

Chairman's Statement

Dear Shareholders,

During the first half of 2015, following the national initiatives of comprehensively deepening reforms and securing stable economic growth through structural adjustment, the Group fully adopted the management philosophy of "innovation and transformation, seeking steady development, and pursuing efficient development". While persisting in the development of the "Two New Markets"¹, the Group properly allocated its resources and captured the rare opportunity in the development of domestic telecommunications operator market by leveraging its competence and competitiveness in providing integrated services, which resulted in a remarkable results in the complicated and ever-changing market. The growth of the total revenues accelerated, net profit resumed steady growth and free cash flow achieved a significant improvement compared to the previous year. Meanwhile, the Group insisted on deepening reforms, continuously promoted innovation in operational management and business model, and strengthened the impetus for subsequent development, which laid a solid foundation for its sustainable development.

Operating Results

During the first half of 2015, the Group fully captured business opportunities from domestic telecommunications operators, such as 4G network construction, speed enhancement of fiber optic broadband and maintenance and optimization of networks, and provided its customers with integrated services of "construction and maintenance", resulting in a significant improvement in operating results. The Group achieved total revenues of RMB37,563 million, representing a year-on-year increase of 11.3% and a remarkable growth in terms of growth rate². The cost of revenues was RMB32,387 million, representing a year-on-year increase of 12.0%. As a result of the decrease in service charges and increase in labour-related cost, the gross profit was RMB5,176 million, representing a year-on-year increase of 7.3%, while the gross profit margin was 13.8%, representing a year-on-year decrease of 0.5 percentage point. The Group strictly implemented cost control in selling, general and administrative expenses and such expenses was RMB3,930 million, accounting for 10.5% of the total revenues and representing a year-on-year decrease of 0.6 percentage point. Profit attributable to the equity shareholders of the Company was RMB1,271 million, resuming a steady growth with a growth rate of 2.7%. The net profit margin was 3.4% and the basic earnings per share amounted to RMB0.184. As a result of the ongoing enhancement of working capital management, turnover days of accounts and bills receivable were 140 days, reversing the growth trend and achieving a year-on-year decrease. Free cash flow³ amounted to RMB151 million, achieving a positive indicator value for a first half-year period for the first time since the listing of the Company.

1 Two New Markets refer to domestic non-operator market and overseas market.

2 In the first half of 2014, the total revenues of the Group were RMB33,743 million, representing a year-on-year increase of 4.3%.

3 Free cash flow = Profit for the year + Depreciation and amortisation – Changes in working capital – Capital expenditure

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Business Development

During the first half of 2015, the Group's operating results was characterized by the increase in both the capital expenditure and operating expenditure of domestic telecommunications operators. The issuance of the 4G (LTE FDD) license led to the continuous growth in fixed asset investment of domestic telecommunications industry⁴. The Group captured this opportunity and achieved revenue from telecommunications infrastructure services of RMB18,022 million, representing a year-on-year increase of 16.6%, with a significant increase in the growth rate as compared with the same period last year⁵ and accounting for 48.0% of the total revenues. Among that, the revenue generated from the domestic telecommunications operators⁶ grew even more rapidly with a growth rate of 25.6%. We focused on the opportunities brought by the increase in the operating expenditure of domestic telecommunications operators and helped our customers to enhance their network quality and responsiveness, and the Group's revenue from business process outsourcing services amounted to RMB16,050 million, representing a year-on-year increase of 7.6% and accounting for 42.7% of the total revenues, among which the revenue from management of infrastructure for information technology business ("Network Maintenance") achieved a year-on-year increase of 14.6%. The Group's revenue from applications, content and other services was RMB3,491 million, representing a year-on-year increase of 3.3% and accounting for 9.3% of the total revenues, and indicating that innovation and transformation achieved a preliminary result. We focused on the informatization demand of the government and industrial customers and strongly promoted high-valued products and services such as "Smart City", "Smart Security", "Smart Industrial Park" and "Smart Home". Meanwhile, the Group intensified efforts in expansion of "Success Factors", a human resources management solution, and "Gripay", an Internet mobile financial service platform, resulting in a greater breakthrough in the number of users.

4 In the first half of 2015, fixed asset investment in domestic telecommunications industry was RMB143.73 billion, representing a year-on-year increase of 5.6%. (Source: Ministry of Industry and Information Technology of the People's Republic of China)

5 In the first half of 2014, the Group's revenue of telecommunications infrastructure services was RMB15,453 million, representing a year-on-year increase of 0.7%.

6 The Tower Company (full name: China Tower Corporation Limited) was jointly established by the three domestic telecommunications operators in July 2014. Since 2015, the Group's revenue from the Tower Company is temporarily classified as revenue from the domestic telecommunications operator market.

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The Group has fully leveraged the development trend in the domestic telecommunications industry, and allocated resources and provided services according to the market demand. During the first half of 2015, revenue from the domestic telecommunications operator market was RMB23,802 million, representing a year-on-year increase of 15.9% and accounting for 63.4% of the total revenues. Among that, revenue from China Telecom was RMB15,850 million, representing a year-on-year increase of 25.4% and accounting for 42.2% of the total revenues. We seized the opportunity arising from the increase in the operating expenditure of the domestic telecommunications operators and the aggregate revenues from sources other than China Telecom⁷ was RMB7,952 million, representing a year-on-year steady increase of 0.6% and accounting for 21.2% of the total revenues. In accordance with the arrangements of preferential treatment and non-competition made with the Tower Company, the Group commenced to undertake business from the Tower Company and further reached consensus on cooperation during the first half of this year, making full preparation to serve the customers comprehensively.

