

# Chairman's Statement



*Telecommunications industry is now undergoing Big Change, Big Integration and Big Development, generating new opportunities and challenges. Our people, instead of getting complacent with their past successes, proactively liberate their own mindsets. They are keen to embrace the changes and innovate for breakthroughs, striving to bring more compelling experience and delights to our customers. Seeing their dedication to the success of the company, I feel so encouraged and grateful. I also firmly believe that a vibrant, responsible and innovative China Telecom is emerging and will be a legend again!*

In 2013, the Company accurately captured the development pattern of mobile Internet and the integration trend of the industry. Deepened transformation has enhanced its scale as well as profitability, with progressive strengthening in market position. Riding on the comprehensive implementation of the "Three New Roles"<sup>1</sup> strategy, the emerging businesses experienced rapid growth while the business structure optimisation has accelerated, steadily enhancing our corporate development capabilities. Adhering to the Internet's spirit of "openness, cooperation and innovation", the Company boldly explored and accelerated its evolution into a mode of operation that integrated deepened efficiently-centralised management and comprehensive subdivision of performance evaluation units, leading to pronounced improvement in corporate vitality and efficiency. The Company also established its grand blueprint of "creating a New China Telecom in five years". 4G licensing started a new era of mobile Internet, bringing vast potential for future corporate development.

## Operating Results

In 2013, the Company continued to maintain its healthy and rapid growth momentum. The operating revenues amounted to RMB321.6 billion, representing an increase of 13.6% over last year. Excluding the mobile terminal sales, the operating revenues were RMB284.1 billion, representing an increase of 10.0% over last year, with revenue growth surpassing industry average and revenue market share further increased. Of which, mobile revenue accounted for approximately 50%, and the business structure continued to optimise. Profitability has been significantly enhanced with the profit attributable to the equity holders of the Company reaching RMB17.5 billion, increased by 17.4% over last year, and basic earnings per share were RMB0.22. EBITDA<sup>2</sup> was RMB96.6 billion, while EBITDA margin<sup>3</sup> was 34.0%. Capital expenditure was RMB80.0 billion. Free cash flow<sup>4</sup> reached RMB11.1 billion.

1 The "Three New Roles" refers to the Leader of Intelligent Pipeline, the Provider of Integrated Platforms and the Participant of Content & Application Development.

2 EBITDA is calculated based on operating revenues minus operating expenses plus depreciation and amortisation.

3 EBITDA margin is calculated based on EBITDA divided by the operating revenues excluding mobile terminal sales.

4 Free cash flow is calculated from EBITDA minus capital expenditure and income tax.

Taking into account the return to shareholders, the Company's cash flow and its capital requirements for future development, the Board of Directors has decided to recommend at the forthcoming Annual General Meeting that a dividend being an equivalent of HK\$0.095 per share for the year 2013 be declared. Dividend per share increased by 11.8% compared to 2012.

### **Strong execution reinforcing corporate strength**

#### **Fundamental services continued its scale development**

In 2013, the Company accelerated its scale expansion and significantly increased its market influence by fully leveraging the competitive strengths in network, brand recognition and services edges in mobile services and benefiting from the efficient unified operation of the network assets and mobile services as a whole. Persisting in a terminal-led approach and reinforcing terminal segmentation, the Company continuously expanded the variety of terminal models and optimised the structure of the Company's terminal device offerings. Through the deepening of channel distribution, the Company focused its strengths on enhancing the coverage and the portion of sales derived from open channels, which further improved the overall capability and strength of open channels. The Company's subscriber base and quality continued to enhance through initiatives such as strengthening application-driven development, continued improvement in functionalities and presentation of applications, and refining customer acquisition strategy. Mobile services revenue reached RMB113.8 billion this year, representing an increase of 23% over last year, which was the highest growth rate in the industry. The net addition of mobile subscribers was approximately 25 million, with total mobile subscribers reaching 186 million. 3G subscribers had a net addition of approximately 34 million, with a total exceeding 100 million. The number of 3G subscribers as a percentage of total mobile subscribers increased to 56%, further optimising the structure. The Company's fundamental market share was further strengthened, with its mobile subscriber market share surpassing 15%.

