

Chairman's Statement



In the first half of 2016, with a unitary goal cohering as a whole, the Company adhered to the established development strategy to persist in excellent execution. Firmly seizing opportunities and taking steps in reform and innovation, the Company accomplished brilliant results. With accelerated expansion of operation scale, our business structure was continually optimised while our competitive capabilities were remarkably strengthened. The vitality of our employees was fully demonstrated. Through proactively grasping the arising opportunities and adapting to the changing trends in a timely manner, the Company firmly established a new strategy on transformation and upgrades, aimed at providing superb customer experience in an era of intellectual services and facilitating the Company's evolution into a leading integrated intelligent information services operator.

Overall results

In the first half of 2016, the Company had excellent performance in its overall results. Operating revenues amounted to RMB176.8 billion, representing an increase of 7.2% over the same period last year, achieving industry-leading growth. Service revenues¹ amounted to RMB155.2 billion, representing an increase of

5.6% over the same period last year with continual rapid optimisation in revenue structure. EBITDA² was RMB50.6 billion while EBITDA margin² was 33%. Profit attributable to the equity holders of the Company was RMB11.7 billion, representing an increase of 6.3% over the same period last year. Basic earnings per share were RMB0.14. Capital expenditure was RMB40.7 billion while free cash flow³ was RMB6.1 billion.

Taking into consideration the Company's profitability, cash flow level and the capital requirements for future development, the Board of Directors has decided not to pay an interim dividend this year in order to maintain adequate funding flexibility. The Board of Directors will proactively consider the expectation of shareholders' return and evaluate the final dividend proposal when reviewing the full year results and will propose to the shareholders' general meeting accordingly.

Scale Breakthrough with Favourable Trends

In the first half of the year, the Company comprehensively implemented aggressive marketing strategy and emphasised the operating focuses, "2+5"⁴. With persistent promotion of in-depth integration and enhancement in efficiently-centralised operation,

¹ Service revenues were calculated based on operating revenues minus sales of mobile terminals, sales of wireline equipment and other non-service revenues.

² EBITDA was calculated based on operating revenues minus operating expenses plus depreciation and amortisation while EBITDA margin was calculated based on EBITDA divided by service revenues.

³ Free cash flow was calculated from EBITDA minus capital expenditure and income tax.

⁴ "2+5" refers to two fundamental businesses namely 4G and fibre broadband plus five emerging areas namely e-Surfing HD, BestPay, Internet of Things, cloud and Big Data and "Internet+".



the Company expanded open cooperation and fully leveraged the differentiated edges, resulting in notable improvements in competitive strengths.

Comprehensive upgrade in 4G capabilities to drive industry-leading growth in mobile business.

By fully leveraging the competitive advantages in 4G network and “multi-mode” handsets, the Company increased efforts in integration and the effect of 4G driving the scale development of mobile business was evident. The net increase of 4G terminal users was 31.64 million, accounting for 18% market share in industry’s net additions. The total number of 4G terminal users reached 90.10 million, accounting for 15.2% market share. The net increase of mobile subscribers was 9.04 million, accounting for 32% market share in industry’s net additions. The total number of mobile subscribers reached approximately 210 million, representing 15.9% market share. 4G users accounted for 44% of total mobile subscribers, representing an increase of 14 percentage points from the end of last year. The monthly average data traffic per 4G user reached 889 MB while the aggregate handset Internet data traffic increased by 135% compared to the same period last year. The mobile handset Internet access revenue increased by 42% over the same period last year, accounting for 47% of the mobile service revenues. The mobile service revenues increased by 8.3% over the same period last year, outperforming the industry growth.

Sustained expansion of fibre broadband edges to further strengthen our leading position in broadband service.

The Company proactively implemented the national strategy of “Broadband China” and insisted on expediting bandwidth upgrade in broadband. Persistently driven by 100 Mbps products with trial run of 1,000 Mbps products, the Company comprehensively integrated and optimised our services quality, resulting in remarkable achievements in development. The wireline broadband service revenue increased by 3.3% over the same period last year, driving the wireline service revenues achieved healthy growth. The net addition of Fibre-to-the-Home (FTTH) subscribers was 17.35 million, reaching a total of 88.34 million. The net addition of wireline broadband subscribers was 4.94 million, reaching a total of approximately 120 million. FTTH subscribers accounted for 75% of the total wireline broadband subscribers, an increase of 12 percentage points from the end of last year. The market share of wireline broadband business within the service area of the Company’s wireline operations was 62% whereas the market share of FTTH subscribers was approximately 66%, continuing to maintain the leading position in wireline broadband market.

Rapid expansion in emerging areas and accelerated cultivation of new growth engines.

