

Chairman's Statement



Dear Shareholders,

Early this year, a snowstorm with its scale and duration unprecedented in the last century occurred in China. The snowstorm caused grave disturbances to people's daily lives, as well as serious challenges to our telecommunications services. During the Lunar New Year, in places where the snowstorm was most severe, I myself witnessed many of our people volunteered to sacrifice their precious family gathering opportunities to make emergency repairs on the telecommunications facilities fearlessly under the harsh weather conditions. In some circumstances, in order to ensure smooth communications, they even insisted on staying on duty under no power and water supply which lasted for several days. Their courage and strong team efforts well demonstrated the "unwavering dedications" spirits of our China Telecom people – "Exceptional strength, exceptional endurance and exceptional devotion". Their actions had written a new chapter of "Customer First, Service Foremost". I am deeply impressed with the vibrancy of the Company despite its long establishment over a century. As we further drive our strategic transformation and progress our way to the upcoming full services offering, I firmly believe the Company will have a thriving future.

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Looking back at the corporate development in the past three years, we are grateful to see the encouraging results achieved by our persistent efforts in strategic transformation and innovation. Strategic transformation has accelerated our corporate development and placed us at the forefront of the telecommunications industry. Strategic transformation also injected new energy into the Company's development. We have established a customer-oriented brand management system and strengthened our capabilities in integrated information application services. With further optimized business structure and enhanced financial capabilities, we have reinforced our ability to increase our shareholders' value.

2007 FINANCIAL RESULTS

In 2007, the Company grasped the opportunities brought by informatisation. We tackled various challenges to promote the scale development of transformation business, which helped to sustain overall revenue growth. We also took initiatives to alleviate the decline in our traditional voice business. As a result, we maintained solid fundamentals and achieved favorable financial results in the

highly competitive market. Operating revenues reached RMB178,656 million, in which the amortisation of upfront connection fees was RMB3,294 million. Excluding the upfront connection fees, operating revenues were RMB175,362 million, a 2.8% increase from 2006. EBITDA¹ was RMB85,974 million, a 1.3% increase from 2006. EBITDA margin¹ was 49.0%, broadly at the same level as 2006. Profit attributable to equity holders of the Company² (excluding the effect of the related assets revaluation, which was carried out at least once every three years) was RMB22,517 million, an increase of 1.1% from 2006. Capital expenditure decreased by 7.2% from 2006 to RMB45,558 million. Free cash flow³ reached RMB33,964 million, a 17.2% increase from 2006.

Taking into consideration of our shareholders' return and the Company's capital requirements for future development, especially the preparation of our full services offering, the Board of Directors will recommend at the forthcoming Annual General Meeting that the dividend be an equivalent of HK\$0.085 per share, same as last year.

¹ Including the amortisation of the upfront connection fees, EBITDA was RMB89,268 million, EBITDA margin was 50.0%.

² According to the Company's accounting policy, in 2007, the Company carried out a revaluation on property, plant and equipment (which was carried out at least once every three years). The surplus on revaluation of RMB4,809 million was shown in the consolidated statement of changes in equity. The deficit on revaluation of RMB2,755 million was recognized in the consolidated income statement. Profit attributable to equity holders of the Company, including amortisation of the upfront connection fees, deficit on revaluation and respective income tax effect, was RMB23,702 million.

³ Free cash flow is calculated from EBITDA (excluding amortisation of the upfront connection fees) minus capital expenditure and income tax.

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BRAND ORIENTED AND INNOVATIVE OPERATIONS

In 2007, brand operation was the main theme of the Company. We continued to put enormous efforts in developing our two major customer brands- "BizNavigator" and "One Home", targeted at government and enterprise customers and mid-to-high-end household customers respectively. Upon converging various businesses and products according to customers' demands, values and core competitiveness of the customer brands were enhanced. Contract subscribers to "BizNavigator" and "One Home" reached 1.884 million and 10.536 million respectively in 2007. Informatisation services were the focus of our business transformation. Broadband services, value-added services and integrated information services achieved significant breakthrough. Non-voice business revenue represented 36.5% of the Company's overall operating revenues, an increase of 7.4 percentage points from 2006. Due to intensifying mobile substitution, the Company experienced negative growth in access lines in service for the first time. Voice business revenue decreased by 7.9% from 2006. Facing new challenges in our traditional voice business, we will consolidate its performance by further enriching the applications on informatisation and improving service packages.

