AA- Brazilian Scale.

Innovation

The history of Algar Telecom shows evidences that, since its foundation, innovation has been a fundamental tool to back up the Company's differentiation strategy, within a service rendering industry disputed by major worldwide players. Among a series of pioneering initiatives, of special reference was the installation of Brazil's first optical communication system in Uberlândia in 1984. Years later, in 1992, Algar Telecom launched the mobile telephony service to the inland region of Minas Gerais State, even before it was available in several Brazilian state capitals. Six years later, in 1998, it was the first company in Brazil to offer pre-paid phone services, currently predominant in Brazil's mobile phone system.

With a view to strengthening this pillar that an integral part of the Company's culture and processes, Algar Telecom has launched a specific program that relies on its own budget, with the participation of the Innovation Committee. This group made up of professionals from different areas is responsible for assessing and coordinating the introduction of projects that may lead to improvements, savings or new revenues, and disseminate the culture that encourages associates' commitment to generating ideas. This committee is connected with the Algar Group's Innovation Advisory Committee, in charge of disseminating the innovation policy throughout the Algar companies.

The motivation that encourages the presentation of innovative ideas is supported by the "Process Management Program" (PGP) and the "Idea Management Program" (PGI) methodologies, geared towards improvement projects for all business segments. Moreover, technical and financial support is granted by the Algar business incubator for the execution of prototypes that are likely to generate new business, Once approved, associates' ideas are developed, and contributors are rewarded financially. The projects delivered to the Algar business incubator are incorporated into the Company's portfolio, and sometimes they may also give rise to a new company, of which Algar becomes a partner.

The best initiatives presented during the course of 2011 were displayed at the Algar Innovation Exhibition, hosted by Algar Holding, outside the city of Uberlândia, at Algar Tecnologia's headquarters, in Campinas, on July 4, 2012. The event was attended by over 1,500 associates, clients, suppliers and other guests.

In 2012, Algar Telecom developed 10 innovative projects, which produced R$ 13 million in revenue. Since 2007, the accrued revenues deriving from this program amount to over R$ 43 million.

Apart from the generation of revenues, Algar Telecom's innovation culture is reflected in the appreciation that the Company enjoys in the market. In 2012, its expertise in coordinating marathons with the participation of students conferred the Company the privilege of hosting, in Uberlândia, the Minas Programming Marathon, which was engaged by 150 students from 21 universities located in the state of Minas Gerais.

The acknowledgement of the value attributed to Algar Telecom's innovation culture is also expressed in terms of awards. Algar Telecom ranked Brazil's 10th most innovative company (1st among telecom companies) in the Best Innovator category, published by the Época Negócios magazine in 2012, which also nominated the twenty companies that achieved the highest results based on innovation. The Company also won the first place in the Technology, Media and Telecommunications category, and received the prize The 100 Most Innovative Companies in the Use of IT, sponsored by IT Mídia and InformationWeek Brasil. The first place was attained due to the Sales Portal case, which was designed by means of an innovative architecture, enabling the Company to attain further improvement in delivering services to its clients.

GRI: 2.10

Growth Strategies

Algar Telecom's growth strategy is focused on geographical niches that enjoy corporate and retail market opportunities. In 2012, the delivery of voice and data services for medium-sized and large companies has kept the uptrend, by achieving an 18% growth in revenues, which reiterates the fact that the corporate segment stands out as the main driving force that shall boost the Company's growth for the upcoming years.

Even though the Company is allowed to extend the offer of these services throughout Brazil, Algar Telecom's strategy has been concentrating on providing top-quality speedy data services through a modern IP network in the best areas around its backbone from a commercial perspective. The Company's circular long-distance fiber optic network of 12,000 km in length managed to cover 70 cities in the Southeast, Mid-West and South regions of the country, including major metropolitan areas such as São Paulo, Campinas, Ribeirão Preto, Goiânia, Brasília, Belo Horizonte, Juiz de Fora, Rio de Janeiro and Curitiba.

The amount of investments earmarked for the expansion of the Company's participation in the B2B market also involve brand strengthening and further enhancement of the Company's commercial area relationship efforts. During the period, Algar Telecom, in partnership with HSM Management, promoted five events focusing on sharing of management and quality content with its clients. Moreover, it also invested in marketing campaigns broadcast by channels oriented to the target public.

From a commercial perspective, the creation of the Prime Corporate Club was rather fruitful. This program was intended to bring together different business areas, with the purpose of promoting a better understanding of their clients, assess needs and propose the best solutions. Initially, the portfolio was composed of eighteen accounts, which are served by the Key Account Manager (KAM) consultants, sales professionals who have received special training developed by UniAlgar. In 2012, the activities performed by the Prime Corporate Club Clube Corporativo Prime strongly contributed to increase revenues from this client group.

The regional offices, representing a significant competitive edge aligned with the Algar Telecom's way of serving, have also played a major role in conducting the strategy of bringing the Company closer to its clients, thus strengthening the brand in the market. In this sense, the highlight in 2012 was the inauguration of the Algar Group's headquarters in the city of São Paulo. For 2013, further inaugurations are planned to take place.

In the retail segment, main strategic focus for the coming years is the expansion of Band H, the last frequency band available for 3G telecom services in Brazil. IN 2012, Algar Telecom completed the full payment for the concession acquired at an auction held by ANATEL in December 2010, for the total amount of R$ 30.6 million. Furthermore, the Company consolidated its presence in the first group of 31 cities (Area Codes 34, 35 and 37), by offering packages that combine services of fixed and mobile 3G telephony, broadband internet and pay-TV.

Just as in the corporate market, the quality of customer service and close relationship, features that regional offices mostly benefit from, is one of the key stepping stones towards growth in the retail segment of the new cities encompassed by the expansion project, as well as in the 87 municipalities located in the Company's concession area. With a view to placing a competitive proposal on the market, the Company also invests in technology and innovation. The search for process improvement, which enables the enhancement of quality and cost reduction, is crucial to remain competitive within such a market disputed by major players.

Other major highlights that marked the year 2012 have come to signal a positive outlook for growth in the retail segment for the next years. One of them, of regulatory nature, was the "General Competition Goals Plan" (PGMC), introduced by ANATEL, which requires the largest companies of the industry to share their infrastructure with the smaller ones. This compulsory sale, which benefits the mobile telephony segment for a niche-oriented company such as Algar Telecom, will add part of the traffic network capacity, as well as a further availability of space for the accommodation of cables through ducts, trenches and towers of the companies classified as "Significant Market Power".

As for the pay-TV segment, the positive expectations derive from the launch of the HD 44-channel package, which extends the Company's service package offer to over 170 channels. The results for the next years are also expected to be positively impacted by the investments in the amount of R$ 40.5 million carried out during the 2012-2013 period, in the improvement of physical network to support the Ultra Broadband internet access – a higher speed service target to A and B classes, as well as to micro and small enterprises.

The segment of Business Process Outsourcing and IT, targeted to large companies, enjoys growth rates that exceed the rates of the country's GDP. Recent data published by IDC and Gartner have pointed to the maintenance of this trend. This segment has registered growth rates that exceeds the sector's average over the last years, due to the increase in business with existing clients, coupled with the geographical expansion, both in commercial and operational terms.

Relationship is a key factor to promote growth, and for this reason the Company seeks to maintain a close communication with its clients, with a view to jointly develop customized solutions that confers more efficiency and efficacy to all processes. The Company's current growth strategy aims at concentrating efforts geared towards the strengthening its brand image, resulting from its participation in events and the sector-related publications, press relations, use of new social media tools, and reinforcement of relationship with its clients' base.

Internal service quality programs were developed to support growth. A good example is Top Performance, designed to increase productivity and improve service quality at the contact center. The results of this program reshaped Algar Tecnologia's management, and the program was replicated for the other products and all support divisions.

GRI: 2.9

Risk Management

The corporate risk management is an integral part of all strategic and operational processes, and aims at preserving and creating value to Algar Telecom, its shareholders and the other stakeholders. In line with both the best corporate governance practices and the Algar Group's directives, the Company holds a committee, which directly reports to the Board of Directors, alongside a well-structured risk management policy, shared with all related parties.

With the purpose to identify, assess, classify and prepare he action plans to mitigate the different risks inherent to the Group's business operations, the Risk Audit and Management Committee makes use of the Enterprise Risk Management (ERM) methodology, adopted by the Committee of Sponsoring Organizations (COSO), an international organization that sets out and disseminates the best risk management, internal controls and fraud detection practices.

The committee is responsible for monitoring the compliance with the rules set out by the Algar Group's Risk Management System, without losing sight of the principles established by the management model – among which, "Autonomy with Responsibility". Cases involving conflicts of interest must be identified, assessed and treated in accordance with the best corporate governance practices.

In 2012, the Company experienced a solid reinforcement of its risk management policy, by executing the action plans related to the strategic risk control, which had been mapped in previous years. At present, the Company seeks to mitigate the different types of strategic risks found in Algar Telecom, Algar Tecnologia and in Engeset, which take into account the sector's regulation, the market, the business management, availability of workforce, supply of raw material, third-party default, besides other likely adverse situations that may impact the Company's operations.

