



Dear Shareholders,

It gives me great pleasure to present my first report to you. Appreciating the trust and the great responsibilities you and my fellow Directors have vested in me, since my appointment as the Chairman and Chief Executive Officer of the Company last year, I have undertaken extensive investigation and examination of the subsidiaries of the Company, communicated and exchanged opinions with the management, employees, customers, business partners of the Company and relevant regulatory authorities. I have gained a better understanding of the operations, corporate management, business strategy, corporate culture and other aspects of the Company. I have full confidence in the Company's fundamentals and its future development.

China Telecom is a long-standing and leading operator in the wireline telecommunications service sector. With a substantial and solid subscriber base, a well recognised brand name, a high quality telecommunications network, a strong management foundation, an outstanding management team and a group of high-calibre employees, the Company has been operating efficiently and performing well.

Our financial performance in 2004 was favourable. We recorded continuous growth in revenue and were successful in managing our operating costs and capital expenditure. The Company's operating revenue reached RMB161,212 million, an increase of 6.4% from last year, of which RMB8,458 million was generated from the amortisation of upfront connection fees. Excluding the upfront connection fees, our operating revenue was RMB152,754 million, an increase of 7.7% from last year. Our EBITDA* was RMB78,542 million, an increase of 12.7% from last year. Our EBITDA margin* was at a relatively high level of 51.4%. Our net profit* (after deduction of deficit on revaluation of property, plant and equipment of RMB1,262 million) was RMB19,565 million. Our earnings per share* reached RMB0.25.

The Company's strong operating cash flow provides funding for the necessary investment in relation to our long-term development, and it also ensures our shareholders receive a favourable cash return. Taking into consideration of the Company's operational and financial

conditions and capital expenditure required for our future business expansion, in particular, the investment necessary for our future strategic transformation, the Board of Directors will propose to declare a dividend in the amount equivalent to HK\$0.065 per share in the upcoming Annual General Meeting, so that we can retain sufficient financial flexibility, with a view to achieving the best return to our shareholders.

Our businesses grew steadily in 2004. Our local telephone subscriber base increased by 25.66 million, to 187 million, of which 42.17 million was made up of local wireless access subscribers, with an increase of 16.60 million. Such growth made an important contribution to the increase in the usage volume and our operating revenue. Long distance services developed better than previous years, recording a revenue growth of 2.1%. Revenue generated from Internet services sustained rapid growth and accounted for 9.2% of our operating revenue (excluding the revenue from amortisation of upfront connection fees), an increase of 2.2 percentage points over 2003. This increase in revenue generated from Internet Services contributed to the increase in operating revenue (excluding the revenue from amortisation of upfront connection fees) of 2.9 percentage points. Broadband subscribers increased by 6.61 million to 13.84 million. Value-added services continued to grow steadily and showed a strong potential for further growth. At the same time, the contribution of non-voice services to revenue growth was increasing.

* After incorporating the revenue from the amortisation of upfront connection fees, EBITDA was RMB87,000 million, EBITDA margin was 54.0%, net profit was RMB28,023 million, earnings per share was RMB0.36.

Our Company has always attached great importance to corporate governance and business integrity to ensure its sustainable development. We shall continue to improve our corporate governance and increase the transparency of the Company in accordance with the requirements of relevant regulatory authorities (in particular the requirements promulgated under the United States *Sarbanes-Oxley Act* of 2002) and generally accepted international best practice. We shall continue our efforts in promoting and improving our operational and information disclosure internal control systems. The Board of Directors has already approved the optimisation of the Company's internal controls in accordance with COSO framework, and the establishment of an integrated multi-level internal and external assessment system with a view to further improving operational efficiency and information quality and to better managing financial risks to preserve shareholders' interests.

While the Company performed well in general, it faced a number of challenges: the growth in the wireline telephone subscriber base has slowed down; the wireline telecommunications services has witnessed substantial substitution by the mobile services; revenue growth rate has been declining. As a result of the intense competition, marketing costs increased continuously, putting pressure on growth of profits. Due to the lack of new prominent growth-driving products, the disadvantages of providing only wireline telecommunications services became increasingly apparent. The Company's network resources have yet to be fully exploited.

We see valuable growth opportunities in the future. China's GDP per capita has exceeded a momentous US\$1,000. Benefiting from the positive effect of macro economic measures of China and improving living standards of the Chinese people, demand in the telecommunications market is continuously expanding. With the growing popularity of information technology, customers' demands for one-stop overall solutions for integrated services and information provision are increasing.

In general, China Telecom Corporation Limited faces both opportunities and challenges, with opportunities outweighing challenges. As the wireline telecommunications business enters into a maturing phase worldwide, we have realised the risks inherent in operating only wireline telecommunications business. Following a comprehensive review of the history, current situation and prospects of the telecommunications industry as well as the development direction of the Company, we have decided that, from 2005, our strategy will be to transform China Telecom from a traditional network operator into a modern integrated information services provider.

We shall continue to pursue the operation of mobile business proactively so as to realise potential synergies by operating both mobile and wireline businesses. Simultaneously, we shall actively promote the establishment of orderly competition through co-opetition. Based on a win-win business model, we shall actively explore the development of IP-based multimedia services by leveraging our telecommunications network resources. We shall strengthen co-operation with content

providers with a view to extending the value chain. We shall seek to work with IT service providers to provide differentiated total solutions for our enterprise customers. In addition, the Company will fully exploit the development potential of rural telephony, value-added services, leased line and other services with a view to creating new revenue growth drivers. The Company will also strive to transform our networks into intelligent, broadband and IP based networks, and to enhance the development and convergence of multi-terminals and multi-businesses. In addition, we shall leverage tariff packaging to deliver integrated information services and to ensure the Company's sustainable development.

To ensure our successful business transformation, we shall implement precision management at all levels of the Company, so that quantitative standards will be adopted with reduced data deviations in all aspects of management on an integrated basis covering marketing activities, network operations, allocation of financial resources and human resources.

As a telecommunications operator conscious of its social responsibilities, the Company has launched the "Green Internet" project to clean up Internet content to protect the well being of youngsters. The Company has also made great efforts to promote the establishment of the "Green Dynamic" Internet cafe chain for the purpose of creating a good and healthy Internet access environment for the public. In addition, the Company has taken active measures to provide humanitarian aid to tsunami victims in the Indian Ocean region and other

regions, to subsidise children who are unable to attend school owing to financial difficulties, and to help underprivileged people in society.

We are confident in our future. By leveraging our strategic transformation and competitive edge, and seizing the opportunities brought by China's economic growth and new technology, we shall endeavour to provide our customers with modern integrated information services of high quality, and provide an even better return to our shareholders.

Finally, on behalf of the Board of Directors of the Company, I would express our gratitude to Mr. Zhou Deqiang and Mr. Chang Xiaobin for their significant contribution to China Telecom Corporation Limited during their time with us, and at the same time welcome Mr. Leng Rongquan, Mr. Yang Jie, Mr. Sun Kangmin and Mr. Li Jinming to join the Board of Directors of the Company. I also would like to take this opportunity to express my sincere appreciation to all of our shareholders, directors, members of the Supervisory Committee, employees and customers.



Wang Xiaochu
Chairman and Chief Executive Officer

Beijing, PRC
31 March 2005



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