

PRESIDENT'S STATEMENT

In 2017, the Group kept transforming growth momentum, insisting on both domestic non-telecom operators and domestic telecommunications operators-driven as well as CAPEX and OPEX-driven, realizing complementary advantages of its smart products and integrated service and integrating finance with industrial development and expanding ecosystem in terms of deployment, which secured sound operating results and laid a solid foundation to forge the Group into a top-tier enterprise and open a new chapter in innovation and development.

Si Furong
President



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Dear Shareholders,

I am very pleased to present the operating results of the Group in 2017.

FINANCIAL PERFORMANCE

In 2017, while adhering to the principal philosophy of “value-driven, seeking steady yet progressive growth and efficient development”, the Group vigorously developed the domestic non-telecom operator market and the OPEX market of the domestic telecommunications operators in order to reduce the reliance on the network investment of domestic telecommunications operators, and thereby optimized its business and customer structure, enhanced its overall efficiency, and achieved satisfactory operating results. Total revenues for the year amounted to RMB94,572 million, representing a year-on-year increase of 6.9%. The Group's overall gross profit margin for the year was 12.9%, representing a year-on-year decrease of 0.3 percentage point. The decline rate obviously moderated as compared with the same period of last year⁶. The selling, general and administrative expenses for the year accounted for 10.5% of the total revenues, representing a year-on-year decrease of 0.2 percentage point. Profit attributable to equity shareholders of the Company for the year amounted to RMB2,714 million, representing a year-on-year increase of 7.0%. The net profit margin was 2.9%, which remained the same as that of last year. In 2017, the Group's basic earnings per share was RMB0.392. As we constantly strengthened the management of our working capital and achieved solid results, our free cash flow amounted to RMB6,118 million, representing a year-on-year increase of 40.3%.

BUSINESS DEVELOPMENT

As clearly indicated, while the Group's revenue scale in recent years has been constantly expanding, the dependence of its operations on the network investment of domestic telecommunications operators has been gradually weakening and the contribution from the Core BPO services and domestic non-telecom operator customers to the overall incremental revenue of the Group has been significantly increased as compared to the same period of last year, which broadly indicated the realization of the transformation of growth momentum.

In 2017, while continuing to control the development of its products distribution business with low efficiency proactively, the Group vigorously developed its TIS services, Core BPO services and ACO services, and recorded favourable revenue growth from these services with our business structure further optimized.

Revenue from TIS services amounted to RMB50,511 million, representing a year-on-year increase of 10.1%, and accounting for 53.4% of the total revenues. We captured the important opportunities of the domestic telecommunications operators' network upgrade and the upgrade of fiber optic broadband networks as well as tower construction and the deployment of the IoT, and thereby reinforced our business from domestic telecommunications operators. Meanwhile, the Group continued to shift its products and capabilities to the domestic non-telecom operator customers market, resulting in the revenue of TIS services from this customer group growing at a significant year-on-year rate of 30.3%. The rapid growth of TIS services of the domestic non-telecom operator customers has greatly enhanced our ability to withstand the impact from the decline in the CAPEX of domestic telecommunications operators.

Revenue from BPO services amounted to RMB32,763 million, representing a year-on-year increase of 0.7% and accounting for 34.6% of the total revenues. The Group's insistence on value-driven principle and proactive control of its products distribution business with low efficiency were the main causes for the slow increase in the revenue from this segment, whereby revenue from products distribution business for the year reported a significant year-on-year decrease of 33.6%. Excluding this factor, revenue from its Core BPO services reported a rapid year-on-year increase of 17.0%, demonstrating the favourable results of the Group's transformation of its growth momentum. Revenue from the network maintenance business increased by 20.1% year-on-year, indicating a remarkable acceleration as compared with the same period of last year⁷, and revenue from supply chain service increased by 16.8% year-on-year, demonstrating the sound results of synergistic business operation.

⁶ For 2016, the Group's overall gross profit margin was 13.2%, representing a year-on-year decrease of 0.9 percentage point.

⁷ In 2016, the Group's revenue from network maintenance business reported a year-on-year increase of 9.5%.

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Revenue from ACO services amounted to RMB11,298 million, representing a year-on-year increase of 12.7%, accounting for 12.0% of the total revenues. We captured the business opportunities arising from the intelligentization transformation of domestic telecommunications operators as well as the flourishing demand of the domestic non-telecom operator customers for informatization construction and vigorously promoted our smart-typed products, thereby increasing the core competitiveness of this business segment. In 2017, the aggregate revenue from the Group's system integration, software development and system support businesses increased by 20.7% year-on-year, which is 6.8 percentage points higher than the "Revenue Growth Rate of National Software and Information Technology Service Industry"⁸, i.e. the industry average level.