Total strategic risks - (cases in 2012)

Algar Telecom	Algar Tecnologia	Engeset
11	14	13

The Company has an Information Security Team, dedicated to fighting fraud. No corruption cases were found during the 2005-2012 period.

Intangible Assets

Intangible assets are those that cannot be measured in numbers and, therefore, are not shown in the Company's financial statements. These assets are major distinct features that strengthen the businesses and significantly help the Company create value. Among the intangible assets that have been consolidated by Algar Telecom during the period of over five decades of operations, the most relevant are:

Brand power

Algar Telecom, which owns the CTBC brand, is the oldest telephone company in Brazil, acknowledged for its top-quality services and client satisfaction, since its foundation in 1954. It is a Brazilian public limited company controlled by the Algar Group, which operates in the segments of IT/Telecom, Agribusiness, Services and Tourism. In 2012, the strong image enjoyed by the Company in the market was a determining factor for the success of its second public placement of debentures, whose demand exceeded estimates by nearly 65%.

Excellence in technology

The excellence in technology and the offer of innovative services are some of the main competitive edges that reinforce Algar Telecom's position in the market, which consist in crucial factors within a market whose largest portion is controlled by major international players. The excellence in technology results from the Company's innovation culture, as described in a specific chapter in this report.

Human and intellectual capital

Algar Telecom is recognized by its team of highly-skilled professionals, who are committed to the clients. Such acknowledgement stems from the Company's belief in the ability to change and in the engagement of the people who bring the Company to life, expressed in the Vision "PEOPLE SERVING PEOPLE" and supported by its well-structured policy of valuing talents, which is chiefly fostered by UniAlgar, the Group's corporate university. UniAlgar is present throughout each associate's human and intellectual development and manages all knowledge acquired, disseminating it to all Algar companies.

Work environment

A company's sustainability also depends on its Human Talents' satisfaction. The Company constantly seeks to create a healthy working environment, to which all its associates are proud to belong. The effectiveness of its initiatives, as well as the development of new strategies to improve the working environment in all its units, is assessed by a quantitative and a qualitative Organizational Climate Survey conducted every year and every two years respectively. In 2012, 95% of the associates were covered by the survey, including professionals of all Algar Telecom's hierarchic levels. For 93% of the participants, Algar Telecom shows respect in treating its associates, whereas 96% stated that are committed to the goals and targets attributed to their areas. The general satisfaction rate stood at 67%.

PERFORMANCE

Economic Environment

The first half of 2012 was marked by the uncertainties brought about by the world economy as a result of the European crisis. Concerns about a breakup of the bloc affected the world's economic performance throughout the year and remains one of the main risk factors in 2013. The sluggish rebound in the U.S. and the slowdown in China also contributed to the deterioration of the economic agents' estimates.

The Brazilian economy, as well as all other emerging economies, was affected by this situation. The monetary authority and the Government took anti-cyclical measures to check the downturn in industrial activity. Although an upward trend started in the second half of the year, the 2012 growth rate was disappointing. The Brazilian GDP grew by 0.9% in 2012, far below the 3% expansion projected in the previous year. An even greater reason for concern was the perceived drop in investments, essential to promote growth and mitigate the infrastructure bottlenecks. The main stimulus measures taken by the government included a temporary tax break for certain industries and a steady reduction in the basic interest rate, which fell from 11.5% at the close of 2011 to 7.25% at the close of 2012.

Nevertheless, it was not a lost year. The labor market remains one of the pillars of the Brazilian economy and helps maintain household spending. According to IBGE (Instituto Brasileiro de Geografia e Estatística, or Brazilian Institute of Geography and Statistics), the unemployment rate stood at 4.6% at the close of 2012 – the lowest in the historical series–, with an average rate of 5.5% in the year. The average income of the working population rose by 4.1% versus a 2.7% rise in 2011.

The credit granted to the private sector totaled R$ 2.2 billion in 2012, 15% higher than in the previous year, which accounted for 95% of the total balance of credit supplied by the financial system. Loans to the segment of other services rose 3.7%, with special mention to the industries of power, telecom and transportation.
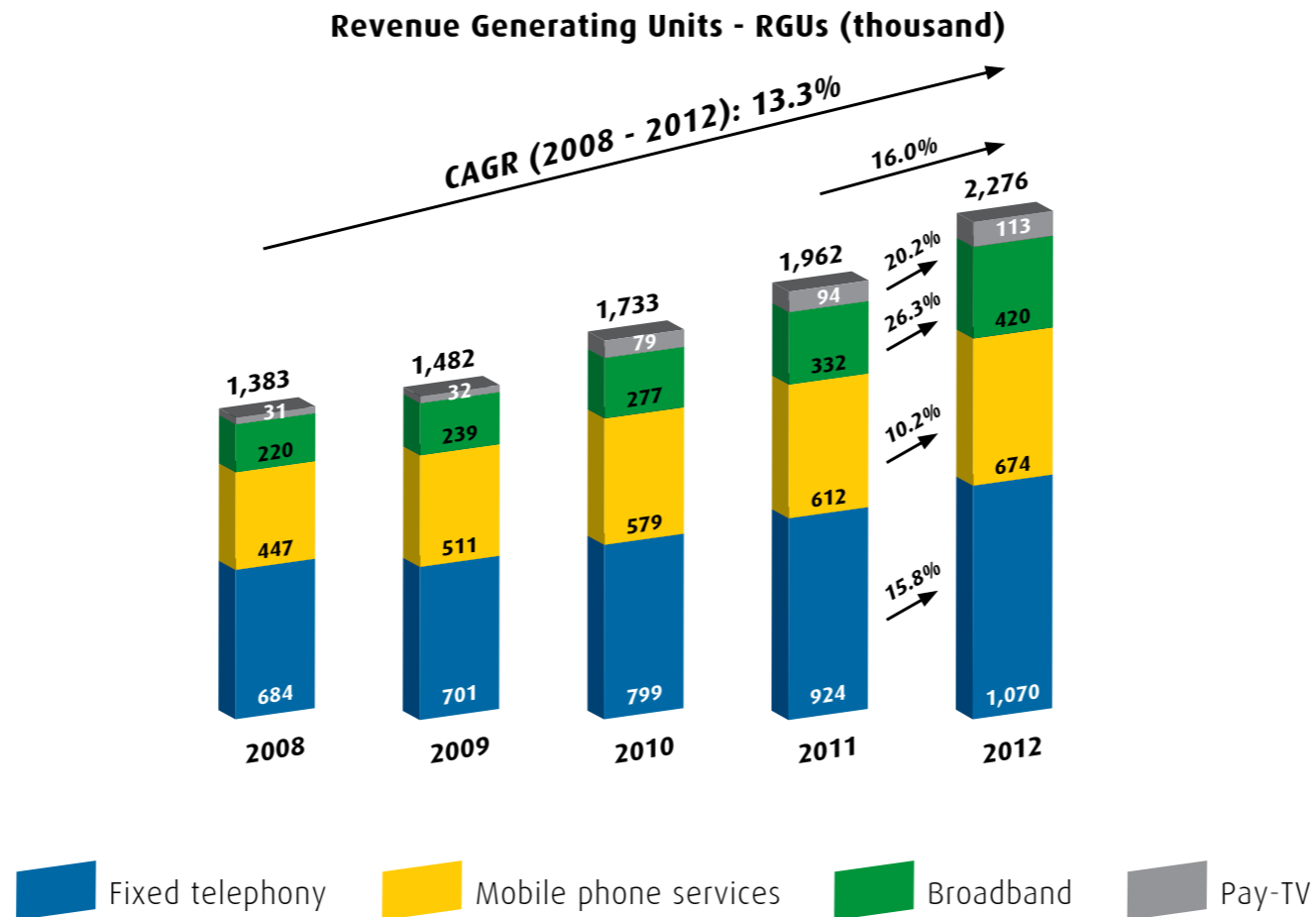
Even within an adverse economic environment, Brazil registered 342 million telecom (fixed and mobile telephony, accesses at the close of 2012, according to data released by the Brazilian Telecommunications Association (Telebrasil), representing a 9.7% growth year-over-year. The highest increase in demand was registered in the pay-TV segment, which reported 16.2 million accesses, up 27% from 2011, followed by broadband services, mobile and fixed telephony, which posted increases of 10%, 8% and 2% respectively.

The segment of mobile phone services, which accounts for 76,5% of the overall number of accesses in the industry, recorded a number of over 261.7 million lines in service at the close of 2012, of which 80.5% consists of pre-paid phone services and 19,5% of post-paid. A total number of 19.5 million mobile lines were enabled in 2012, representing an 8% increase over the previous year. Brazil's teledensity stood at 132.78 lines per 100 inhabitants in 2012, up 7.19% from 2011. As for the 3G lines, with access to mobile broadband, accounted for 22.6% of the base, representing 59.2 million accesses during the year.

Economic and Financial Performance

Telecom

At the close of 2012, Algar Telecom had 2.3 million Revenue Generating Units (RGU) in its Telecom segment, representing a 16.0% increase year-over-year.