The Company persisted in profitable scale development and has seen a steady and healthy growth in its wireline broadband services with its high-speed fibre broadband services fully rolled-out. The Company has comprehensively stepped up its efforts in its

wireline broadband network maintenance and service quality enhancement, and has continued to promote bandwidth upgrade. The Company introduced the 100Mbps home fibre broadband product, which improved customer experience and network utilisation, resulting in the steady growth in return. The Company propelled the increase in its customer value by enriching its high-bandwidth products portfolio, accelerating the research, development and promotion of "Smart Family" products and strengthening the premium content and enriched value. The Company insisted on rational competition and gained customers' recognition through high price-to-performance factors, defending the value propositions of the industry, while reserving room for future growth. Wireline broadband revenue reached RMB70.8 billion this year, representing an increase of 6% over last year. The total number of wireline broadband subscribers exceeded 100 million, with a net addition of approximately 10 million. Among these subscribers, the number of Fibre-to-the-Home (FTTH) subscribers was close to 27 million, representing an increase of over 70% year-on-year. FTTH subscribers accounted for nearly 30% of the total number of wireline broadband subscribers and the subscriber structure has been further optimised.

#### **Emerging businesses grew rapidly**

In 2013, the Company prospected the industry landscape and accelerated the strategic restructuring of its business structure. Emerging businesses, including mobile data traffic, Internet applications and informatisation applications, experienced rapid growth of nearly 30%, accounting for close to a quarter of the total revenue. The new customer acquisition approach led by applications and services achieved remarkable results. The Company has duly implemented its deepened strategic transformation.

Continued optimisation of data traffic operation fostered the rapid growth in the scale and value of data traffic. The Company reinforced its efforts in targeted marketing and locked its sights on its targeted customer groups through its continuous efforts to reinforce its brand awareness and brand influence, and offering data-focused, flexible and self-designed packages to high value customers. By strengthening the promotion of smart terminals, enhancing the pre-installed applications and customer coaching and enhancing customer experiences, the Company cultivated and strengthened the customers' data usage habits. Relying on its intelligent pipeline and integrated platform, the Company fully exploited the

data-converging characteristics of its Internet portal-type applications such as "YiChat" and "Best Pay", to strengthen its product offerings focusing on dedicated-data traffic and data traffic backward monetisation operation. During the year, smartphones sales accounted for more than 80% of the total handset sales, while the total data traffic by 3G handsets increased by 142% over last year. The monthly average data traffic per 3G handset subscriber reached 190MB, representing an increase of 42% from last year. Internet access revenue by handsets increased by 88% from last year, while the 3G handset Internet access ARPU accounted for 33% of the 3G ARPU.

The accelerated promotion of Internet applications and industry-specific applications drove the robust scale development. With a rapid scale expansion of "Best Pay", the penetration of customers, entrepreneurs and financial system has progressively expanded. In 2013, the transaction amount of "Best Pay" reached RMB133.1 billion, representing a growth of 226% over the previous year. The Company also jointly launched "YiChat" with NetEase, Inc. to promote the development of product hosting channel and create a new type of mobile Internet portal. At present, the number of registered "YiChat" users is nearly 60 million. To actively develop the cloud computing applications, the Company proactively promoted the incorporation of the "cloud" element into its existing products and services to further enhance its product range. In order to reinforce its efficiently-centralised development, the Company completed the strategic planning of 16 application development centres covering eight industries to promote the continuous optimisation of the informatisation application system. Emphasising on the Smart Cities project and key industry customers expansion, the Company continued to strengthen its edge on strategic cooperation in informatisation applications. With a focus on customer experience, the Company placed an equal emphasis on product standardisation and differentiation. Through the improvement of the functionalities of informatisation applications and service quality, customer satisfaction has been enhanced which effectively increased the value of customers' contribution. During the year, there was a net addition of over 13 million mobile subscribers driven by industry-specific applications, up by 30% from last year, of which over 70% was generated from its six major applications including the "e-Surfing School" initiative.

