



***MD&A***

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## BUSINESS REVIEW

The following table sets out the key operating data for 2012, 2013 and 2014:

	Unit	2012	2013	2014	Rate of change over 2013
Mobile subscribers	Million	160.62	185.58	<b>185.62</b>	0.0%
Of which: 3G/4G subscribers	Million	69.05	103.11	<b>118.63</b>	15.1%
Wireline broadband subscribers	Million	90.12	100.10	<b>106.95</b>	6.8%
Access lines in service	Million	163.00	155.80	<b>143.56</b>	-7.9%
Mobile voice usage	Million minutes	509,229	603,616	<b>655,939</b>	8.7%
Mobile SMS usage	Million messages	55,789	64,235	<b>64,583</b>	0.5%
Handset data traffic	KTB	72.3	175.1	<b>273.2</b>	56.0%
Wireline local voice usage	Million pulses	172,175	148,690	<b>130,439</b>	-12.3%
BestPay gross merchandise value	RMB Billion	40.8	133.1	<b>352.0</b>	164.5%



*Conducted video calls with the southern-most city in China through the 4G network*

In 2014, in the face of various changes in policies and the environment both within and out of the industry such as the licensing of 4G services and Value-Added Tax Reform (VAT Reform), the Company proactively adapted to and took initiatives to manage the challenges, continued to promote the transformation of sales and marketing models and developed extensive cooperation in various fields. The Company achieved steady growth in subscribers' scale and industry-leading growth in service revenues with a continual increase in the proportion of revenues attributable to its emerging businesses and a further enhanced competitive position in the market.

**Handset Data  
Traffic 273  
KTB**

### Key operating performance

#### (1) Industry-leading growth in revenue with a continually optimising structure

In 2014, the Company's operating revenues increased by 0.9% to RMB324,394 million. Service revenues increased by 3.1% to RMB287,379 million. The Company's revenue structure was further optimised, with mobile revenues accounting for 46.7% of operating revenues, and revenues of emerging businesses accounting for 29.1% of service revenues, up 4.8 percentage points.

#### (2) Steadily growing mobile services with remarkable results in data traffic operations

In 2014, the Company strengthened its content application-driven strategies, promoted the transformation of sales and marketing models, persisted in the terminal-led approach and deepened cooperation with open channels, achieving a collaborative development of 3G and 4G services and managing to maintain a stable scale of mobile subscribers with an optimised subscriber structure and steady growth in the revenues of mobile services. The number of mobile subscribers reached 185.62 million, with a net addition of around 40,000 subscribers, and mobile service revenues increased by 5.7% over last year to RMB120,268 million.

The Company continued to improve the data traffic product offerings, and launched 4G packages focusing on data traffic and multi-terminal data sharing. We upgraded "DIY" data packages to fully customised packages and regulated the data traffic promotion strategies, maintaining a steady value of data traffic. The Company actively strengthened the development of data backward monetisation and launched data backward monetising products such as "Liuliangbao" and Data Traffic 800, expanded high-valued data traffic customers in scale and at the same time cooperated with Internet companies to promote heavy data usage applications, such as video streaming. In 2014, total handset data traffic reached 273KTB, with an increase of 56% compared to last year, and the monthly average mobile data traffic per handset subscriber reached 227MB.

**FTTH**  
subscribers  
~40%  
of the total  
wireline broadband subscribers

**(3) Wireline broadband services continued to develop steadily, maintaining a leading position in the market**

In 2014, the Company continued to promote the implementation of wireline and mobile integration, enhancing customer value while stabilising the wireline revenue base. Wireline revenues increased by 1.4% to RMB172,783 million, maintaining positive growth in revenues.

In response to regulatory policy changes and in order to reinforce its competitive edges in the wireline broadband market, the Company continued to rapidly promote fibre network construction and bandwidth upgrade, and further optimised the subscriber structure, thereby achieving steady growth in subscriber scale and revenues. In 2014, wireline broadband revenues grew by 3.8% to RMB73,485 million. Total number of wireline broadband subscribers reached 106.95 million with a net addition of 6.85 million subscribers.