Revenue Generating Units - RGUs (thousand)

CAGR (2008 - 2012): 13.3%

16.0%

2008 — 1,383
- 31
- 220
- 447
- 684

2009 — 1,482
- 32
- 239
- 511
- 701

2010 — 1,733
- 79
- 277
- 579
- 799

2011 — 1,962
- 94
- 332
- 612
- 924

2012 — 2,276
- 113
- 420
- 674
- 1,070

20.2%
26.3%
10.2%
15.8%

■ Fixed telephony   ■ Mobile phone services   ■ Broadband   ■ Pay-TV

Fixed telephony

The Company closed 2012 with a number of 1,070,000 fixed lines. The 15.8% growth in relation to the previous year was driven by the performance achieved in both areas of authorization and concession. In concession area, where the Company's business is mainly concentrated in the retail segment, the number of fixed lines climbed from 693,000 to 760,000, reflecting the positive response to offering of packages combining fixed-line phone, broadband and pay-TV services. In the authorization area, where the Company provides services to the corporate segment, the number of fixed lines grew by 33.9%, from 231,000 to 310,000, which reflects the uptrend for the number of clients located in the cities surrounding the Company's backbone.

Broadband

Broadband connections reached 420,000, representing a 26.3% growth year-over-year, which evidences the clients' credibility in the Company's focus on quality. A contributing factor to this performance was the increase in the Ultra Broadband internet access plan, of up to 100 Mbps, through HFC (hybrid fiber-coaxial) cable and GPON networks. In the segment of 3G technology, an important addition to the range of products and services, the number of clients grew from 56,000 in 2011 to 93,000 in 2012, representing a year-over-year growth of 65.0%.

Mobile Phone Services

In this segment, the client base in 2012 climbed by 10.2% year-over-year, to a total of 674,000 clients. The post-paid segment showed a 2.7% increase, from 205,000 clients in 2011 to 211,000 in 2012. The pre-paid segment, in turn, presented a 13.9% growth year-over-year and totaled 463,000 clients. At the end of 2012, 31% of Algar Telecom's mobile phone clients had post-paid plans, with an ARPU (Average Revenue per User) of R$ 32.40.

Pay-TV

The number of clients for this service totaled 113,000 at the close of 2012, representing a 20.2% increase in relation to 2011. In December 2012, the Company provided access to 44 HDTV resolution channels, for both cable and satellite TV plans.

Consolidated gross revenues

At the close of FY 2012, consolidated gross revenues came to R$ 2,338.7 million, up 8.4% from 2011, mainly driven by the broadband services (35.4%), telecom engineering (29.1%), voice and data services for the corporate market in the authorization area (18.2%), and Business Process Outsourcing and IT (13.1%). The revenue profile evolved in line with the Company's strategic plan. At the close of 2012, only 39% of the overall revenues came from voice services, 33% from data and broadband services,19% from Business Process Outsourcing and IT, 4% from pay-TV, and 5% from other services.
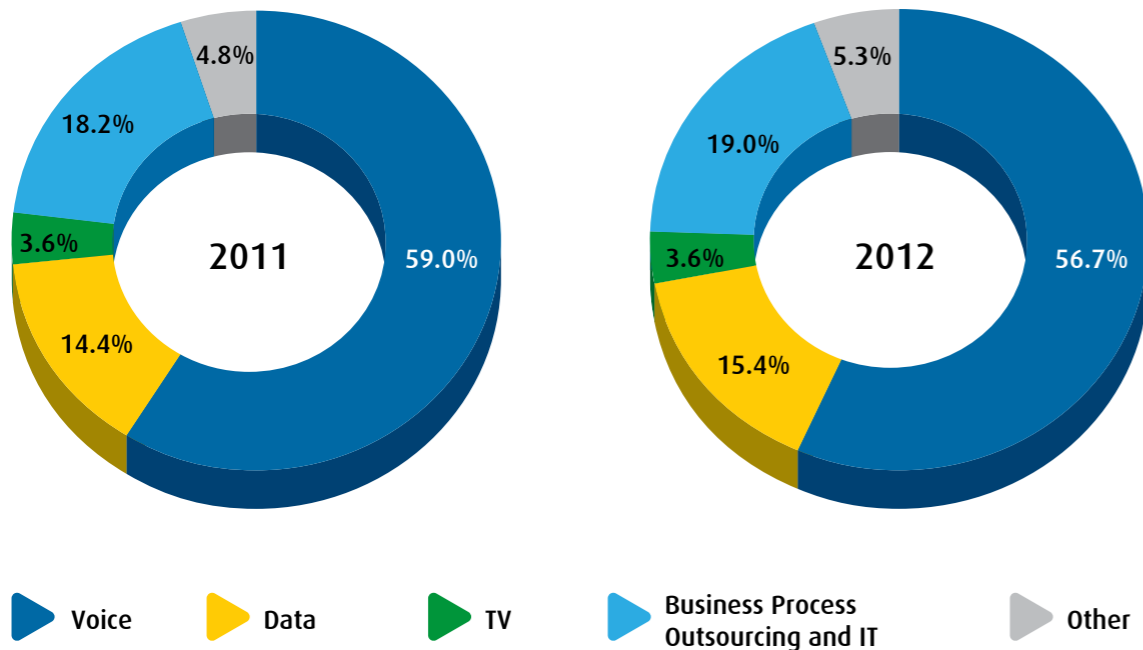
Telecom
Revenues from telecom services, which accounted for 76% of the Company's overall revenues in 2012, amounted to R$ 1,770.4 million, up 6,7% from 2011. This increase mainly resulted from higher revenues from voice and data solutions to the corporate market in the authorization area, broadband services and mobile telephony, which more than offset the drop in revenues from fixed-line local traffic, long-distance calls and fixed telephony cards.

Business Process Outsourcing and IT
Consolidated gross revenues from the segment of Business Process Outsourcing and IT (19% of total revenues) came to R$ 444.2 million in 2012, up 13.1% from 2011, when revenues of R$ 392.7 million were recorded. This rise was due to 9.5% higher revenues from process outsourcing services, and 34.8% higher IT revenues. At the close of 2012, IT services accounted for 21.0% of total revenues from this segment.

Complementary Businesses
At the close of 2012, consolidated gross revenues from Algar Telecom's complementary businesses totaled R$ 124.1 million, versus R$ 104.5 million in 2011, climbing by 18.8%. Of particular reference was the telecommunications engineering business, which reported a 29.1% growth. Revenues from phone directories and guides, in turn, rose by 3.7%.

Net operating revenues

In 2012, Algar Telecom's net operating revenues stood at R$ 1,811.5 million, up 7.7% from 2011, due to the factors previously described.

2011

4.8%
18.2%
3.6%
14.4%
59.0%

2012

5.3%
19.0%
3.6%
15.4%
56.7%

► Voice   ► Data   ► TV   ► Business Process Outsourcing and IT   ► Other

2012 - Annual
Sustainability Report

Operating costs and expenses

R$ million

CONSOLIDATED FINANCIAL SUMMARY	2011	2012	% var.
OPERATING COSTS AND EXPENSES	(1,271.1)	(1,359.0)	6.9%
Personnel	(544.9)	(572.8)	5.1%
Materials	(43.7)	(45.5)	4.0%
Third-party services	(286.9)	(347.2)	21.0%
Interconnection	(210.1)	(176.6)	-15.9%
EILD Connection Means	(39.6)	(44.7)	12.7%
Marketing and Advertising	(29.7)	(29.9)	0.5%
ADA	(16.7)	(25.9)	55.0%
Others*	(99.3)	(116.4)	17.2%

* Including other operating revenues (expenses)

Operating costs and expenses (excluding depreciation and amortization) amounted to R$ 1,359.0 million in 2012. The 6.9% rise year-over-year resulted mainly from:

▸ Personnel costs and expenses (up R$ 27.8 million): (i) personnel costs in the telecom engineering segment climbed by R$ 20.2 million, due to both the expansion of the scope of services regarding existing contracts, coupled with the addition of new clients; (ii) R$ 7.6 million higher personnel expenses, in the three business segments, owing to the wage adjustment as a result of the collective wage agreement, partly offset by the reduction in headcount, due to the termination of some contracts and the termination of some contracts, and the payroll tax reduction (Plano Brasil Maior);

▸ Third-party service costs and expenses (up R$ 60.3 million): (i) R$ 19.9 million higher costs in programming and transmission maintenance of satellite TV; (ii) R$ 18.0 million higher costs in the expansion of Business Process Outsourcing and IT (including software maintenance, training and advisory services); (iii) R$ 11.2 million higher costs in back office and consulting services; and (iv) R$ 5.3 million higher costs in network construction and maintenance, training and others;

▸ Interconnection costs (down R$ 33.5 million): (i) reduction in the VU-M tariff (ANATEL Resolution No. 576); and (ii) reduction in the fixed-line to fixed-line connection tariff, resulting from promotional campaigns to stimulate intra-network and local calls;

▸ EILD costs (up R$ 5.0 million): higher expenses on third-party network fees to serve clients located outside the Company's original area;

▸ "Other" costs and expenses (up R$ 17.1 million): (i) R$ 11.4 million higher costs in infrastructure leasing, easement and real estate in the telecom segment; and (ii) R$ 1.7 million higher costs, due to a contract discontinuation in the Business Process Outsourcing and IT segment, as well as related to the real estate leasing contract in the telecommunications engineering business segment. In addition to the aforementioned increase in costs, the "other operating revenues" declined by R$ 2.1 million.

