

Chairman's Statement



In the first half of 2012, we firmly seized the accelerating trend of social informatisation and leveraged on the valuable opportunities of proliferating mobile Internet to unwaveringly implement our development strategy of dual leadership in innovation and services. We comprehensively promoted the scale development of our three core services, mobile, broadband and informatisation applications, took thorough steps to enhance our management and focused to optimise corporate operation mechanisms. While strengthening the centralised efficient operation capabilities, the Company persistently accelerated its steps in strategic transformation and scale development to steadily enhance corporate long term competitiveness and corporate value.

Operating results

In the first half of 2012, the Company achieved record revenue growth. The operating revenues amounted to RMB138,021 million, representing an increase of 14.8% over the same period last year. Excluding the mobile terminals sales, the operating revenues were RMB126,580 million, representing an increase of 11.2% over the same period last year. The growth rate in operating revenues surpassed the industry average. With the continued optimisation of the business structure, the proportion of revenues from the growth businesses increased to 83.9%. The risk of traditional business was further alleviated with wireline voice revenue as a proportion to total revenues

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decreased to 16.1%. EBITDA¹ was RMB48,760 million, representing an increase of 0.3% over the same period last year while EBITDA margin² was 38.5%. The profit attributable to equity holders of the Company was RMB8,814 million, decreasing by 8.3% from the same period last year. The Company believes that the launch of the iPhone to expand the high-end market would require an appropriate increase in marketing initiatives which would create short-term pressure on profitability, however, it would enhance long-term sustainable growth and value creation for the Company. Basic earnings per share of the Company was RMB0.11. Capital expenditure was RMB25,647 million, accounted for 18.6% of the total revenues, while free cash flow³ reached RMB8,548 million.

Taking into consideration the cash flow of the Company and the capital required for the forthcoming acquisition of mobile network assets from its parent company, the Board of Directors has decided not to pay any interim dividend this year in order to maintain adequate funding flexibility. The Board of Directors will proactively consider the final dividend proposal when reviewing the full year results and will propose to the shareholders' general meeting accordingly.

Accelerated development achieving scale breakthrough

3G traction driving rapid mobile expansion

With the increasing proliferation of mobile Internet applications and 3G smart terminals, users' habit on 3G services has progressively been cultivated. The accelerated migration trend from 2G to 3G in China's mobile communications market is becoming more noticeable. In view of such a momentous development opportunity, we proactively allocated resources and adopted effective measures to achieve scale breakthrough in mobile services. In the first half of the year, mobile service revenue showed a strong and industry leading growth momentum with an increase of 36.7% over the same period last year, reaching RMB42,556 million. The net addition of mobile subscribers was 17.71 million, reaching a

total number of 144 million. The mobile subscriber market share increased to 13.8%, of which the net addition of 3G subscribers was 14.67 million, reaching a total number of 50.96 million. Significantly driven by our product center applications, our Best Tone service and Best Pay service, 3G handset data traffic increased rapidly with average monthly data usage per user reaching 111MB. The competitive advantages of Company's mobile services become more noticeable and sustainable growth momentum of mobile services is irresistible.

In the first half of the year, by adhering to our development philosophy of "terminal driven, brand focused and channel oriented", we adopted an innovative development model to effectively promote the scale expansion of mobile service, in particular selling 3G as a single product. We persisted in a 3G smartphone-driven strategy and strengthened the cooperation with vendors to enrich offerings of large-screen smartphones priced around RMB1,000. At the same time, we timely launched iPhone to cater the demand for the mid-to-high end markets and further promoted the breakthrough into the high-end market. We continued to carry out the transformation of sales outlets into specialty stores to strengthen the experience marketing of Internet handsets. Through service demonstrations and customer assistance on applications, users' habit on 3G services was cultivated and hence data traffic was stimulated, which had effectively increased data traffic per 3G handset user. We continued to reinforce the brand promotion of "e-Surfing 3G Internet handset" which focused on key customer groups, such as office staff and trendy youngster. We emphasised on enriching contents, highlighted and promoted the differentiation of high-end brand image. Led by our brand "Young", we proactively expanded in the campus market. We further strengthened our open sales channels for wider coverage in the core business districts. By introducing the private enterprise operating mechanism in our self-operated sales outlets, we effectively improved the outlet sales capability. We perfected our electronic sales channel and implemented centralised efficient operation while driving the transformation of online sales outlets from service-oriented websites to sales-oriented e-commerce websites.

¹ For convenience of investors' comparative analysis, EBITDA is calculated before CDMA network capacity lease fee.