In 2014, revenues from wireline value-added services (VAS) and integrated information services were RMB38,047 million, representing an increase of 11.0% over the last year, with iTV, IT Services and Applications and IDC business being the three key drivers for promoting the growth in the revenues of VAS and integrated information services. The Company reinforced its efforts in promoting the integration of iTV and high-speed

broadband services and enhancing customers' usage experience. With the support from industry application bases, the Company focused on key industry applications to accelerate the development of its ICT business. The Company also enhanced the deployment of its cloud data centres, improving the cloud products platforms and service capabilities.

In 2014, the Company's operating revenues attributable to the wireline voice services further declined, which effectively alleviated the Company's operational risks. Revenues from wireline voice services were RMB33,587 million, or 10.4% of the operating revenues, down 1.6 percentage points compared to last year. The upgrade of the Personal Access System (PAS) subscribers was basically completed.

**BestPay**  
GMV > RMB 350bil  
↑ 164%

**Business operating strategies**

In 2014, the Company closely grasped the work principles of "reform and innovation, open cooperation, and quality and efficiency enhancement", proactively adapting to various changes in policies and the external environment. The Company continuously enhanced its capabilities in areas such as operation, sales and services by transforming its development models and optimising customer acquisition methods. Seven key operational measures were implemented:

**First, efficiently centralising operations in 4G business and strengthening the collaborative development of 3G and 4G**

In 2014, the Company was permitted to commence the LTE hybrid network trial, with a launch of 4G handset services in 56 cities. The Company conducted efficiently-centralised operations of the 4G business and carried out standardised brand and sales promotion campaigns across the entire network by making available one-stop services, standardised tariff and efficiently centralised sales service. We also strengthened the collaboration of 3G and 4G businesses and unified the policies for 3G and 4G services in respect of areas such as package design, resources allocation, sales models and marketing plans. The number of 3G/4G subscribers reached 118.63 million, or about 64% of mobile subscribers. Handset Internet access ARPU and average data traffic per subscriber also increased significantly.





**Second, creating differentiated broadband products for enhanced core competitive advantage in broadband services**

In 2014, the Company continued the promotion of the fibre upgrade for its broadband networks, continually transformed network capabilities into market capabilities through an exploration of capabilities, driving customers to adopt high bandwidth services. With deepened integrated development, the Company launched products such as “Speedy Connect” Card and “Speed Upgrade” Card and expanded open sales channels and implemented collaborative sales operations for online and offline channels. The Company also created a smart family business portal by introducing the “Joy me” product, thereby enriching

high bandwidth applications. FTTH subscribers reached 42.61 million and subscribers of services with 8Mbps access bandwidth or above accounted for a proportion of 45.7%, increased by 18.8 percentage points over 2013.

**Third, persisting in a terminal-led approach, maintaining a prosperous industry value chain**

Through supporting the research and development of chipset manufacturers, the cost of mobile terminal chipsets was lowered. 305 new mobile terminal models were launched within the year, of which more than 100 were 4G terminals while smart devices accounted for over 80% of the terminal sales. The Company provided

terminal direct subsidy to terminals below RMB700, encouraging the industry value chain to drive the sales of mid-to-low end smart devices. We were the first in the industry to launch the “multi-mode” smartphones, and made every effort to gain a share of the handset replacement market of existing customers. The Company also actively attracted the market of popular terminals, such as OPPO, VIVO and Meizu for open channels and Xiaomi, Honor and Dazen for Internet channels. All such popular brands launched customised handsets for China Telecom.

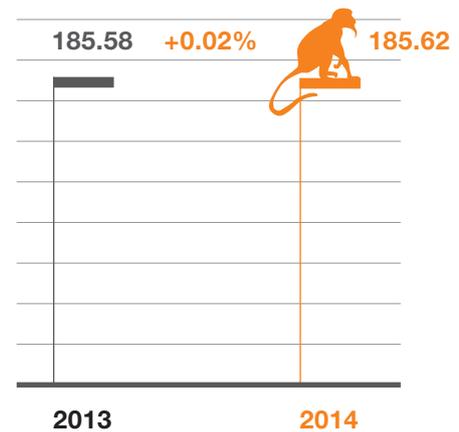
**Fourth, acceleration of the Internet-oriented transformation of channels and implementation of the O2O cooperative model**

The Company accelerated the promotion of the efficient expansion of channels and their professional operations, as well as carried out O2O operations that strengthened traffic flow via online channels and strengthened user experience via offline channels. For physical channels, we focused on increasing the coverage of open channels in urban core business districts, implementing tiered management in store and distributor levels in specialty channels and at the same time establishing sales outlets for “multi-mode” handsets in rural areas. For direct sales channels, the Company established exclusive service centres focusing on enterprise customers in key industries; it also adopted a collaborative marketing approach

integrating “channel manager + distributor + physical store” which focuses on small and medium-sized customers. We accomplished efficiently-centralised operations for electronic channels in the entire network, developed personalised products and innovated the development model of electronic channels through extensive cooperation with e-commerce companies in the society, with a focus on young users.