## Reform and innovation accelerating the creation of differentiated edges

### Persistence in innovation and cooperation brought remarkable results in the "Three New Roles" strategy

The Company boldly created a new model of open cooperation for the development of the emerging businesses, and successfully introduced the essential elements of mobile Internet into the model, leading to a landmark breakthrough for the Company. With newly set segregated operating systems and mechanisms for the emerging businesses, the Company offered support to a highly-efficient "Internet-business type" operating environment and an effective incentive mechanism. By adhering to its market-oriented and capital-driven approach, the Company facilitated dynamic and flexible resources allocation and effectively strengthened its organic vibrancy. With the launch of "YiChat" as a breakthrough, the Company leveraged the Internet companies to rapidly power up its competitive strengths. The Company also leveraged the resources edges of the network, platform, customer services and marketing channels, and the enriched experiences in Internet-type product operation and online sales in the cooperation. The Company has effectively penetrated and integrated the current market influence and customer base of both parties to converge the strengths and opened up a new path for Internet-type services.

Conforming to the industry convergence trends and learning from the mobile Internet development experience, the Company constructed an "Internet-business type" model and accelerated the comprehensive commercial implementation of the "Three New Roles" strategy. The Company fully enhanced the data traffic control and billing capabilities based on customers and service identification. The Company strengthened the self-determined bandwidth upgrade-on-demand function for wireline broadband subscribers. With the promotion of "Big Data", the Company started to monetise from its intelligent pipeline by turning the edges of big volume of data into edges of valuable services. By strengthening the capabilities such as location-based services and unified account operation, the Company sped up the process of opening up its capabilities for cooperation and progressively implemented the integrated platform. The Company accelerated product development and promotion, initiated three business groups: digital entertainment, e-commerce and information services,

and enriched their contents and application systems progressively.

### **Focusing on efficiency and vitality to accelerate the evolution of corporate operation model**

With our in-depth study and grasping the pattern, we set vitality and efficiency as our core objectives on developing a new operation model with the key features of reasonable sub-division of performance evaluation units and efficiently-centralised management operation, for accelerated preparation to adapt to mobile Internet development.

To promote the “market-driven” reform, the Company continued to sub-divide performance evaluation units to fully inspire employee vitality. With a perseverance to explore, the Company further implemented the sub-division of performance evaluation units in the whole company from bottom to top including sales outlets, rural sub-branches and investments units, which allowed better matching between operation responsibilities and authorities of resource allocation such as cost and investment resources in the frontline business units, and established a close and direct linkage between the employee remuneration and the integrated return of the frontline business unit. This resulted in high degree of alignment of the operating goals of the frontline business units with the overall corporate goal and highly aligned the interests of the employees with those of the Company. Over the past year, the operational efficiency and profitability of the frontline business units experienced a rapid growth.

Adapting to the development pattern of the mobile Internet business, the Company further stepped up its effort in efficiently-centralised management to strengthen its entire-network operation and management capabilities. The Company also accelerated its network upgrade, and steadily expanded its capabilities. Platform integration and consolidation was strengthened and cloud resources were deployed to further enhance the level of efficiently-centralised operation of the network. The Company further refined its package structure resulting in an increase in the proportion of the sales of efficiently-centralised packages. With a focus on the promotion of “Best Pay”, “YiChat” and all sorts of livelihood-related applications, the product management systems were continuously optimised. The Company strengthened the synergistic collaboration of channels, promoted the efficiently-centralised control and resources exchange

of open channels such as large chain stores and manufacturers, enhanced integrated operation and development of electronic channels at group level to further strengthen the overall capability in channel sales. To lower the management costs, the Company continuously improved its level of efficiently-centralised management on procurement, IT, finance and other areas. Through promoting the efficiently-centralised operations of overseas businesses, profitability was significantly enhanced. The Company recorded a 38% growth in the revenues from overseas during the year.