Leveraging the e-Surfing HD platform and smart home gateway, and riding on our competitive advantages in subscribers scale, the Company endeavoured to build a “Smart Family” system. The net addition of e-Surfing HD subscribers was 9.78 million, representing an increase of 129% as compared with the subscriber growth number recorded in the same period last year. The total number of e-Surfing HD subscribers exceeded 50 million while the revenue increased by 33% over the same period last year. The number of active “BestPay” subscribers exceeded 8 million and “BestPay” positioned the second in third-party ranking of mobile payment industry apps⁵, while total transaction amount was approximately RMB380 billion. The whole-network efficient-centralisation of Internet of Things (IoT) business was launched in April with a focus on key breakthroughs in areas such as smart transport, smart logistics, wearable devices and Internet of vehicles. In the first half of the year, the net addition of IoT connections exceeded

⁵ Data source: Top 20 mobile payment apps in June 2016 by Analysys.cn.

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3 million. The Company will expedite the construction of an advanced IoT platform through self-R&D and cooperation. Fully leveraging the integration of cloud and network together with the existing data resources advantages, the Company accelerated efficiently-centralised development of cloud and Big Data businesses. The revenues from cloud services increased by 41% over the same period last year while the revenues from Big Data increased by nearly 3 times. We actively explored and developed the "Internet+" market with a focus on three key areas including government administration, education and healthcare and hence the quantity of orders from key government and enterprise customers increased by nearly 30% over the second half of last year. The development trend of emerging areas progressed well with vast potentials in the future prospect.

Excellent execution with notable advantages

In the first half of the year, the Company examined and assessed the market trends, planned meticulously and executed efficiently to establish new and all-rounded competitive advantages while striving to promote changes towards a more favourable direction for the Company in the competitive landscape.

Extensive in-depth integration. Exploiting the competitive strengths in full-service operation, the Company promoted in-depth integration and innovative development in various areas including business, network, platform and services, resulting in mutual promotion and interactions amongst respective businesses while effectively driving concurrent enhancements in scale and value. The high-value users subscribing to 4G, fibre broadband and e-Surfing HD services accounted for 45%⁶ of total subscribers, facilitating the steady growth in operating revenues. Integration has become the Company's strong and powerful competitive edge.

Leading superior network. 4G and fibre broadband formed and shaped competitive network advantages featuring broad coverage, fast network speed and high stability. In highly profitable 4G service areas, the Company fully leveraged the strengths of international mainstream FDD technology, spectrum resources and

co-sharing of telecommunications towers as well as appropriately utilised carrier aggregation technologies. The integrated experience of the Company's 4G network has become users' preferred choice. Meanwhile, the Company has been approved to reform the 800 MHz frequency bandwidth and planned to build a nationwide high quality 800 MHz LTE network in year 2017 at low costs to achieve 4G network coverage in rural areas and in-depth coverage in cities. We will lay down the foundations for the VoLTE and NB-IoT networks so as to foster rapid accomplishment of industry-leading 4G network quality. Through the acceleration of fibre network coverage, end-to-end bandwidth upgrade and interconnection of data centres, the Company effectively secured a high speed and high quality network browsing experience for our customers. In the first half of the year, the average bandwidth of wireline broadband subscribers reached 37 Mbps, representing 20% higher than the industry average. This further strengthened the Company's leading market position in the fibre broadband industry, where we led the high-bandwidth development trends.

Flexible and innovative marketing strategies.

The Company endeavoured to promote "multi-mode" handsets as market mainstream, effectively expanding our sales radius and significantly improving our terminal competitiveness. Data traffic operations were further promoted and the cooperation with heavy data usage products such as video content was further reinforced, continuously enhancing data traffic scale and value. The Company continuously implemented the "Speed Upgrade and Tariff Reduction", gradually cancelled the long-distance and roaming charges, proactively innovated the billing model and became the pioneer in China to explore and introduce on trial basis the "All-charge-as-data" billing, which effectively simplified customers' choices and profoundly enhanced service attractiveness. The Company actively implemented Internet-orientation of channels, enhancing high collaborative operations of online and physical channels. The coverage and sales capabilities of physical channels were significantly improved while online channels have become the main sales channel for services such as data traffic packages and online top-up. The proportion of users derived from online channels continued to increase.

⁶ Up to the first half of 2016, the total number of users subscribing to access lines in service, mobile, wireline broadband and e-Surfing HD of the Company reached approximately 510 million.

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Remarkable achievements in cooperation.