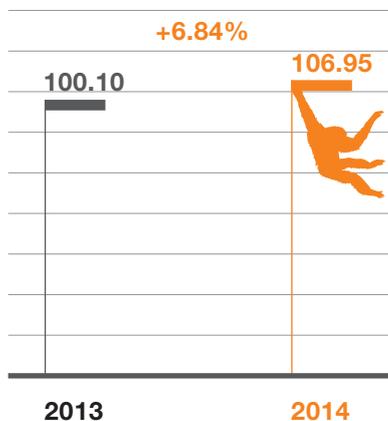
**Mobile Subscribers**

(million)



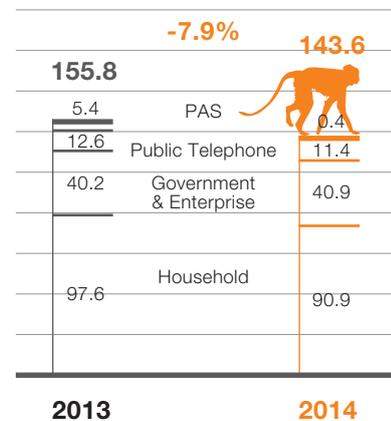
**Wireline Broadband Subscribers**

(million)



**Access Lines in Service**

(million)





### Fifth, enhancing application promotion to enhance customer value

In 2014, the Company continued to innovate application products and reinforced its efforts in promoting the various applications. In respect of Internet applications, the Company continued to strengthen its Internet application development system which comprises of portals, content and capabilities, leading to a significant improvement in user scale and the capability of application platforms, such as YiChat, BestPay and the integrated platforms. In respect of industry applications, the Company primarily promoted products such as Popular Shop Assistant, Out-of-Office Assistant, video streaming services, general office assistance services and e-Surfing RFID, targeting at various individual customer groups. The Company also focused on promoting products such as “e-Surfing School” and “Nongjibao” in schools and rural markets. In respect of daily life applications, the Company reinforced its efforts to promote public transportation applications, banking services applications and BestPay application based on NFC function.

### Sixth, promoting sub-dividing performance evaluation units with performance contracts, unlocking internal momentum and vitality of the Company

In 2014, the Company deepened the reform in establishing market-driven resource allocation and operation mechanisms, fully promoting the “sub-dividing performance evaluation units with performance contracts” project among frontline production and operation units, and creating autonomous operation entities that are highly unified in terms of accountability, authorities and interests. Through key procedures including flattening organisation structure, authority delegation, “top-down” service system, process reengineering, efficiently-centralised support and reversed evaluation, the Company also promoted the construction of “top-down” management and support system to allow frontline employees who were closest to the customers to decide on internal resources

allocation of the Company, motivating the enthusiasm, proactiveness and creativity of the individuals with delegated authorities. In 2014, over 80% of the frontline operating units implemented “sub-dividing performance evaluation units with performance contracts”, and 70% of the individuals with delegated authorities were selected by a market-oriented approach, leading to a widely acclaimed market-oriented mechanism.

**Seventh, focusing on customers’ perceptions to promote the Internet-oriented transformation of services**

Focusing on its key services including 3G/4G and broadband, the Company established and implemented service standards, promoted convenient and transparent services, implemented regular customer experience programmes in multi-levels and various ways, comprehensively promoted the construction of a credit management system and carried out service promotion campaigns, sustaining a continual leading position in customer satisfaction and maintaining the No. 1 position in the industry in the customer satisfaction assessment on both wireless and wireline internet access services conducted by the Ministry of Industry and Information Technology in 2014. The Company proactively adapted to the industry development trends, and accelerated the Internet-oriented transformation of services while promoting self-service and sharing-based online services. A significant improvement in the service capabilities of the new channels was achieved, as the users of new media customer service channels (YiChat, Weibo and WeChat customer services) reached over 127 million and the average monthly service volume exceeded over 74 million times.