CUSTOMER DEVELOPMENT

In 2017, the domestic non-telecom operator market was the fastest growing market of the Group and played an important role in propelling the overall sustainable development of the Group. The revenue from this market amounted to RMB26,656 million, representing a year-on-year increase of 12.4%, accounting for 28.2% of the total revenues of the Group. The revenue from the Core Businesses of this market increased by 26.5% year-on-year, accounting for 83.2% of its overall revenue, representing a year-on-year increase of 9.3 percentage points, which demonstrated the optimization of business structure. In the domestic non-telecom operator market, the Group focused on key areas such as government, electricity and transportation, reinforced its marketing team construction, enhanced the products enabling through training camps for industry-leaders and talented staff in domestic non-telecom operator market, broadened its external cooperation while constantly building up its product series, including Smart City, Smart Security, Smart Park, Smart Transportation, Smart Safety, Smart Town and Smart Grid, thereby progressing the cross-region promotion of its products and capabilities and boosting the Group's development. During the year, the Group continued to expand its businesses into the power sector effectively, where 49 business development units for the power sector have been established nationwide and 172 business licenses in the power sector have been obtained. The Group also achieved breakthroughs in the transportation sector with the official launch of our "Smart Highway" solution by means of holding a nationwide summit, and the summit has significantly enhanced the Group's influence in the industry and drove the development of the platform and related integrated businesses.

In 2017, for the domestic telecommunications operator market, the Group insisted on leveraging both the "CAPEX and OPEX-driven" businesses and "the priority of service quality", thus realised a revenue of RMB65,080 million, representing a year-on-year increase of 6.9% and accounting for 68.8% of the total revenues of the Group. Among that, the revenue from China Telecom amounted to RMB41,568 million, representing a year-on-year increase of 2.4% and accounting for 43.9% of the total revenues. The revenue from domestic telecommunications operators other than China Telecom reported a year-on-year increase of 15.9% and accounting for 24.9% of the total revenues, representing a year-on-year increase of 2.0 percentage points. Among that, the Group exploited the new characteristics of China Mobile's centralized procurement and emphasized on maintaining a positive cooperative relationship with China Tower, strived to expand new businesses and enhanced market share, thereby supported the rapid growth of the related businesses.

In 2017, affected by cyclical fluctuations of its overseas projects and the Group's proactive control of low efficiency businesses, revenue from overseas market recorded a year-on-year decrease of 26.2% and amounted to RMB2,836 million, accounting for 3.0% of the total revenues. We have strengthened our risk prevention measures in our overseas businesses, and actively adjusted our overseas business operation and management structure. At present, the new management structure for China Communications Services International Limited has been established, under which we have accelerated the building up of our marketing team, resulting in improved capabilities in marketing. Meanwhile, overseas market was divided into five major business regions geographically, which is managed dynamically in a more flattened manner for business development. An overseas technical support centre was also established to centralize the allocation of resources and provide support to the expansion of our overseas projects.

⁸ In 2017, the revenue of the software and IT service industry in China increased by 13.9%. Source: Ministry of Industry and Information Technology of the People's Republic of China.

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DEVELOPMENT DEPLOYMENT

The Group has constantly transformed its new growth momentum, mapped out new deployment and explored new rooms for expansion. In terms of market development, the Group's business focus has been shifted from the traditional CAPEX of domestic telecommunications operators to the OPEX of domestic telecommunications operators, domestic non-telecom operator customers and overseas customers. The Group has put greater efforts in product innovation to promote its branding in Smart Services of the Group, and shifted its capabilities from a traditional labour-intensive service to a technology-based and digital services. In terms of business model, we have striven to expand our external cooperation and build an ecosystem featuring win-win outcome while exploring business models such as PPP (Public-Private Partnership), BT (Building + Transfer) and BOT (Building + Operation + Transfer). In terms of new business segment, Comservice Capital Holding Company Limited was established to explore the integration of finance with industrial development.

The Group has accelerated the consolidation of its professional services and continued to push forward its integrated operations, embedding in the demand of product and service through our customers' full lifecycles, so as to get better and earlier preparation for future market demands in the era of 5G and IoT. Cross-province integration has been initiated for our distribution, facilities management and logistics businesses, in an attempt to promote the cross-region, cross-industry and cross-customer coverage of our traditional service capabilities and accelerate the convergence of upstream and downstream industries, with the brand influence of our “中通福” (ZhongTongFu), “中通服物業” (ZhongTongFu Wuye) and “中通服置業” (ZhongTongFu Zhiye) gradually emerged. We also accelerated the cross-profession collaboration such as capitalizing on design business to drive infrastructure business, so as to fulfilling the new demand for turnkey projects. For example, for the Qianbei Logistics Town project in Guizhou Province, the Group's Jiangsu Design Institute collaborated with our Zunyi Branch Company in Guizhou Province, and leveraged on the design business as entry point to drive multi-profession and cross-province cooperation, which helped build up our new capabilities in marketing. The synergistic management of resources was also strengthened to optimize the allocation of key resources and improve the efficiency of synergistic operations.