The Company took the initiative in innovation of development model, extensively consolidated competitive resources, cooperated with strong partners, resulting in a win-win outcome. Fully leveraging the co-sharing of telecommunications towers resources, the Company has been at the forefront of offering a superior 4G network experience rapidly. With the promotion of in-depth cooperation with other parties in the industry and enhancements in the co-building and co-sharing of networks, the Company successfully promoted "multi-mode" handsets as a national standard. In the first half of the year, the proportion of "multi-mode" handsets sold in the industry reached 34%, enabling the Company to swiftly achieve the decisive breakthrough in developmental bottleneck. In emerging areas such as "Smart Family", mobile payment, "Internet+", cloud and Big Data, and IoT, the Company proactively carried out crossover cooperation and cultivated a highly efficient and synergetic industrial ecosystem by focusing on product services, network platforms, sales channels and resource integration. Our differentiated competitive strengths were effectively enhanced.

Convenient and highly-efficient services. The Company has always persisted in consumer-oriented focus with continual enhancement of customer experience. In order to achieve the integration of marketing and maintenance as a whole, the Company introduced service modes such as "instant installation process at sales" and "pay after installation". The online and physical channels were well coordinated, effectively expanding service channels. The Company comprehensively promoted premier services and the capabilities of the entire process service were continuously improved. In the first half of the year, the Company was ranked first in the industry in customer satisfaction for both mobile Internet and wireline Internet services.

Persistent and unwavering reform. The Company adhered to the reforms of mechanism and system, and continued the in-depth promotion of subdivision of performance evaluation units. The Company increased efforts in promoting frontline entrepreneurial platform

to persistently stimulate the vitality of employees, resulting in continual enhancement in the morale of development. The results of frontline performance contract units remarkably improved. By strengthening the market-oriented corporate resources allocation, together with the establishment and gradual optimisation of "top-down" integrated service support system and effective collaboration of front-end and back-end operations, the efficiency and effectiveness of the Company's overall operation was significantly improved. The "Internet+" talent development programme was established with a focus on nurturing a team of new talents including both professional and technical personnel, hence strengthening the Company's ability to attract talents. Vigorously promoting the transformation of achievements in innovation, the Company became the first batch of the state's model in mass entrepreneurship and innovation.

Continual optimisation of operation management.

Through precision management and efficiently-centralised operations, the quality and efficiency of our operations were significantly improved. The Company persistently promoted automation of network maintenance and further improved IT operational efficiency by leveraging support systems such as MSS, resulting in continuous enhancement in efficient centralisation of networks and IT operations. Through proactively deploying the co-building and co-sharing of networks, continually improving the financial management, strengthening the scope and depth of centralised procurement, and improvement in investment and cost efficiency, our corporate value was continually enhanced.

Comprehensive transformation and upgrades

Starting from the end of 2004, the Company unwaveringly persisted in pursuing strategic transformation and upgrades, and has surmounted tough difficulties to pave a new path for promoting China Telecom's development through transformation. At the end of 2004, the Company first put forth strategic transformation (Transformation 1.0)⁷, achieving a change from telecommunications to information services. By the end of 2010, the Company proposed in-depth transformation (Transformation 2.0)⁸ and

⁷ Transformation 1.0 defined the corporate as Telecom Full Service Provider, Internet Applications Aggregator and Leading Enterprise ICT Service Provider.

⁸ Transformation 2.0 adjusted the corporate's positioning as the Leader of Intelligent Pipeline, the Provider of Integrated Platforms and the Participant of Content & Application Development.

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explicitly defined the clear positioning of “Three New Roles” in order to adapt to the latest trend of mobile Internet and to proactively explore emerging business areas. The history has proved and confirmed that each and every transformation and upgrade in more than ten years in the past represented China Telecom always accurately grasps the prevailing development trends as every transformation and upgrade resulted in remarkable achievements. This also demonstrated that forward-looking strategic planning and trend-leading role are both vital to overall corporate development.

At present, we are about to enter into an advanced stage of information civilisation of mankind, the era of intellectual service. The Company officially established a comprehensive transformation and upgrades plan (Transformation 3.0) at the end of June 2016 and positioned itself as a leading integrated intelligent information services operator. Intelligent information services built on digitalisation and networkisation as fundamentals; widely used intellectualisation technologies such as cloud computing, Big Data, Mobile Internet, IoT, artificial intelligence as main drivers; in-depth integration between cloud and network including Software-Defined Networking (SDN), Network Functions Virtualisation (NFV), hardware generalisation and platform-based capabilities development as the priority; deepened exploration and value realisation of corporate internal and external data resources as the norm; and diversified intelligent terminals as the carrier, altogether enables the Company to accomplish crossover development in different areas.