EBITDA

R$ million

EBITDA and EBITDA Margin	2011	2012	% var.
Telecom	**361.8**	**376.3**	**4.0%**
margin	29%	29%	-
Business Process Outsourcing and IT	**36.1**	**58.9**	**63.4%**
margin	9%	13%	-
Complementary businesses	**13.1**	**16.2**	**23.4%**
margin	8%	8%	-
CONSOLIDATED EBITDA	**411.1**	**452.3**	**10.0%**
margin	24%	25%	-

The EBITDA of the Telecom segment amounted to R$ 376.3 million in 2012, up 4.0% from 2011. The EBITDA margin, in turn, remained virtually flat, at 29%.

The Business Process Outsourcing and IT segment reported EBITDA of R$ 58.9 million in 2012, up 63.4% from 2011, with an EBITDA margin of 13%, versus 9% in 2011. This increase primarily derives from the improved operational performance, stemming from efficiency and quality projects, in addition to the "Plano Brasil Maior", which incurred a payroll tax reduction for the contact center services.

Complementary businesses recorded a R$ 16.2 million EBITDA in 2012, up 23.4% from 2011, with an EBITDA margin of 8%, flat in relation to the previous year.

As a result of the above-mentioned events, Algar Telecom's consolidated EBITDA came to R$ 452.3 million in 2012, up 10.0% from 2011. The consolidated margin was 25%, representing a 0,6 p.p. increase over 2011.

Net financial result

Algar Telecom's net financial expenses amounted to R$ 82.4 million in 2012, down 5.8% from 2011, mainly due to the drop in CDI's average rates.

Net income

The Company recorded consolidated net income of R$ 141.0 million in FY 2012, versus R$ 144.4 million in 2011. Net margin stood at 7.8%, versus 8.6% in the previous year. nevertheless, it is worth pointing out that in 2011, the Company's net income had a positive impact from a non-recurring effect in the amount of R$ 17.1 million, related to deferred tax credits. If this extraordinary effect over the 2011 earnings is disregarded, the net income in 2011 results in R$ 127.3 million, and consequently the 2012 net income would show a 10.8% increase year-over-year, with a 0.2 p.p. rise in net margin.
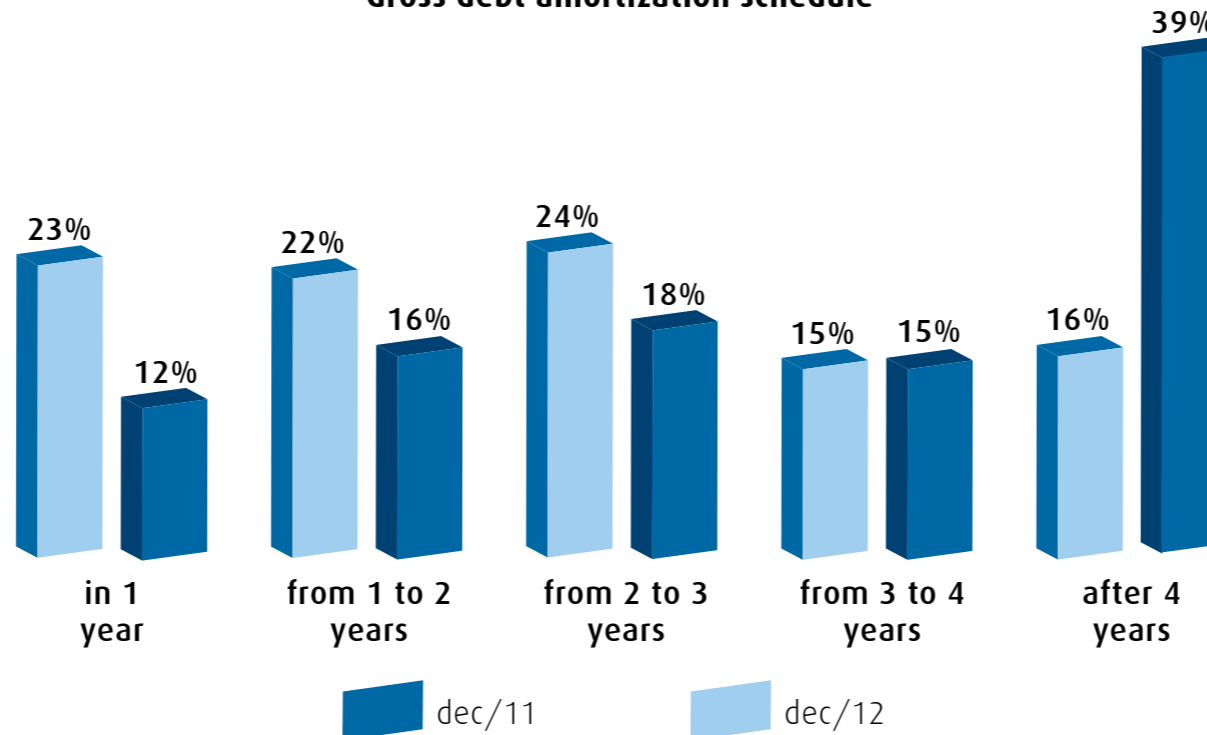
Debt

At the close of 2012, Algar Telecom's gross debt stood at R$ 925.5 million (R$ 814.8 million in 2011). Net debt, in turn, totaled R$ 738.7 million, versus R$ 636.5 million in the previous year. The R$ 102.2 million increase in net debt results from the additional fund-raising required to cover part of the investments carried out during the period, in he amount of R$ 350.8 million.

In 2012, the Company completed its second successful public placement of non-convertible debentures. This issue, effected in November 2012, resulted in proceeds that totaled R$ 293.9 million, divided in two series. The first one enjoys a 5-year maturity, with a CDI + 1.40% p.a. remuneration, and the second trench features a 7-year maturity, remunerated at   IPCA + 6.00% p.a. The funds raised were partly used for the redemption of the debentures from the first issue, as well as to reinforce the amount of liquid assets. Hence, there was a significant improvement in Algar Telecom's debt profile, with more extended maturities over the next years.

Furthermore, the Company managed to maintain a suitable financial leverage, measured by the Net Debt/EBITDA ratio, which stood at 1.6x in 2012, versus 1.5x in 2011.

**Gross debt amortization schedule**

	in 1 year	from 1 to 2 years	from 2 to 3 years	from 3 to 4 years	after 4 years
dec/11	23%	22%	24%	15%	16%
dec/12	12%	16%	18%	15%	39%

■ dec/11   ■ dec/12

Investments - CAPEX

In 2012, investments totaled R$ 350.8 million. The funds were allocated to reinforce the Company's structure intended to support the growth of its operations, as well as to reinforce the Company's competitive position over the ensuing years. From the total volume of investments, 48% was allocated to the network expansion, with a consequent growth in data, voice and TV services. 8% was allocated to the growth in the Business Process Outsourcing and IT, and 44% was directed to support the maintenance services and the quality of operations.

Total investments in 2012: R$ 350.8 million

155
44%

168
48%

28
8%
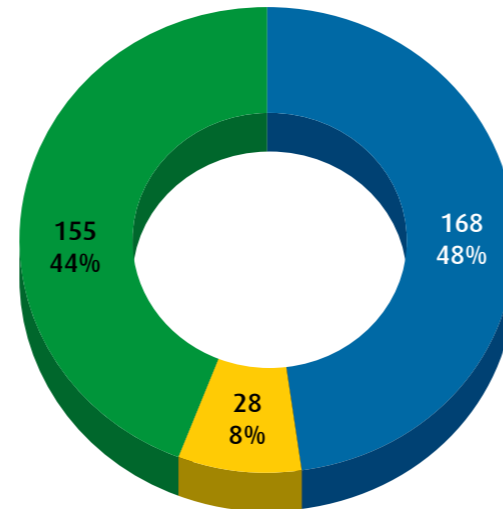
■ Network expansion ■ Expansion of the Business Process Outsourcing and IT ■ Operations maintenance

