

CHAIRMAN'S  
STATEMENT

# “FOCUS STRATEGY

# *PAYS OFF*

**DEAR SHAREHOLDERS,**

Addressing acute challenges from market competition in 2016, the Company actively advanced the implementation of the new development strategy centred on “Focus, Cooperation and Innovation” and strived to mitigate the underlying shortcomings. As a result, fundamental capabilities in network, terminals, channels, services and IT were notably enhanced, with business and service revenue restored to a positive and steady momentum while the overall competitive edges were strengthened and cemented, further solidifying the foundation of the Company for a further turnaround and healthy development in the future.

**OVERALL RESULTS**

To promote long-term sustainable development, the Company braved the short-term profit pressure, strengthened its fundamental capabilities, and increased cost initiatives (including selling and marketing, network, operation and support expenses) as appropriate to strive for a gradual turnaround. It achieved initial success in turning around the unfavourable conditions in operation and development. In 2016, service revenue of the Company bottomed out and reached RMB240.98 billion, up 2.4% year-on-year. The Company's EBITDA amounted to RMB79.50 billion, down by 9.1% year-on-year and accounted for 33.0% of

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CHAIRMAN AND CEO



the service revenue. Profit attributable to equity shareholders of the Company was RMB0.63 billion, down by 94.1% year-on-year, which, however, showed substantial improvement compared to the loss attributable to equity shareholders of the Company (excluding the gain on disposal of tower assets) of approximately RMB3.36 billion in the second half of 2015. Going forward, the Company will continue to deepen the implementation of Focus Strategy and strive to improve profitability.

Through implementing precise investment and actively promoting cooperation and resource sharing within and beyond the industry, the Company attained substantial improvement in the network capability while capital expenditure decreased to RMB72.11 billion, down by 46.1% from last year. Benefiting from the gradual improvement in service revenue and the substantial decline in capital expenditure, free cash flow of the Company turned positive and reached RMB2.48 billion.

Taking into consideration the Company's profitability, debt, cash flow level and capital requirements for its future development, the Board has resolved not to pay a dividend for the year 2016. The Company will strive to enhance its profits while paving the way for paying a dividend for the year 2017.

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**BUSINESS DEVELOPMENT****4G continuously gaining edges with a robust kick-off of marketing model transformation set to accelerate mobile service development**

In 2016, the Company focused on the acceleration of 4G business development, driving the turnaround of the operational challenges of mobile service. Mobile service revenue bottomed out and achieved RMB145.02 billion, up 1.7% year-on-year. The number of mobile billing subscribers beat the downward trend for consecutive months last year, registering a net addition of 11.51 million and reaching a total of 263.82 million mobile billing subscribers. The ARPU of mobile billing subscribers remained stable with a slight increase to RMB46.4.

During the year, the Company expedited 4G network construction and achieved 4G network quality on par with the industry in the focused regions with ample capacity; audaciously popularised "All Network Access" handsets with dual SIM card slots, contributing to the fast improvement in terminal supply; triggered rapid increase in mobile data traffic by targeted marketing of data capacity bundled with contents and speeding up the migration of 2G/3G subscribers to 4G; and strengthened the mutual promotion and coordinated development of the integrated offerings in 4G, fixed-line broadband, video, applications, etc. In 2016, the number of 4G subscribers of the Company demonstrated a net

increase of 60.40 million to a total of 104.55 million. The proportion of 4G subscribers to mobile billing subscribers increased by 22.1 percentage points year-on-year to 39.6%, still with enormous potential for growth. The monthly average DOU per 4G subscriber reached 1,521MB.

Leveraging the advantages brought by rapid improvement in 4G network capabilities, wide adoption in "All Network Access" handsets, the proprietary centralised BSS system and the nationwide e-commerce platform, the Company initiated 2I2C marketing model in the fourth quarter of 2016 and began to collaborate with Internet companies on innovative targeted marketing. Through sub-dividing market segments and strengthening data traffic operation, differentiated products and development models were established with a view to achieving win-win scenarios with both subscribers and partners. The innovative business model of 2I2C business not only enables the Company to develop new touch points for customer acquisition and lift the capabilities to drive 4G subscriber and revenue growth at low incremental cost, but also continuously enhances customer value through smart marketing and convenient promotion of consumption upgrade. At present, the 2I2C business has achieved a robust kick-off, which will facilitate marketing model transformation of the Company and accelerate the scale development of its 4G business in future.