² EBITDA margin is calculated based on EBITDA divided by the operating revenues excluding mobile terminals sales.

³ Free cash flow is calculated from EBITDA minus CDMA network capacity lease fee, capital expenditure and income tax.

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Broadband upgrade boosting scale development

In the first half of the year, we seized the opportunities arising from broadband development as a national strategy. We accelerated the penetration of “fibre broadband” to build a superior network with good customer perception. We proactively enriched the content applications, further extracted broadband development potential and strengthened our broadband's leading position in the market. In the first half of the year, wireline broadband revenue was RMB33,369 million, representing an increase of 12.1% over the same period last year. The net addition of broadband subscribers was 6.89 million and the total number of broadband subscribers reached 83.70 million, maintaining our leading position in subscriber market share.

We continuously adhered to the overall development strategy of “bandwidth upgrade, content enrichment and brand building”. With proactive promotion in “Broadband China • Fibre Cities” project, we accelerated the fibre roll-out in key areas. FTTH covered approximately 40 million households, which manifested the superior quality of China Telecom's fibre broadband network. We further strengthened the marketing promotion of “Lightening Fibre Residential Areas” to speed up the bandwidth upgrade of the mainstream customers and transform the network strengths into competitive edges. Broadband customers with 4Mbps bandwidth and above accounted for more than 60% of the total. Concurrent with bandwidth upgrade, we proactively developed high-bandwidth Internet applications, such as online media, video chatting and interactive games, to boost high-bandwidth demand and inject new impetus for the high growth broadband market.

Focusing on key industries to expedite informatisation applications

Facing the rich gold mine of informatisation applications market, we fully leveraged our integrated strengths to satisfy the core demand of customers. Driven by the promotion of “Smart Cities” development, we focused on three key field areas, namely smart government, smart living and smart industry. We emphasised to develop key industries applications,

such as e-Surfing RFID, e-administration, transport and logistics, digital campus and busy-shop assistant, and accelerated the scale replication and promotion of matured products. Meanwhile, we organically integrated our fundamental services, such as mobile, broadband etc., into industry applications, to effectively drive the scale development of our core services. We proactively expanded the cloud service market and established a cloud computing company to operate the full network cloud service in a centralised efficient manner. The launch of basic products, such as cloud central processing, cloud storage etc., were completed. We vigorously promoted and developed cloud computing in industry applications to continuously enhance our capabilities in providing industry informatisation solutions. In the first half of the year, revenue from wireline value-added services and integrated information services reached RMB16,343 million, an increase of 7.4% over the same period of last year.

Alleviating operational risk of wireless voice

We adopted effective measures to consolidate wireline usage and strived to mitigate the decline of wireline voice service. The operating risk was gradually alleviated. As at the end of June, the total number of access lines in service was 167 million, a net decline of 2.1 million in the first half of the year. Wireline voice revenue in the first half of the year amounted to RMB22,241 million.

Innovative development mode promoting management enhancement

“Three New Roles” transformation achieving substantive progress

In the first half of the year, we pragmatically promoted the development of our Three New Roles — “a leader of intelligent pipeline, a provider of integrated platforms, and a participant in content and application development” to lay a solid foundation for the sustainable growth of the Company. We speeded up the commercialization of an intelligent pipeline by



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implementing self-served bandwidth upgrades for wireline broadband services in certain provinces and cities and accelerating the promotion of intelligent network trials and upgrades for mobile network based on service identification and traffic management. We proactively promoted the construction of an integrated platform to promptly realize the resource integration and open operation in order to enhance the rapid product deployment capability. We continued to expand the creativity in developing content and application-type products with fast growing subscriber scale of our product centre services and increasing activity level. e-Surfing open platform has gathered nearly 400 co-operative application developers. The scale of content applications development emerged.

Invigoration through mechanism innovation

Following the development pattern of Internet businesses, we proactively promoted innovation in mechanisms and systems and devoted to establish a new system appropriate for emerging businesses. We introduced private capital into the e-Surfing Media Company to deepen its market operation, invigorate its development potential and build a specialised enterprise with market competitiveness. We set up a product incubator centre, cooperated with venture capital firms, activated the system, stimulated the passion of entrepreneurship of our employees and cultivated new growth drivers. By fully utilizing social resources, we focused on the open co-operation with Internet application dominant enterprises and system developers of key industry applications and proactively explored new modes of co-operation to develop the informatisation application market together. We consolidated overseas operation units and established China Telecom Global Limited, which would unify customer interface and operate in a centralized efficient manner with global resource allocation and coordinate the development of overseas market.