DVA

The Value Added Statement shows the breakdown of the total direct economic value generated and distributed by the Company, which includes revenues, operating costs, remuneration to employees, donations and other investments in the communities, retained earnings and disbursements related to funding sources and the government. In 2010, 2011 and 2012, the Company generated R$ 1,224 million, R$ 1,402 million and R$ 1,437 million respectively. The largest portion of those amounts was distributed to associates and the government. The amount distributed to shareholders remained virtually stable over the last three years.
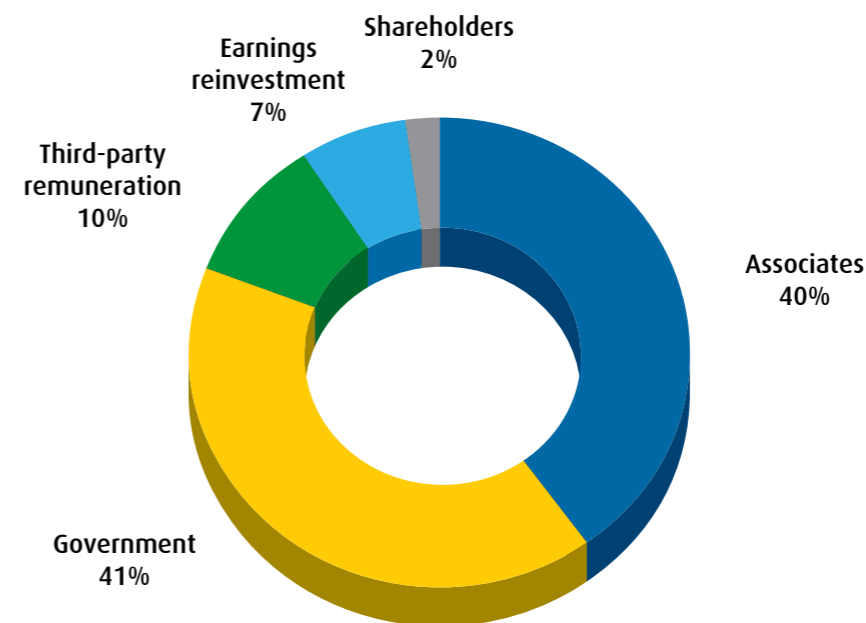
VALUE ADDED STATEMENT

R$ million

	2010	2011	2012
Revenues	**1,960**	**2,183**	**2,336**
Revenues from sales	1,960	2,183	2,336
Inputs acquired from third-parties	**(621)**	**(667)**	**(763)**
Cost of goods sold and services rendered	(418)	(403)	(489)
Materials, power, outsourced services and others	(204)	(264)	(274)
Provision for losses / asset devaluation	-	-	-
Gross value added (1-2)	**1,339**	**1,515**	**1,573**
Depreciation and amortization	(150)	(145)	(162)
Net value added (3-4)	**1,189**	**1,371**	**1,412**
Financial Income	35	31	25
Total value added to be distributed (5+6)	**1,224**	**1,402**	**1,437**
Value added breakdown	**1,224**	**1,402**	**1,437**
Personnel	**394**	**484**	**573**
Taxes and contributions	**548**	**594**	**584**
Third-party capital remuneration	**151**	**179**	**139**
Interests	103	119	73
Leases	49	60	66
Dividends and Interest on equity	**31**	**35**	**34**
Retained earnings for the period	**100**	**109**	**107**

The retained amount, which represented 7% of the total distribution in 2012, shall be allocated to new investments and to the maintenance of operations in 2013, aimed at providing quality products and services to the clients.

Distribution of value added in 2012: R$ 1.4 billion

- Shareholders 2%
- Earnings reinvestment 7%
- Third-party remuneration 10%
- Associates 40%
- Government 41%

GRI: EC1

Acknowledgements and awards

The services rendered by Algar Telecom and its subsidiaries were acknowledged during the period, with yielded important awards and certifications, thus corroborating the Company's distinguished position in the Brazilian telecom industry.

Algar Telecom

The 20 Most Innovative Companies in Brazil – Revista Época
Outstanding position among the most innovative companies in the country. Algar Telecom won the 10th place (the first place among the telecom companies), in the Best Innovator category.

Brazil's 100 Most Innovative IT Companies - IT Mídia and InformationWeek Brasil
1st place in the Technology, Media and Telecom category, due to the Sales Portal case.

XII Prêmio ABT – Associação Brasileira de Telesserviços
Gold trophy in the Innovation category, for the case "URA of Unlocking", as well as a silver trophy in the Internet and Social Media category, with the "SAC 2.0 CTBC" case.

Prêmio Tele.Síntese de Inovação
The Company won the 2nd place, with the case "3G Reporter"

Aberje 2012 award – Associação Brasileira de Comunicação Empresarial
1st place in the country, in the "Communication with the Consumer", with the "CTBC Responde" case, and regional 1st place in the "Communication with the Society" category, with the "Iniciativa Verde" case.

Melhores Empresas para se Trabalhar no Brasil - Revista Época
Great Place to Work Institute jointly with Época Magazine – Ranked 37th among the 100 best companies.

Melhores Empresas para Trabalhar em TI e Telecom 2011 (Best IT and Telecom Companies to Work – 2012)
Ranked 25th among the 100 Best IT and Telecom Companies to Work, by the Great Place to Work Institute.

Prêmio Consumidor Moderno de Excelência em Serviços ao Cliente 2012
1st place in the Regional Fixed Telephony category and 1st place in the Regional Mobile Telephony category.

Ranking da Sustentabilidade 2012 – Revista Imprensa
Brazilian highlight in the category "The most sustainable companies according to the media".

GRI: 2.10

Algar Tecnologia

As mais Admiradas do Brasil – Revista Carta Capital
Highlight among the most admired companies in the country, ranking 4th in the contact center category.

Melhores e Maiores do Brasil 2012 – Revista Exame
Highlight among the Brazil's 1,000 largest companies. The company climbed 31 positions (to 873rd) in relation to the previous year.

Prêmio Consumidor Moderno 2012
Was elected the contact center of the year in the 13th edition of Prêmio de Excelência em Serviços ao Cliente (Client Service Excellence Award), given by the Consumidor Moderno (Modern Consumer) Magazine.

TOP 10 Full Outsourcing – Anuário da Série Estudos
10th position in the Full Outsourcing ranking, with the best improvement among all players, in the main ranking of the industry.

Top 200 2012 – Anuário de Informática Hoje
Was ranked 43rd among the top IT companies, climbing 55 positions in relation to the previous year.

Ranking IDC - International Data Corporation
A 2011 study ranked Algar Tecnologia among the top-growing IT companies.

Prêmio INSADI Excelência em Processos
The DTH Lean case, the first major project in which Algar Tecnologia used the Lean Seis Sigma methodology, won first prize in the Process Excellence category.

Prêmio Nacional de Telesserviços 2012 (2012 Brazilian National Tele-Services Award)
The TOP Performance case won first prize in the Best Job Training Initiative category of the award, given by Associação Brasileira de Telesserviços (Brazilian National Tele-services Association), which undertakes initiatives so that its members are motivated and united around a common purpose, and can, therefore, help their clients achieve their goals more assertively.

SAP Hosting Partner
Received the international certification SAP Hosting Partner, recommended by SAP Global, which recognizes superior performance, scalability and availability of the IT environment.

Selo SCC - Support Center Certification
Two service desk operations of the company received the certification, given by HDI Help Desk Institute.

Selo Amigos da Cultura (Friends of Culture Seal)
Uberlândia Municipal Government

Prêmio Empresário Amigo do Esporte (Entrepreneur Friend of Sports Award)
A tribute from the Ministry of Sports for the entrepreneurs who mostly contributed to sports projects through the Sports Incentive Law.

Engeset

Top 200 2012 – Informática Hoje (IT Today) Yearbook
Engeset was ranked 13th among Brazil's 50 largest system integration companies.

Melhores Empresas para Trabalhar em TI e Telecom 2012 (Best IT and Telecom Companies to Work – 2012) – ComputerWorld
Was ranked 97th among the 100 Best IT and Telecom Companies to Work in Brazil by the Great Places to Work Institute.

2012 Telecom Yearbook
Ranked 56th among the 100 largest IT companies.

ISO 9001 – Bureau Veritas Certification
Earned ISO 9001 (Quality Management) recertification in October 2012.

ISO 14001 – Bureau Veritas Certification
Earned ISO 14001 (Environmental Management) recertification in October 2012.

People

BUSINESS SEGMENTS

Telecom

The service portfolio of this segment comprises retail and corporate, telephony services (fixed and mobile), broadband internet, data transmission, internet provider and pay-TV. In this segment, the Company hires outsourced services only for help desk assistance, antivirus and data storage. In the case of voice service to corporations, Algar Telecom may occasionally acquire third-party networks.

Products and Services

Fixed-Line Phone Services
Local calls, domestic and international long-distance phone calls (with Carrier Selection Code 12), public and VoIP (Voice over Internet Protocol) phone services.

Mobile Phone Services
Pre-paid, post-paid and third generation (3G) plans, with video call and internet access services.

Broadband
(Type I and Type II) ADSL, HFC and GPON (Gigabit Passive Optical Network) access, with maximum speed of 1 Gb per second, and 3G mobile broadband services, with capacity to transmit data at up to 100 Mbps through HFC (hybrid fiber optic and coaxial cables), and GPON networks.

Data Communication
High-speed data communication services intended to the corporate market, which are provided through a modern IP network.