To facilitate brand operation, we continuously optimized our organizational structure and promoted management innovation. We incorporated a subsidiary specializing in "Best Tone" services to rapidly strengthen our vertically-integrated operation in the information media areas. We adjusted the operational structure of our system integration business that strengthened our capabilities to provide better professional solutions and services to our government and enterprise customers, as well as other business customer groups. Our staff force was optimized by recruiting more professional personnel to IP, IT and information services operations. We also perfected our incentive schemes, focusing especially on the promotion of strategic transformation and value enhancement and stimulating the activeness and creativity of our staff in transformation business.

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We endeavor to improve our operation support system and our brand recognition. The full deployment of CRM system strengthened our customer relations management. The launch of integrated multi-service billing system provided effective means for targeted precision marketing. Meanwhile, we further pushed forward the establishment of customer-oriented network maintenance system to closely link up front-line operations and back-end support. As a result, we progressively enhanced our capabilities of providing diversified services to customers.

We proactively implemented financial precision management to enhance shareholders' return. The Company continued its strict control over capital expenditure. The ratio of capital expenditure to operating revenues was further lowered by 2.8 percentage points from 2006. Resources allocation was further optimized with strict control over investments in our traditional fixed-line voice business, while ensuring the investment needs of transformation business such as broadband services, value-added services and integrated information services. Our operating efficiency was raised through optimizing capital, cost and asset structures, strengthening cost management and capital budgeting and optimizing asset resources.

We expanded our services into rural and overseas markets. The Company increased its efforts to promote broadband access services in relatively affluent rural areas so as to meet their demand for informatisation. We are delighted to achieve growths in both revenue and subscribers in rural markets. In respect of overseas markets, we successfully acquired from our parent company its subsidiaries in Hong Kong and America to benefit from the rapid growth of these two overseas markets and also enhance our capabilities of providing global one-stop shopping services for multinational customers.

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CORPORATE GOVERNANCE

In order to enhance operating efficiency and investor confidence, we are firmly committed to adopting international best practices to improve corporate governance and transparency continuously. The Company greatly emphasizes the importance of internal control and risk management. In terms of meeting regulatory requirements, we further improved our internal control and assessment systems, and progressively integrated the comprehensive risk management mechanisms into our daily operations. Thus the interests of our shareholders are safeguarded. Our continuous efforts in corporate governance were widely recognized by the capital market. We have been accredited with a number of awards, including "World's Most Admired Companies" for the year 2007 by *Fortune* and "Asia's Best Managed Fixed Telecom Company" in 2007 by *Euromoney*.

CORPORATE SOCIAL RESPONSIBILITY

We operate with integrity and offer credible services to customers. In facilitating healthy development in telecommunications industry, we endeavor to protect fair and orderly market competition, and advocate multiple-wins cooperation for all participants in the value chain. Aside from the sustainable growth of our own, we devote to contribute to the country's economic development, environmental protection and construction of a harmonious society, and to create a favorable environment for the success of our upcoming full services offering.

OUTLOOK FOR 2008

In 2008, strategic transformation of the Company will enter into a new phase. For this purpose, we have advocated the strategy of "Customer-focused Innovative Informatisation", which will accelerate our transformation into a leading integrated information services provider. We will make greater efforts in management reform and innovation, and consolidate provincial subsidiaries into branches to strengthen integration of operational management systems. We will also restructure our front-line departments, which will enable us to implement better customer group management and sales. We will allocate more resources to core customer groups and strengthen our customer-oriented operation systems to raise our brand recognition.

Looking ahead, we are fully confident. Although the intensifying market competition is a serious challenge to us, the upcoming full services offering will bring enormous business opportunities. We will keep abreast of the trend of global telecommunications industry as we implement the convergence of multi-communication means and multi-products in a broader perspective. We will also strengthen our execution capabilities in providing integrated information services to customers, and thus to continually create new values for our shareholders.

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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 thank Madam Huang Wenlin for her brilliant contributions during her term as Executive Director of our Company and welcome Mr. Zhang Chenshuang to join our management team.



Wang Xiaochu

Chairman and Chief Executive Officer

Beijing, China
31 March 2008