The Company adopted various initiatives to improve its operating efficiency and profitability. The Company implemented a market-oriented approach internally by focusing on the key evaluation metrics and optimising its resources allocation model while creating an internal competition mechanism for costs and investment resources to tilt the resources towards high growth and high returns areas. To adapt to a new operating model, the Company restructured its front-end organisation, and further strengthened the efficiently-centralised operation and co-ordination from a vertical perspective while enhancing the synergistic collaboration of various sales channels to enhance the efficiency of its front-end decision-making and execution. The Company also innovated services approach with customer experience as a core by launching multimedia customer services on Internet through handset application, “YiChat” and “Wechat” to achieve “one-point access for entire-network service”. The Company progressively promoted the mobility of service processing to further improve service efficiency. The Company strengthened precision management by actively enhancing the utilisation and consolidation of its existing assets, as well as increasing the level of capital centralisation, strengthening its control over investment and costs to increase the efficiency and return of the use of its capital and assets.

### **Corporate Governance and Social Responsibility**

We continue to strive to maintain a high level of corporate governance, attaching great importance to risk management and control. We strive to enhance corporate value and transparency to ensure our healthy and orderly growth. Our persistent efforts in corporate governance have been widely recognised by the capital markets. We were accredited with a number of awards and recognition, including being voted the “No. 1 Best Managed Company in Asia” by *FinanceAsia* for three

consecutive years, "No. 1 Most Honored Company in Asia" by *Institutional Investor*, and also "Overall Best Managed Company in Asia" by *Euromoney* five years in a row.

We persisted in operating with integrity and proactively fulfilled our corporate social responsibility while promoting a healthy and orderly development of our industry. Meanwhile, we enhanced the information security assurance for our nation and customers, while persistently maintaining a good network environment by actively promoting Internet interconnections and further strengthening energy conservation and emission reduction. We also helped proactively with fighting major natural disasters such as earthquakes and typhoons, and have accomplished telecommunications assurance services for significant events such as the China-Eurasia Expo and the launch of Shenzhou-10 spacecraft, receiving high recognition and appreciation from the society.

## Outlook

At present, China's deepening reform and accelerating the adjustment and restructuring of the national economy, together with accelerating social informatisation process with the promotion of information consumption and implementation of "Broadband China" strategy, offers vast market potential. The mobile Internet business in China has undergone an explosive growth momentum. Coupled with the accelerated evolution of technology and industry chain, there is a rapid upgrade in smart terminals and data usage habits. 4G licensing opens up a brand new development space for mobile Internet, bringing in a valuable opportunity for a full scale transformation and upgrade in the information industry. Meanwhile, the global economy is still in a deep adjustment period. More industry reforms pushed by integrated development are emerging. "Customer flow, Data traffic flow and Capital flow" now become the new key value of the industry development. The value shifting in the industry is accelerated, while competition is further intensified in respect of its scope and magnitude with gradual roll-out of regulatory policies such as amendments to wireline broadband competition policies. As such, the Company will face new challenges.

With the 4G licensing, China Telecom embraces the best period of its full-services operations. We will grasp the opportunity for rapid development, proactively and appropriately tackle the challenges from regulatory and policy changes such as national tax reform, striving to create a New China Telecom. Based on the characteristics of its own resources, the Company will fully leverage the dual-technology strengths of wireline broadband and wireless broadband and continue to strengthen the wireline broadband network through the IPv6 evolution and fibre broadband. The Company will also actively apply for the permit of LTE FDD operation and will deploy LTE network appropriately with regard to the government policy and business development. A seamless high-speed mobile network built through the hybrid LTE network, coupled with highly efficient and coordinated development of 4G and 3G, will establish a full scene of network edge. The Company will deepen the reform to create incremental value, share the return with employees to fully unleash their vibrancy, and accelerate the evolution towards an Internet-business type operation model. Capitalising on reform and innovation, the Company will firmly persist in the implementation of the "Three New Roles" strategy. With quality and efficiency enhancement, the Company will promote dual enhancement in scale development and profitability with continual reinforcement in competitiveness. By proactively open cooperation based on complementary resources and edge, the Company will endeavour to achieve a win-win cooperation in the industry value chain and accelerate the strategic planning of emerging businesses. The Company will strive to expand the value creation areas and continue to be the forerunner in the mobile Internet era, while continuously creating new values for shareholders.

Finally, on behalf of the Board of Directors, I would like to take this opportunity to express my sincere appreciation to all our shareholders and customers for their support, and my gratitude to all our employees for their hard work and their contribution to the Company.



**Wang Xiaochu**  
Chairman and Chief Executive Officer  
Beijing, China

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