Leveraging data traffic operation to enhance quality of development

While expanding our subscriber scale, we expedited our transformation from traditional voice operation to data traffic operation to enhance quality of development. We endeavoured to develop a new system of mobile Internet products and grasped the

first customer contact point with "e-Surfing Cloud Desktop". We continued to expand the subscriber scale of product centre services to invigorate data traffic demand. We promoted the coordinated development of various channels, implemented precision sales of data traffic and increased customer activity level to drive data usage per subscriber. We also speed up the development of services such as Best Tone and Best Pay service to promote data traffic aggregation. In the first half of the year, mobile data revenue was RMB19,267 million, representing an increase of 46.7% over the same period last year. Mobile data revenue accounted for 45.3% of the mobile service revenue, which is at an industry-leading level.

Enhancing centralised efficient capability and deepening precision management

To adapt to the development pattern of mobile Internet, we strengthened the coordination and centralised efficient operation of our sales and marketing systems, IT support and supplies procurement. We strived to achieve the goal of "one-point access and entire-network operation" to maximize the operating efficiency of the entire network. We reinforced the coordination and planning together with centralized efficient management in five areas, namely brand promotion, product optimisation, tariff standardisation, terminal management and services enhancement, to expand the market. In addition, through refining IT system and structure, we offered greater support to our centralised efficient operation. We strengthened the degree of centralised procurement, effectively enhancing investment cost savings per unit. Focusing on key areas, like sales and marketing and network construction, we continued to deepen implementation of the sub-division performance evaluation units to increase the efficiency of sales and marketing cost as well as network investment.

Acquisition of Mobile network for corporate value enhancement

This year, we would complete the acquisition of the CDMA network assets from our parent company pursuant to statutory procedures and integrate mobile



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assets and business altogether. The acquisition of CDMA network assets will be beneficial to strengthening the overall operation efficiency of the Company's mobile service and improving profitability in the future. It will also enhance the Company's ability to coordinate the mobile network investment and construction with its operation management and upgrade planning, appropriately grasping the opportunity of advancement to new technologies with a view to fostering the development of the mobile service.

Corporate Governance and Social Responsibility

We continue to strive to maintain a high level of corporate governance and corporate transparency to ensure the healthy development of the Company and enhance corporate value. Our persistent efforts in corporate governance have been widely recognised by the capital markets. We were accredited with a number of awards and appreciation in the first half of the year, including the "Overall Best Managed Company in Asia" by *FinanceAsia* for two consecutive years, "No. 1 Best Managed Company in Asia" by *Euromoney*, being the first company receiving such honour for three consecutive years, and also "The Best of Asia" by *Corporate Governance Asia* for three consecutive years.

We persist in operating with integrity and strive to maintain fair and well disciplined market competition. We promote collaboration with value chain partners with the aim to achieve a win-win scenario among all parties to foster the healthy development of the whole industry. We proactively participated in relief activities for the natural disasters such as the earthquake in Xinjiang and mudslides in Sichuan. We also provided telecommunications assurance services for the launching of Shenzhou-9 spacecraft and Shanghai Cooperation Organisation Summit, receiving high regards and appreciation from the society.

Outlook

At present, in respect of the changes of China's mobile telecommunications market, the trend of migration from 2G to 3G services has emerged. Approximately 900 million 2G service users nationwide are potential

3G service users of the Company. The development of broadband service still has great prospects while the demand for social informatisation is ever increasing. However, we are also facing new challenges brought by intensifying market competition and cannibalisation of traditional businesses by advanced technologies.

Aiming to achieve a breakthrough of its full services development, we will grasp the opportunities and cope with the challenges. In the second half of the year, the Company will adhere to its strategy of advancing its dual leadership in innovation and service quality. The Company will exert efforts in accelerating the scale development of its three core services, including 3G service, broadband service and informatisation applications, to increase revenue market shares of its full services. Furthermore, we will endeavour to enhance our management to strengthen four major capabilities, including innovation, services, efficient centralisation and operation. The Company will also consolidate its differentiated competitive edges of its products, services, networks and terminals to enhance both customer value and corporate value.

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 Mr. Zhang Chenshuang, Mr. Li Jinming, Mr. Miao Jianhua, Mr. Xu Cailiao and Madam Han Fang for their valuable contribution during their tenure of office as Directors and Supervisors of the Company. Also, I would like to welcome Mr. Ke Ruiwen to join our Board of Directors.



Wang Xiaochu

Chairman and Chief Executive Officer
Beijing, China

22 August 2012