Pay-TV
This service provides access to over 170 channels, including 44 in HDTV resolution, which began to be marketed in late 2012. The plans offered can be either via satellite, covering 115 municipalities at the close of 2012, or via cable, comprising a network of 930 km in length, in the cities of Araguari and Uberlândia, Minas Gerais State.

Operating areas

In the concession area, where it has been operating since 1954, Algar Telecom caters for both the residential and corporate markets of 87 municipalities in the states of Minas Gerais, São Paulo, Goiás and Mato Grosso do Sul – a region that consists of 2.9 million inhabitants and per-capita consumption 16.5% above the country's average statistics. Its service portfolio comprises fixed and mobile telephony services, broadband internet access, data communication, internet provider, pay-TV (DTH and cable), in addition to code 12 operator for long-distance and international calls.

Since 2003, Algar Telecom has also held an authorization by ANATEL to provide fixed and voice telephony throughout Brazil. In this segment, the mainly target market is the corporate one. At present, the Company is present in 70 municipalities in the states of São Paulo, Rio de Janeiro, Minas Gerais, Goiás, Paraná and the Federal District, providing solutions of fixed telephony and data communication.

The Company's third niche of operations is called "Expansão Minas" (Minas Expansion), whose focus consists in the residential market of the Band H, a frequency range for 3G telecom services that the company acquired at an auction two years ago. Since the end of 2011, Algar Telecom markets packages that combine services of broadband internet, pay-TV, mobile 3G telephony and fixed-line phone services to nineteen cities (from a total number of 233 allowed).

Infrastructure

Algar Telecom's backbone comprises a long-distance circular optic fiber network, of 12,000 km in length, which extends across the main cities of the states of Goiás, Minas Gerais, Rio de Janeiro, São Paulo and Paraná, in addition to Brasília, in the Federal District. The Southeast Region, in which most of the network is, accounts for 55% of the country's GDP. Since 2010, the Company has had an international Point of Presence (POP) at the NAP of the Americas, appointed to connect Brazil to the rest of the world.

Algar Telecom complies with the local, state and federal legislation governing the construction and implementation of antennas by consulting with ANATEL, COMAR (the Regional Air Command), as well as with other competent bodies. On the grounds of sustainability, the Company prioritizes the adaptation of the structures it already has, in addition to sharing antennas with other companies. The Company's inventory comprises all its physical structures, such as antennas, towers and buildings, taking into account which are shared with other carriers and/or installations (leases). At the close of 2012, 34% of the total number of 1,629 physical structures were shared.

Business Process Outsourcing and IT

Algar Tecnologia

In the corporate market since 1998, Algar Tecnologia provides technology solutions for business processes. At the close of 2012, the company held a headcount of over 10,000 associates, alongside a diversified client portfolio consisting of nearly 190 clients from distinct industries, such as health care, financial, education, manufacturing, utility, media and entertainment industries, as well as the government. Algar Telecom, its partner and also its main client, accounted for 9% of the overall client base.

The service portfolio of Algar Tecnologia can be breakdown into four areas of expertise:

Information technology (IT) infrastructure
Services intended to yield gains in productivity, coupled with the maximization of the cost-effective IT solutions considering clients' business performance. To that end, the company holds three data centers strategically located: two in Uberlândia (Minas Gerais State) and one in Campinas (São Paulo State), which are interconnected by a fiber optic network and covers the whole country and abroad. In 2012, in preparation to meet the ever-increasing demand, the facilities that encompass the Campinas data center was expanded by over 1,000 square meters, equivalent to a 30% rise in the total area.

Services Management
The Company provides support and management of IT & Telecom services. Experienced professionals specializing in the main technologies and market practices concentrate their efforts to provide more security to the clients' operations and to certify that the IT functions be available for all users in the organization.

Business application
Considering the expertise and a professional team that is avowed by the major market players, Algar Tecnologia offers business applications with comprehensive solutions. Either through the company's own software plants or the strategic partnerships with major software manufacturers on the market, the service encompasses the development and upholding of the solutions that are suitable to each client's business profile. The company's methodology is based on cutting-edge software engineering, project management and most accepted maturity models.

Relationship with clients
Algar Tecnologia employs quality solutions aimed at ensuring the companies to take care of one of their main assets: their clients. Its team makes use of advanced support technologies and the best market practices to enhance its relationship with the clients, by means of contact centers and the internet. The company currently has nearly 7,500 work posts to perform customer care services, credit risk management, telemarketing sales, business back office and client experience management.

COMPLEMENTARY BUSINESSES

Engeset – Telecommunication Engineering

Engeset has expertise in comprehensive IT and telecom infrastructure solutions, which comprise consulting services, project development, as well as network installation and maintenance. Since the company was founded in 1991, it has already installed over 20,000 km of fiber optic grids and is currently in charge of the maintenance services of 23,000 km in length.

Although Engeset plays a strategic role as concerns Algar Telecom's development, it has an ongoing expanding addressable market. Currently, its diversified client base is served by highly skilled professionals, based in 23 business units spread across the country, including the cities of São Paulo, Rio de Janeiro, Belo Horizonte, Salvador, Campinas, Recife, Fortaleza, Brasília, Macaé, Goiânia, Curitiba, Porto Alegre, Uberlândia, Uberaba and Franca.

Algar Mídia

In the market for over four decades, Algar Mídia is a transmedia company that offers solutions for interaction between its clients, chiefly small and medium-sized companies, and the public in general by means of different information platforms, which can be breakdown into three segments:

Updating media
This group includes Correio de Uberlândia, a newspaper founded in 1938, with an average distribution of 12,000 copies and a measured readership of about 50,000 people/day, in addition to the derivative products: an online version with an average of 30,000 single visits a day, plus the magazines accompanying the copies throughout the whole year.

Consultation media
The company's core business, this segment comprises the phone directory Sabe, with an annual distribution of 1,250 million copies, the guides Sei, Viver and Netsabe (an online search engine with the contents of the directory and guides). This products are delivered to nearly 250 municipalities located in the states of Minas Gerais, São Paulo and Goiás.

Exposure media
This is the company's most recent business. It started up in 2011 to meet the further demand for digital solutions, and shows a significant growth potential in upcoming years. Available in the same cities as the consultation media segment, digital Out-of-Home consists of offline tools (voice) and online tools (information screens) installed in busy areas, such as supermarkets, bus terminals, gyms, clinics and hospitals. At the close of 2012, Rede Alooh held 640 digital screens and, including offline services, reached approximately 4.5 million people/day.

A few stages of the operations carried out by Algar Mídia are outsourced, such as the printing (phone directories and guides), as well as the delivery of products (Correio de Uberlândia newspaper, printed directories and guides), in addition to software and platforms of digital Out-of-Home medium and internet.

GRI: 2.2; 2.7

Society and the environment

Algar Telecom believes that inspiring people to adopt sustainable practices can change the future of our planet. The same conviction is shared by all companies of the Algar Group, which is a signatory to the Global Compact, an initiative developed by the United Nations Organization (UNO) to encourage the corporate community to adopt values in connection with human rights, labor relations, the environment and the fight against corruption.

The initiatives taken by Algar Telecom to motivate its associates bring together a set of practices that concern all the Company's stakeholders, which are embedded within the scope of economic, environmental and social aspects.

To ensure its economic sustainability, the Company follows an efficient management model and a solid corporate governance policy, which makes it possible for the Company to make wise decisions at the present time, whose unfolding shall determine the future of the Organization.

The environmental cornerstone of sustainability requires a conscious and responsible management approach, through the conduction of practices directly aimed at engaging the entire business networking in a commitment to preserving the ecosystem. Furthermore, in 2012, Algar Telecom succeeded in retaining the ISO 14001 certification, issued by Bureau Veritas Certification, having been acknowledged for its efficient Environmental Management System.

Lastly, Algar Telecom's initiatives concerning social sustainability focus on the development of the communities where the Company performs its activities, by means of undertaking educational projects, funded by Instituto Algar de Responsabilidade Social, coupled with the incentive to culture in some of the locations where it operates, including performances that were attended by more than 40,000 people.

Environmental Sustainability

Algar Telecom environmental policy goes beyond the efforts to mitigate environmental impacts in its activities. The greater purpose, fully aligned to the Company's values and beliefs, is to create an incentive chain to environmentally-sustainable practices, providing associates, clients, suppliers and communities with conditions and motivation to contribute to the future of the planet. Internally, the movement to involve all the stakeholders in this pillar is called Green Influence.

The Company's Environmental Program, "Telecom Verde", joins actions, campaigns and differentiated projects that – when incorporated to the daily operations – can reduce the use of environmental resources and the production of waste. The permanent search for new ideas in this field is motivated by different actions involving associates. Since 2011, environmental engagement is a bonus-related performance that composes professionals' variable compensation. Is the last year, 100% of the associates met their goals.

Still with the goal of disseminating the environmental culture and the developing new ideas, the Company has the Telefone Verde Hotline: 4005- 9912), a voice portal created to allow clients, suppliers, communities and associates to record suggestions of good practices, environmental projects, send reports or doubts related to environmental sustainability. The call can come from anywhere in Brazil at the cost of a local call and the Company commits to return the contact in less than 48 hours in working days.