During the first half of this year, the Group's revenue from the domestic non-operator market was RMB12,177 million, representing a year-on-year increase of 6.3% and accounting for 32.4% of the total revenues. The Group identified six major group-level products⁸, put in more marketing efforts and successfully realized cross-region promotion of its products. The Group focused more in expanding market coverage, resulting in an initial breakthrough in industries such as electricity and transportation. The Group strengthened cooperation with domestic telecommunications operators to jointly develop projects in the domestic non-operator market, with the revenue generated therefrom amounting to approximately RMB700 million. During the first half of 2015, the Group's revenue from the overseas market was RMB1,584 million, representing a year-on-year decrease of 9.2% and accounting for 4.2% of the total revenues. Although there was a decline in overseas revenue due to the Group's initiative to scale down business with low operating efficiency and the cyclical fluctuations of large projects and implementation timing of projects, we strengthened our development efforts in overseas turnkey projects and continuously optimized the revenue structure in overseas market, and the proportion of the revenue from turnkey projects increased to 69% of revenue from overseas market.

⁷ Revenues from sources other than China Telecom include revenue from China Mobile, China Unicom and the Tower Company.

⁸ Six major group-level products include "Smart City", "Smart Security", "Intelligent Building", "Smart Industrial Park", "Cloud Computing" and "E-certification".

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Corporate Management and Governance

During the first half of 2015, the Group was awarded "5A" qualification certificate as a logistics enterprise by China Federation of Logistics & Purchasing, becoming the only enterprise awarded with the "5A" logistics qualification in the telecommunications industry. The Group further established China Comservice Supply Chain Management Ltd. in July 2015 to further integrate resources to actively explore professional logistics business. Also, we commenced to explore the feasibility of professional operation for the traditional business segments and improved the standard in synergistic operation. Regarding the fundamental management, the Group continued to optimize the organization structure, streamlined administrative staff, increased manpower for frontline marketing activities, and facilitated cost-effectiveness.

During the first half of 2015, the Group was again awarded "Best CFO" and "Best Investor Relations" in the 5th session of the Asian Excellence Recognition Awards 2015 by *Corporate Governance Asia*, a renowned journal on corporate governance in Asia.

Corporate Social Responsibility

The Group has always focused on environmental protection, energy conservation and emission reduction, actively participated in various disaster relief and charitable activities so as to fulfill the social responsibility and actively contribute to the society. The Group insists on promoting energy-saving products and services and assists domestic telecommunications operators to handle redundant assets and save operating cost through contracted energy management platform and other innovative methods. During the first half of this year, after the occurrence of a magnitude 8.1 earthquake in Nepal, the Group immediately joined the international disaster relief by assisting the local operators and the PRC Embassy in restoring the communications network and aid supply delivery, which demonstrated social responsibility and international humanity of the PRC enterprises. After the sinking of the cruise ship *Eastern Star* in the Yangtze River Basin and the disaster brought by Typhoon *Chan-hom*, the Group actively assisted the operator customers to ensure the normal operation of the communications network and received extensive praises from customers and the society.

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Prospects

Against the backdrop of slow recovery in global economy and with China's economy entering into a "new normal" phase, the Group is encountering many new situations and changes in its development. The strong promotion by the government in areas, such as the "Internet+", "Broadband China", "Made in China 2025", "One Belt, One Road", "Information Security", "Utility Tunnel System" construction, and "enhancement of the speed and quality of operators", will expand the market potential for the Group. Meanwhile, factors such as slowdown of the macroeconomic growth, low development rate of the communications industry, decrease in service charges and changes in regulatory policies also brought many challenges to the Group. We will capture the opportunity arising from domestic telecommunications operators' construction of 4G and fiber optic broadband network, continuously seek new business opportunities in the internet-oriented transformation of domestic telecommunications operators and step up efforts in the expansion of northern China market, with a view to maintaining a stable fundamental of our operation. Meanwhile, the Group will strengthen the value-driven principle, deepen innovation and transformation, and facilitate the development through innovation. Firstly, the Group will optimize the structure of its businesses and customers. The Group will continuously pursue opportunity arising from the increase in the operating expenditure of domestic telecommunications operators, strongly expand the businesses that foster customers' loyalty, such as maintenance and logistics, and also the high-valued businesses such as "Smart City", "Smart Security", "Smart Industrial Park" and "Smart Home". The Group will also capture the opportunity in the industrial Internet and speed up the development in major sectors, such as government, electricity, water conservancy, transportation and municipal infrastructure to realize the scale development in the domestic non-operator market. Leveraging on the opportunity of the "One Belt, One Road", the Group will pursue breakthrough in the turnkey projects in overseas market. Secondly, the Group will optimize its operating model. The Group will actively explore the operating model in combination of investment and financing, undertake large turnkey projects under the BT/BOT model on a trial basis, accelerate integration of the new technology with traditional business and promote cross-sector operation. The Group will gradually promote the appropriate integration within professions such as logistics, distribution, design and construction, and strengthen synergistic operation. Thirdly, the Group will optimize its internal management. The Group will further build a flat organization structure to increase management efficiency, sub-divide performance evaluation unit to match resources precisely and strengthen the foundation management to prevent various risks. Through continuous optimization, the Group can speed up its transformation towards high-end areas and continually create higher values for its shareholders and customers.

Finally, on behalf of the Board, I would like to express my sincere gratitude to Mr. Wei Leping, who resigned as an independent non-executive director of the Company in June 2015, for his outstanding contributions to the Group and express my sincere welcome to Mr. Lv Tingjie and Mr. Wu Taishi for joining the Board. I would also like to take this opportunity to express my sincere gratitude to shareholders and customers of the Group and all sectors of society for their long standing care and support to the Group.



Sun Kangmin
Chairman

Beijing, PRC
26 August 2015