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**Fast Development of Innovative Services in Key Areas Driving Steady Growth in Fixed-line Service Revenue**

In 2016, the Company sped up the development of innovative services such as Internet Data Centre (IDC)/cloud computing, Information Communications Technology (ICT), video, Internet of Things (IoT) and others, effectively offsetting the revenue decline in fixed-line voice. The fixed-line service revenue reached RMB94.66 billion, up 3.7% year-on-year, of which the proportion of fixed-line voice revenue dropped to 14.0%, mitigating the operating risk of the decline in fixed-line voice, while further optimising the fixed-line revenue structure.

During the year, the Company actively leveraged its advantages in fibre network and informatisation with the focus on industrial Internet and platform-based services and fully promoted product development, platform support, marketing services and other core capabilities. Besides, it propelled new breakthroughs in IDC and cloud computing, ICT, IoT, Big Data, IPTV, industry applications, Internet finance and other innovative services. In 2016, the Company's IDC and cloud computing revenue reached RMB9.45 billion, up 33.7% year-on-year. ICT revenue reached RMB5.94 billion, up 37.0% year-on-year, enjoying the leading position in educational informatisation while advancing scale development in healthcare informatisation. IPTV revenue reached RMB1.41 billion, up 68.1% year-on-year.

**Actively Countering Competitive Challenges in Broadband Market by Promoting Subscriber Consumption Upgrade and Integrated Development Leveraging High-Bandwidth Products and Video Applications**

Faced with fierce market competition in fixed-line broadband, the Company, by taking full advantage of the network capabilities generated from fibre network upgrade, vigorously promoted high-bandwidth products and enriched video contents and applications to stimulate bandwidth upgrade and showcased differentiation and brand edges. The Company optimised fixed-line broadband customer service, installation and maintenance work flow, and strengthened support capabilities, which in turn enhanced end-to-end network experience and customer satisfaction. It also pushed forward the optimisation and upgrade of the household Internet integrated products of the broadband, video and applications to drive mutual-promoting development. In 2016, the Company's fixed-line broadband access revenue amounted to RMB43.87 billion, maintaining steady performance year-on-year. Fixed-line broadband subscribers increased by 4.0% year-on-year to 75.24 million, of which 71.2% were Fibre-to-the-home (FTTH) subscribers. "Smart WO Family" subscribers accounted for 26.1% of the fixed-line broadband subscribers, up 12.8 percentage points year-on-year.

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**NETWORK DEPLOYMENT**

With an aim to providing high quality network experience of "faster speed, broader coverage, better perception" to its customers, the Company focused on key regions, including 4G, fixed-line broadband and other key businesses, and deepened cooperation and co-sharing in deploying premium network with craftsmanship spirit under highly precise and efficient investment. In 2016, the Company recorded a net increase of 337,000 4G base stations to a total of 736,000, with coverage, speed and signal quality of the 4G network in key regions on par with the industry. As a result of the steady progress in the speed upgrade in fixed-line broadband, ten provinces in Northern China achieved "all fibre network", in which city areas were basically equipped with 100Mbps access capability. The Company continued to enhance its basic network capabilities such as transmission and carrying network with industry-lowest backhaul latency. Rapid improvement in network capabilities has laid a solid foundation for the Company to accelerate its business development.

**IN-DEPTH COOPERATION AND INNOVATIVE TRANSFORMATION**

In 2016, the Company actively promoted in-depth cooperation in various aspects to facilitate improvement in the network and service development capability, as well as cost reduction and efficiency enhancement, with fruitful results gradually emerging. Through innovative targeted marketing cooperation with Internet companies, the Company managed to expand touch points with customers. The Company implemented infrastructure resources co-building and co-sharing within the industry; proactively promoted cooperation with mobile virtual network operators (MVNOs), maintaining leadership in MVNO subscriber market share. The Company also strengthened cooperation with private capital on local access in Southern China and promoted diversified and cross-industry cooperation for win-win development.