Algar Telecom Environmental Program practices contribute to the ecosystem and strengthen the Company's culture as all earnings from environmental projects ("Green Money") are 100% invested in talents training and development, as per the CEO's strategic guidelines.

In 2012, Algar Telecom destined R$ 356.0 thousand to environmental actions. The value was divided among planet conservation, awareness building and energy efficiency projects.

Total Investments and Expenses with Environmental Protection, per type.

Type of Expense	Investment	%
Residue Disposal	8,000	2.25
Treatment of Emissions	30,000	8.43
Cost of Remediation	28,000	7.87
Cost of Prevention	40,000	11.23
Environmental Management	250,000	70.22
Total	356,000	100

The objective of the Environmental Program is also to comply with the applicable legislation and help companies to achieve the environmental certifications relevant to their business areas. From 2009 to 2012, Algar Telecom was not penalized or suffered any non-monetary sanctions for non-compliance with environmental laws or legislations.

The main Algar Telecom Environmental Program practices are presented bellow and generated savings of more than R$ 874 thousand in 2012. The greatest achievements, however, cannot be measured in figures, but are rather translated into the Company's reputation in the market, which is essential for its perennial standing.

GRI: EN28, EN30

Natureza em conta [Nature into Account]

The unnecessary and exaggerated consumption of paper fuels deforestation. To avoid the waste in paper printing, Algar Telecom encourages the replacement of the printed bill for the online statement available through the web services channel, where the bill breakdown can be found, a second copy can be printed and payment slips downloaded. Adhesion to the electronic bill is rewarded with 50-minute free conversation bonus. In 2012, the number of clients who chose to receive their bills electronically reached 113,700.

Eco ponto [Eco Point]

It is a selective waste collection point installed at the Algar Telecom Administrative Center to receive solid waste brought by associates and community members, including cooking oil. The Company organizes several actions to raise awareness and monitors the selective garbage collection stations on a daily basis, awarding coordinators for the correct separation of residues every month (Organic, Recyclable, Non-Recyclable). During the year, 26.2 tonnes was collected and sent to the Brazilian Association of Recycling and Selective Collection.

World Car-Free Day

In the "World Car-Free Day", September 22nd 2012, the Company and other subsidiaries of the Algar Group got several associates together in a Bike Ride to raise awareness on the impact of the Greenhouse Gases effect and the importance of the Company's programs to reduce or avoid emissions, such as the Car Pooling.

Car Pooling

A permanent program aimed at decreasing the impact of associates' mobility, the second highest source of emissions of GGEs at Algar Telecom. There are twelve carpool groups (each in a different area) composed of associates who commute to work together every day. There is a specific, duly marked area in the Administrative Center parking lot for associates participating in this initiative. Associate commuting is the Company's second largest source of GGEs

Recicle na Linha [Recycle on Line]

With the goal of giving a social-environmental destination to the bubbles that cannot be reused in Public Telephony, Algar Telecom, together with other community partners, use them to manufacture garbage collectors and boxes to store batteries. In 2012, they were also used as furniture at the trade fair Futurecom.

Energy Efficiency Week and Environment Week

The Energy Efficiency Week and the Environment Week are organized by Algar Telecom Environmental Management System and are aimed at changing the culture, encouraging conscious consumption and sustainable environmental practices. The event was held from May 28th to June 1st at the Administrative Center and offered different talks, product displays and booths with the theme of energy efficiency and environment.

Iniciativa Verde [Green Initiative] Cultural Contest

In its second edition, the educational contest on environmental sustainable practices received applications for two categories. One of them, open to the general audience through the Facebook, gathered 127 participants. The other category, with 48 applicants, was directed to journalists who wrote articles published by the print media or electronically between January 1st and November 23rd. In both cases, the winners received trips to Zurich, Switzerland.

Tree Planting

The action aims at zeroing Greenhouse Gases emissions. In 2012, the goal was reached by the regional office in Franca (SP) where 2,000 trees were planted. In consolidated figures, Algar Telecom closed the year with 4,000 trees planted by its associates (over 4,236 in 2011) in four Brazilian states: Minas Gerais, São Paulo, Paraná and Goiás. The importance of this action is reinforced in the New Talent Integration Program (PINT), as everyone who enters the Company plants a tree and is committed to its growth.

SUSTAINABILITY INDICATORS

Energy Efficiency

The Company undertakes solid actions and energy efficiency projects, as well as power consumption reduction campaigns, through the Internal Energy Conservation Commission (CICE). One of the cornerstones of such efforts is the management of new technologies, aimed at preserving an environmentally-friendly telecommunication network.

At the close of 2012, 22.34% of the Company's network was grounded on the Next Generation Network (NGN) technology, which allowed for the deactivation of sites and central stations. The vacation of physical spaces results in declining demand for refrigeration, hence the power consumption. Moreover, the new central stations have no generators, which brought about a further saving on diesel consumption, thus avoiding CO_2 emissions.

The combination of such initiatives yielded a 4% reduction in power consumption, equivalent to 2.2 million kWh, exceeding the established target of 2.1 million kWh.

Indirect Energy Consumption by Source

In 2012, Algar Telecom consumed 280,136 gigajoules (Gj) of hydroelectric power (renewable). In 2011, consumption came to 220,028 Gj. The higher volume is explained by the expansion of Algar Telecom's activities.

Nevertheless, a careful examination of these figures evidences that the set of energy efficiency initiatives had a positive impact on the total reduction of energy consumption in 2012. Among the most relevant measures, of special reference are: the "Higher Temperature" project, which entails the setting out of a standardized temperature at 25°C for the air conditioning system installed at the work facilities; replacement of chillers and air-conditioners for new equipment that enjoys more advanced technology; in addition to the installation of lead lag equipment that features an automatic controller for air conditioners. Other initiatives include the modernization of the air conditioning system at the Ibiraci facilities (Minas Gerais State), the deactivation of both CDMA Central Stations and under-utilized switching equipment; as well as the replacement of analogue for digital cable TV equipment.

The table below sets out the positive impact form the projects of improvement regarding power reduction and efficiency. In 2012, Algar Telecom achieved a 8,068 Gj reduction, versus 4,555 Gj in 2011.

Total power saved

2011 Initiatives	
Temperature Increase Project	708
Compact Range Unit Replacement	994
Chiller Replacement	1,361
Lead Lag Project	932
Auto power-off Project	21
CDMA Project	288
Meeting Room Power Switches	6
Franca Store Upgrade	74
Air Conditioning at the Ibiraci Site	25
Eco-Switching Project	35
Verde Unix Project	111
Total savings*	**4,555**

2012 Initiatives	
Temperature Increase Project	1,117
Compact Range Unit Replacement	1,359
Chiller Replacement	1,981
Lead Lag Project	2,458
CDMA Project	308
Replacement of Switches	7
Franca Store Upgrade	12
Air Conditioning at the Ibiraci Site	8
Eco-Switching Project	75
Verde Unix Project	90
Araguari Headed	53
Source Replacement - 236	533
Air-conditioning system replacement	66
Total savings*	**8,068**

*electric power in Gigajoules

GRI: EN4, EN5, EN7

Water consumption

Water consumption totaled 128,888 m3 in 2012. The year-over-year increase can be explained by the addition of new data measured by Algar Tecnologia in 2012, which were not covered by the 2011 mapping. The total sum considers ground water and supplies from water utilities. Water sources that are significantly affected by withdrawal of water - seven ground and nine surface sources - are not regarded as protected areas. Algar Telecom has no data for the size of the basins used.

	2010	2011	2012
Surface water, including water from wetlands, rivers, lakes, and oceans	-	-	-
Ground water	8,648	16,982	14,586
Rainwater	-	-	-
Waste water from another plant	-	-	-
Municipal water supplies or other water utilities	15,663	29,160	114,302
TOTAL	24,311	46,142	128,888

GRI: EN8, EN9

Use of land

The Company is not present in permanently protected areas or conservation units. However, it develops biodiversity protection programs, which include the recovery of damaged land and the planting of saplings of Cerrado area native species. Additionally, Algar Telecom conducts environmental education programs for associates, suppliers and partners. In 2012, 14 hectares of damaged land was recovered through the planting of approximately 3,500 native species saplings, exceeding the target of 3,000 saplings for the period.

The planting of trees contributes to the challenging goals related to the reduction and offsetting for the greenhouse gas emissions (GGE) of that have been set out by the Company for the ensuing years. Moreover, this initiative is aligned with the Company's Integration Program. The Company's new talents and existing associates are encouraged to plant a tree, who also by commit themselves to monitor the plant's growth.

GRI: EN11

Greenhouse Gas Emissions (GGE)

Algar Telecom's commitment to the reduction of greenhouse gas emissions can be evidenced by the number of initiatives previously mentioned, such as the tree planting and the incentive to join the Car Pooling Club. In 2012, Algar Telecom increased its CO_2 emissions by 48.7% year-over-year, primarily due to the inauguration of a new regional office in Divinópolis. If this event is not considered, the consistent efforts exerted by the Company and its associates contributed a 7.0% reduction in CO_2 emissions. The following sources were considered: cooling sodas, stationary combustion and combustion from the Company's own car fleet (scope 1), electric power (scope 2) and air travel (scope 3).