In terms of development of high-value business, the Company incubated a number of group-level products represented by Smart Highway and Smart Town with its innovation fund, which has enriched its product portfolio. We have noticed that, in view of the Group's unique integrated solution capabilities in the industry, the sound marketing efforts on our smart-typed products have also drastically promoted the development of our TIS services in which we have traditional strengths, and there was a noticeable effect on the ecological development of the Company. We closely monitored the development of frontier technologies, including entering into the quantum communications market in cooperation with CAS Quantum (國科量子), and cooperation with SAP in our public cloud business with a scale of hundred million renminbi. In addition, the Information Security Expert Committee and Big Data Expert Committee of the Group exerted positive impact in bringing talents together and supporting core product creation and key project development.

PROSPECTS

In 2018, the Group will adhere to the overall roadmap of “value-driven, seeking steady yet progressive growth and high-quality development” and generate greater value for shareholders and customers with higher quality development and better efficiency.

Facing the massive market space brought by the digital economy, the Group will focus on the needs of informatization from the government and industries along the vertical chain, unleash our “Consultant + Staff” expertise advantage, in which we act as the consultant for the government and enterprises to coordinate upstream and downstream parties along the value chain, establish new industrial benchmarks and formulate solutions, while playing the role as their staff and better serving the customers, with the view to fulfilling our role as the prime contractor in the new era of informatization and constantly broadening the business opportunities for domestic non-telecom operator customers. We will fully leverage our strengths to centralize product research and development, support the building of product lines covering smart-typed products, IoT and Information Security, strengthen the delivery capabilities of our product centre, accelerate the convergence of our products to the front end of the market to form new synergy, thus achieving a complete alignment of our internal products and delivery capabilities with external customers and market demands to deliver new services externally. At the same time, we will strengthen the external cooperation to introduce the products and delivery capabilities from our external partners and integrate them into the Group's system, with a view to cultivating smart-typed products for better satisfying customers' demand and gradually achieving breakthroughs in key areas and industries.

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The Group will continue to focus on both "CAPEX and OPEX-driven" businesses, and seize the opportunities in the transformation of domestic telecommunications operators. We will closely follow the needs of our operator customers along the national "Cyberpower" strategy and fully participate in the construction of 5G and IoT. While further penetrating the CAPEX-driven business to maintain the stable fundamentals of our operation, we will focus on the OPEX-driven business of our customers through further expansion of businesses in network integrated maintenance, Smart Home and IT operation and maintenance, in an attempt to establish a standardized service system for network maintenance, develop platform-oriented maintenance business and extend it to other customers.

The Group will strengthen the unified management of its overseas businesses and capitalize on its ICT core competence, accelerate its penetration into overseas electricity, education, healthcare and construction industries while maintaining the stability of its traditional telecommunications infrastructure businesses. The Group will strengthen its cooperation with domestic telecommunications operators and the "Go Abroad" Chinese enterprises, utilize the resources of all the relevant parties, and leverage its advantages in consultation planning, network construction and market deployment while continuing to follow up large-scale turnkey projects such as "China-Africa Partnership Program in Trans Africa Information Superhighway" Project and accelerating the transformation and upgrade of overseas businesses.

The Group will continue to deepen its reform and innovation, and further build up a production organization model that can better satisfy the demand of the market. In view of the new demand from IoT, the Group will promote professional integration, facilitate integration of finance with industrial development, explore its transition from product-oriented to platform-oriented operation model, in an attempt to create cross-profession, cross-region, internal-external collaboration capabilities. At the same time, we will accelerate the progress of our smart operations and optimise the unification of IT system so as to manage the operation in a more standardized manner and improve operational efficiency.

2018 marks the 40th anniversary of China's reform and opening up. We will adhere to our original aspiration and keep our mission firmly in mind. With the focus on the target of being a "leading provider of producer services in the informatization sector", we will expand our coverage to high-end services sector, forge the Group into a top-tier enterprise and open a new chapter in reform and development. We will be dedicated to our work with the spirit of "fully committed and waste no time", strive to start a new phase of high-quality development in a new era of the Company and make great strides toward a better future.



Si Furong
President

Beijing, PRC
27 March 2018