The Company will focus and link through the main theme of intelligence and will promote the reconstitution of network, business, operations and management based on the three main directions namely network intelligentisation, service ecologicalisation and operation intellectualisation. Integrated intelligent information services featuring connection on demand, automatic response, realistic virtual experience and high price-to-performance ratio will be provided to customers. **Network intelligentisation:** Being guided by CTNet2025⁹, the Company will promote network reconstitution, deepen open-source technology applications to accomplish the open integration of network and IT, moving forward towards the

combination of development and operations as a whole. The Company will be able to provide customers with state-of-the-art network experience with embedded visible, self-selective and self-served characteristics.

Service ecologicalisation: The Company will further emphasise the key operating focus, “2+5”. Through open cooperation, integrated innovation and promotion of business reconstitution, the Company will endeavour to build up the five key business ecosystems, namely Intelligent Connection, Smart Family, Internet Finance, new style ICT applications, and IoT in order to achieve co-existence, co-innovation and “win-win” outcomes.

Operation intellectualisation: Being driven by Big Data applications, through enhancement of six key capabilities in network fundamentals, network operations, data operation, channel sales, customer service and talent development in order to promote the reconstitution of operations and management to support smart operations.

Recently, the Company has commenced the implementation of Transformation 3.0. With the completion of the top-level design on network reconstitution, the Company published the CTNet2025 white paper and launched the first series of network reconstitution projects encompassing various areas such as network framework, fundamental scientific R&D, network engineering and product development. Surrounding the prevailing “2+5” operating focuses, ecological alliances in the industry comprising “Smart Family”, IoT and Big Data, etc. have been gradually formed. The Company launched the system and evaluation performance index of “Smart Family”. With “BestPay” payment system as the core, the Company accelerated the development of emerging areas including consumer finance and proactively nurtured the industry ecosystem. Through an in-depth exploration and extensive applications coverage of Big Data, the Company will pragmatically promote operation intellectualisation through precision marketing, precision management, dedicated services and lean operations.

As an excellent corporate citizen

We are committed to maintaining a high level of corporate governance, attaching great importance to risk management and control. We strive to enhance corporate transparency and value to ensure our healthy

⁹ CTNet2025 refers to China Telecom's CTNet2025 Network Structure White Paper.

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and orderly growth. Our persistent efforts in corporate governance have been widely recognised by the capital markets. We have been accredited with a number of awards and recognition for the year to date, including being voted as the "Most Honoured Companies in Asia" by *Institutional Investor* for six consecutive years. The Company was also awarded the Platinum Award – "Best Telecommunications Company in Asia" by *FinanceAsia* which honoured institutions and corporations in Asia consistently providing quality, excellent and innovative services to their customers over the past 20 years.

We persisted in operating with integrity and proactively fulfilled our corporate social responsibility while maintaining a fair and orderly environment for market competition and facilitating the healthy development of the entire value chain. Meanwhile, we actively promoted green operations, through further strengthening energy conservation and emissions reduction to improve the efficiency of resource utilisation. We vigorously promoted broadband penetration in rural areas in order to bridge the information gap between urban and rural areas. We received high recognition and appreciation from society through our efforts in combating catastrophic flooding in Southern China.

Endeavour to become bigger, better and stronger

Currently, the implementation of the national strategy of "Cyberpower" coupled with the promotion of supply-side structural reform will foster an advanced level equilibrium of supply and demand. This positive policy environment creates favourable conditions for the sustainable and healthy development of the industry. The Company will seize new development opportunities for transformation and upgrades.

In the second half of the year, the Company will proactively respond to the increasingly intensified market competition and changes in external environment. Oriented by market share dominance, the Company will expedite the scale development of two fundamental businesses, effectively collaborate on the operations of five major emerging areas while also endeavouring to enhance the six key capabilities in order to accelerate the transformation of our resource edges and capabilities into competitive strengths.

With reform and innovation as the driving force, the Company will promote the development strategy with talent development as the priority, optimise the market-oriented incentive mechanism, bolster vitality and improve efficiency in order to lay down a solid foundation for accelerated transformation and upgrades. At the same time, the Company will comprehensively promote reconstitution of four major areas including business, network, operations and management in order to accelerate the implementation of the new strategy on transformation and upgrades. The Company will strive to become a leading integrated intelligent information services operator, facilitate development towards the national strategy of "Cyberpower" and also serve society and the general public as a whole, while continuously creating new value 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. I would also like to express my sincere thanks to all our employees for their hard work and contributions. Furthermore, I would like to extend my sincere gratitude towards Mr. Zhang Jiping and Mr. Zhu Wei for their excellent contributions during their tenure of office as the Directors of the Company.



Yang Jie
Chairman and Chief Executive Officer
Beijing, China

23 August 2016