Total Direct and Indirect Greenhouse Gas Emissions by Weight

Direct Emissions

Substance	2010	2011	2012
Generation of Electricity, Heat or Steam	2,339	1,309	3,660
Other Combustion Processes	-	-	-
Physical or Chemical Processing	-	-	-
Transportation of Materials, Products and Waste	-	-	-
Venting	-	-	-
Fugitive Emissions	-	-	-
TOTAL	2,339	1,309	3,660

Indirect Emissions

Substance	2010	2011	2012
Land Transportation	476	675	963
Solid Waste	2	7	6
Air Transportation	338	233	500
Office and Advertising Paper Consumption	22	22	23
Electricity Consumption	-	-	-
Stationary–Shared Combustion	-	-	-
TOTAL	838	937	1,492

Other relevant indirect greenhouse gas emissions

Substance	2010	2011	2012
Stationary Combustion (tonnes of CO_2e)	148	140	180
Land Transportation – Own Fleet (tonnes of CO_2e)	562	473	481
Cooling Gas Use (tonnes of CO_2e)	21	21	N/A
TOTAL	731	635	661

GRI: EN3, EN4, EN16, EN17, EN18, EN19

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Waste Management

The incorrect disposal of hazardous materials, such as batteries, mobile phones and battery chargers, causes damage to the environment. These products contain highly toxic heavy metals, which when incorrectly disposed may leak and contaminate the soil, until it reaches the groundwater and food plantations. With a view to mitigating such impact, the Company holds collection points for batteries, mobile phones, battery chargers and phone cards, located in all of its stores and offices. In 2012, Algar Telecom disposed of 450 kg of hazardous materials, in addition to 1,000 light bulbs. After sorting them out and returning recyclable materials to producers, the recycling project disposes of potentially hazardous components appropriately.

The table below shows Algar Telecom's total waste management in 2012. The reason for the significant rise year-over-year was due to the fact that Algar Tecnologia started to monitor such data. The Company recorded no significant spills over the last three years. The target for 2013 is to maintain the lack of spills.

Total weight of waste by type and disposal procedure

	Type	Weight	Disposal Method
2010	Composting	3,955	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage). A service provider transports and disposes of it in a landfill.
	Recycling	9,864	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage) and sent to a recycling company later.
	Total	13,819	
2011	Composting	148,885	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage). A service provider transports and disposes of it in a landfill.
	Recycling	106,905	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage) and sent to a recycling company later.
	Total	255,790	
2012	Recycling Residues	30,931	The Company provides collection points located in its own stores, shopping malls, schools, municipal hospital and Cultura HD radio station, intended to collect the technologic residues, which are sent to recycling companies later.
	Non Recycling	206,409	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage). A service provider transports and disposes of it in a landfill.
	Composting	6,465	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage). A service provider transports and disposes of it in a landfill.
	Lamp Bulbs	8,891	Waste is stored temporarily at an Ecoponto (a place at the Company for waste storage) and sent to a recycling company later.
	Total	252,696	

GRI: EN22

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Algar

Hazardous Waste Disposal

The initiatives to mitigate the impact from products and services include actions such as the Algar Telecom's "Natureza em Conta" program, previously mentioned, which aims at reducing the use of tonnes of paper, by encouraging the clients to opt for the use of electronic bills.

At Algar Mídia, only paper produced by manufacturers that use wood of sustainably managed forests is used for the printing of newspapers, phone directories and guides. The purchases are carried out in bulk, aimed at mitigating the impact from transportation. Furthermore, the raw material is stored in a specific location close to the production site, thus avoiding the waste of time in the production process. All the paper that is not used or returned is taken to a recycling company. The offset printing plates are also sent for recycling.

The newspaper delivery is performed by motorcycles and follows a pre-fixed route, with the purpose of speeding delivery and avoiding waste of fuel. For the distribution of phone directories and guides, the suppliers are hired in accordance with the Company's policies. It is worth pointing out that Algar Mídia has been investing significant amounts in digital products (Out of Home, Netsabe, Correio de Uberlândia online newspaper), which comes in line with the current trend and produce a lower environmental impact.

GRI: EN26

In 2012, Algar Telecom's Class I hazardous waste disposal totaled nearly 180 tonnes, including electronic equipment, pay phone domes and air conditioners, versus 160 tonnes in 2011.

GRI: EN24

Product and package recovery

Algar Telecom runs an awareness-raising campaign to encourage clients to return mobile phones no longer used. Since these devices are considered potentially hazardous, the Company takes charge of reverse logistics, disposing of each type of equipment in the correct place, all of which have a disposal flow and certification.

In 2012, 450 kg of mobile phones and components were sent to specialized recycling companies. For 2013, the Company plans to maintain the collection boxes for such materials in its own stores, shopping malls, schools and in other locations of the city, with the purpose of collecting and disposing the residues in a suitable manner.

GRI: EN27

Supplier training

Algar Telecom seeks to establish partnerships with suppliers that are also committed to sustainability. To this end, the Company has included, since 2010, an environmental provision in its contracts, which also addresses issues such as documentation, child and slave labor. Moreover, with the purpose of assuring effective adherence to the new rules, all every supplier must take a distance education training course, which includes a corporate presentation and the Company's environmental projects.

Social Sustainability

Algar Telecom believes that its operations and ongoing expansion have to promote the social development of the communities in which it is present. Constantly seeking to undertake initiatives that can change people's lives permanently, the Company believes that education is the most effective means to become engaged in improving human potential.

The educational initiatives geared towards the community, developed by the Company over the last eighteen years, have been made feasible through Instituto Algar. It is an OSCIP (Organização da Sociedade Civil de Interesse Público, or Public Interest Civil Organization) that receives donations from all the Group's companies. This enables the organization to develop social initiatives that contribute to the human development of school children and educators, which involves continuing education activities for educators and students to improve reading and writing skills, as well as promote digital inclusion. The Company's associates are also encouraged to participate as volunteers in the program.

In 2012, from the total fund raising of R$ 3 million, Algar Telecom contributed R$ 2,2 million. These funds allowed the Institute to extend the coverage of its program, from 11 to 16 cities in four states: São Paulo, Minas Gerais, Paraná, Goiás and Maranhão, involving nearly 350 educators and 6,700 students. All the cities to which the programs were extended are in the area in which Algar Telecom is expanding, which shows that Grupo Algar's business growth and social sustainability initiatives go hand-in-hand.

OUTLOOK

The current situation of the telecommunications market in Brazil points out to good prospects for all the Algar Telecom's business segments. The positive results attained in 2012 evidence the correctness of Algar Telecom's strategic plan, which enables it to assure a sustainable growth.

Always ahead in terms of new technologies, Algar Telecom is undergoing an advanced stage concerning the migration of its network to NGNs (Next Generation Networks), which will enable the total traffic of voice, data and image to flow through a single network, more flexible and of higher capacity.

The constant enhancement in telecom infrastructure is crucial for the development of activities within the Company's areas of concession and authorization, in addition to enabling the expansion in the corporate clients portfolio, the Company's main driver for growth. In 2013, the company will continue expanding its operations in cities and towns along the existing backbone in order to reach at least ten new cities and strengthen the brand to increase penetration in the geographic areas in which it is already present. The inauguration of the Algar Group's headquarters in São Paulo, in 2012, alongside further inaugurations planned for 2013, are expected to contribute to this objective over the next years.

Another contributing factor to bolster the participation in the corporate market is the Clube Corporativo Prime (Prime Corporate Club), created to serve a distinguished group of clients in a personalized manner. This new commercial approach, which yielded quite positive results in 2012, is planned to be extended to a broader number of clients in 2013.

In Business Process Outsourcing and IT, the strategy is to continue investing in infrastructure and offering new customized solutions. In Complementary Businesses, Engeset, which plays an important strategic role in developing the Telecom segment, relies on an ongoing expanding addressable market. Algar Mídia, in seeking to develop its role as a significant link between small and medium companies and its target public,

remains committed to develop new electronic media. Its main potential for growth lies in the exposure media segment (voice tools and monitors installed in areas of major circulation and public concentration). For 2013, it is expected to yield positive results from the unification of printing and online sales team, which acts in the updating media (newspapers) and consulting (directories).

As for the corporate governance area, 2013 will be geared towards the execution of risk mitigation plans, developed over the last two years. In terms of sustainability, Algar Telecom remains committed to becoming a Green or Environmental Conscious Company, proceeding with the initiates aimed at reducing power consumption and Greenhouse Gas Emissions, in addition to contributing to society in the cities where it operates, through the educational initiatives developed by Instituto Algar.

As important to the future as are the concerns with efficiency, productivity and corporate responsibility, one of Algar Telecom's major challenges consists in the enhancement of relationship quality for 2013. The Company continues to tread with conviction that its main competitive edge results from its capacity to provide distinguished services to its clients. To this end, it will maintain its massive investments in innovation and human talents management.

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