**Network and operation support**

In 2014, the Company further optimised resources allocation to secure major networks constructions for mobile, broadband and emerging businesses, etc.

First, leveraging the prime opportunities of the 4G hybrid network trial, the Company accelerated the deployment of 4G networks in 56 trial cities and promoted 4G auxiliary facilities construction in over 100 key cities across the country, assuring network support for the development of the 4G service of the Company. In respect of the existing 2G/3G network, the Company mainly focused on network optimisation and its effective collaboration with 4G service, steadily implementing precise construction and capacity expansion in key



PT / EXPO COMM CHINA 2014



ITU Telecom World 2014



World Internet Conference



areas, maintaining high network quality and excellent customer perception and steadily increasing network utilisation rate, efficiency and return. During the year, the mobile network utilisation rate increased by 3 percentage points.

Second, taking deepening reform and sub-division of investment units as focus, the Company continued to promote the precision and timeliness of its broadband investment and construction and focused on expediting fibre network transformation and bandwidth upgrade in urban core districts. 90% of the southern city areas were covered by networks with 20 Mbps or above. The FTTH access port utilisation rate reached 46%, up 6 percentage points.

Third, the Company accelerated the application of new technologies, effectively supporting the development of emerging businesses. Deploying efficiently-centralised cloud resource pools, the Company was able to launch new products within a short period of time. The Company also continued to promote the integration of cloud technology in its business platforms and improved the operating efficiency of its centralised operations. The 400G platform routers were brought into the carrying network to improve the capacity and

carrying capability. The Company continued to promote the capacity expansion of the metropolitan area networks and the transformation of the next-generation Internet, improving the overall carrying capability of emerging businesses.

### Development measures and highlights for 2015

A series of policy changes in 2014 had brought a long-term impact on the business. In 2015, apart from facing the changes in severe challenges from the changes in the traditional operating model, the Company also sees the enormous market opportunities from the flourishing development in the consumer Internet market and the emerging industrial Internet market. With differentiation as its main line, the Company further changes its subscriber acquisition model and promotes the dual enhancement in corporate scale and efficiency. In respect of mobile services, the Company will fully commence its 4G business operations, leveraging the differentiated advantages of its FDD network and continuously optimising customer experience. In addition, the Company will introduce non-cash cost marketing model, carrying out differentiated marketing and targeting refined markets by strengthening content

applications and offering differentiated products. Following the terminal-led approach, the Company implements “the Excellence 100” programme and launches special handsets such as security handsets and video handsets. In respect of its broadband business, led by the 100Mbps broadband service development, the Company continues to promote the construction of fibre networks, fully realise the end-to-end bandwidth upgrade in terms of access capability, achieving significant improvement in the average access bandwidth and creating the core competitiveness of its broadband services. To promote the integration of marketing and maintenance, the Company optimises its service process, introducing instant installation upon the completion of sales. To enrich the applications for high bandwidth adoption, the Company promotes “Joy me” and cloud products and expands and develops smart home applications such as video surveillance. In respect of its emerging businesses, first, the Company refines data traffic operations based on big data and multi-dimensional analysis of customer behavior characteristics, optimising the data traffic products and implementing targeted and precise marketing. The Company increases promotion of data backward

monetisation, opening up external cooperation capabilities of “Liuliangbao” and unifying the product form of “Data Traffic 800”. Second, expanding information services and seizing opportunities from the traditional industry upgrade, and advancing the change of ICT to IIT (Information Internet-ware Technology), the Company expands the scale of informatisation products. The Company efficiently centralises the development of cloud products, strengthening research and sales of products such as cloud hosting, private cloud and object-based storage systems and speeding up the construction of the IDC unified operating system. Third, the Company diversifies the mobile Internet applications, promoting payment, YiChat, security products and others to satisfy the lifestyle and entertainment demands of customers, and promoting applications focusing on community, education, healthcare to meet the daily life needs of customers. We will also continue to optimise network resources, improve operating and maintenance efficiency, perfect service capabilities of full services and enhance customers’ satisfaction to attain continuous growth in customer value and corporate value.