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During the year, the comprehensive and strategic cooperation with China Telecom was smoothly progressing. During the year, a total of 70,000 4G base stations and approximately 16,000 km transmission fibre cable were co-built and co-shared. The Company also jointly promoted 6-mode "All Network Access" handsets together with China Telecom and standardised the 4K smart set-top box and broadband services. Through the cooperation, savings of approximately RMB3.3 billion in CAPEX and RMB0.35 billion in operating expenses were achieved. Looking ahead, the two parties will further open existing base station resources and strengthen the sharing, while enhancing cooperation in operational maintenance and innovative services to reap new outcomes.

The Company deepened innovation in its systems and mechanisms. For the fundamental services, the Company promoted simplification of administration and pushed forward appropriate delegation and empowerment to enhance efficiency. For the innovative services, it promoted the market-oriented reform and initiated internal innovation incubation projects to actively create an innovative ambience; improved the support capability of its IT systems and strengthened cost and risk control; systematically pushed forward the reform in human resource structure, and optimised staff incentive system and structure to motivate operational vibrancy at all levels.

**CORPORATE GOVERNANCE AND SOCIAL RESPONSIBILITY**

The Company continues on improving corporate governance structure and strengthening execution, leading to steady enhancement in management and corporate governance. In 2016, the Company was awarded a number of accolades, including "Asia's No. 1 Best Managed Company – TMT Sector" by FinanceAsia, and "Asia's No. 1 Most Honored Telecom Company" by Institutional Investor.

The Company took the initiative in fulfilling its social responsibilities and actively supported the harmonious economic, social and environmental development guided by the developmental concept of being "Innovative, Coherent, Green, Open, Sharing". The Company was committed to building the fast, green and secure premium network; actively conducted green operation, carried forward equipment reuse and reduced network energy consumption; enhanced service quality to provide consumers with the most compelling experience, assured consumption and dedicated services; shared the success and growth with its employees while adding values to them; and supported development in the western region by enhancing network coverage and service channel construction in remote areas to narrow the digital divide and create a smart lifestyle.

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### OUTLOOK

Currently, along with the drastic change of the market environment, the Company is undergoing a new stage of transformation. A new round of technology and industrial revolution is steering us into a new digital and intelligent era. While the transmission-based basic services remain as the main revenue stream for operators, the traditional telecommunication subscriber market has already been saturated and voice services are on the downward trend with the existing market to witness fiercer competition. The demand for data traffic, a key element of digital ecosystem, continues to increase. Innovative services addressing new demand have become the new engine for growth. With the "Internet Superpower" strategy and the "Internet+" action plan implemented by the State, the Internet of Things, cloud computing and Big Data have turned into real demands from potential market, promising great industry values. In the meantime, further release of reform benefits generated within and beyond the Company will promote China Unicom to change its operational mechanism at a higher level.

Looking into the future, the Company will respond to hardships and challenges face-to-face, grab development opportunities, deepen the implementation of Focus Strategy, persistently uphold scale and economical development as the centre, promote growth, control costs and reform mechanism, thus pushing the Company to shorten the odyssey of transformation, as well as to accelerate the turnaround in future, and step onto the healthy development path. We will unswervingly promote the innovation and transformation of operating model and manage innovative use of resources, so as to deliver sustainable growth in revenue and gradual economic improvement. We are determined to improve quality and enhance efficiency, eliminate excess capacity and destock based on the practical situation. We will promote frequency band and capacity reduction of 2G/3G networks in an orderly manner to improve management, cost effectiveness and operational efficiency. We will accelerate reform in various fields and build a more market-oriented mechanism in an effort to enhance corporate vibrancy and return.

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Lastly, on behalf of the Board of Directors of the Company, I would like to express my sincere gratitude to all shareholders, customers and friends across the society for their support to the Company, and to all employees for their continuous dedication and contribution along the way!



**Wang Xiaochu**

*Chairman and Chief Executive Officer*

Hong Kong, 15 March 2017

*TO EXPEDITE  
TURNAROUND IN  
FUTURE THROUGH*

**PROMOTE GROWTH;  
CONTROL COSTS;  
REFORM MECHANISM**