

Financial Review

In 2018, the Company further deepened the implementation of the “Big connectivity” strategy and the integrated development of the “four growth engines”, enhanced the differentiation of products and services, fully utilized price elasticity and stimulated customer demand. In the face of severe adversities resulting from stiffening market competition, a rapid decline in data value and a significant reduction in revenue subsequent to the cancellation of data “roaming” charges, the Group has made prompt adjustments to its business strategy, proactively responded to market competition, further consolidated its market share and customer base, and improved the network and service quality. Following its endeavours to increase revenue and reduce costs, the Group’s annual results achieved steady growth.

The Company has continued to actively promote its low-cost, high-efficiency operation model, conducted resources utilization evaluation in key areas, and optimized its strategies, budget and performance-based salary management. The Group’s operational efficiency has remained favorable, thereby maintaining its profitability at the international first-class operators’ level and continuously creating value for shareholders.

	2018	2017	Change
Operating revenue (RMB million)	736,819	740,514	-0.5% (1.8%*)
Revenue from telecommunications services (RMB million)	670,907	668,351	0.4% (3.7%*)
Revenue from sales of products and others (RMB million)	65,912	72,163	-8.7% (-14.0%*)
EBITDA (RMB million)	275,541	270,421	1.9%
EBITDA margin	37.4%	36.5%	0.9pp
Profit attributable to equity shareholders (RMB million)	117,781	114,279	3.1%
Margin of profit attributable to equity shareholders	16.0%	15.4%	0.6pp
Basic earnings per share (RMB)	5.75	5.58	3.1%

* The revenue growth rates in brackets are derived on a comparable basis after applying the new revenue standard (IFRS/HKFRS 15) to the revenue figures of last year pursuant to a static calculation.



OPERATING REVENUE

In 2018, the Company's operating revenue reached RMB736.8 billion, down by 0.5% compared to the previous year, of which revenue from telecommunications services was RMB670.9 billion, up by 0.4% compared to the previous year. After applying the new revenue standard (IFRS/HKFRS 15) to the revenue figures of last year pursuant to a static calculation, the corresponding growth rate of operating revenue and telecommunications service revenue stood at 1.8% and 3.7%, respectively, on a comparable basis.

The cancellation of domestic data "roaming" charges, which has been implemented since July 2018 in compliance with the state's requirements, has posed a significant impact on the Group's revenue. In addition, the increase in competition has led to a rapid decline in data value. The growth in the Group's telecommunications services revenue has been under tremendous pressure.

Revenue from voice services

Due to the substitution effect of mobile Internet, the cancellation of handset domestic long-distances roaming tariffs and other factors, revenue from voice services continued to decline to RMB108.1 billion, down by an ever-accelerating rate of 31.1% compared to the previous year, representing 16.1% of revenue from telecommunications services, down by 7.4 percentage points compared to the previous year.

Revenue from data services

Revenue from data services was RMB542.1 billion, up by 9.9% compared to the previous year, representing 80.8% of revenue from telecommunications services, up by 7.0 percentage points compared to the previous year. The Group's revenue structure was further optimized.

As a result of the Group's continuous enrichment of its data products, enhancement of its precise marketing and deepening of its data traffic refined operation, data traffic business maintained a rapid growth. Revenue from wireless data traffic was RMB383.3 billion, up by 5.0% compared to the previous year, and was the significant engine of revenue growth. However, due to factors such as increasing competition and the cancellation of domestic data "roaming" charges, the revenue growth rate has declined. Wireless data traffic revenue as a proportion of revenue from telecommunications services rose to 57.1%. SMS/MMS services revenue was RMB28.8 billion, up by 2.6% compared to the previous year.

The Group has actively established high-quality broadband products, enhanced network service quality and enriched the contents and applications for the household market, thereby maintaining a strong growth in the number of broadband customers. Revenue from wireline broadband services reached RMB54.3 billion, up by 36.6% compared to the previous year, and became the significant source of growth for the Group's revenue.

The applications and information services made a breakthrough, with a rapid growth in dedicated lines, IDC, Internet of Things, "MIGU Video" and other businesses. Revenue from applications and information services was RMB75.7 billion, up by 24.8% compared to the previous year, representing a further enlarged scale of operation.

Revenue from sales of products and others

In order to provide customers with a broader offering of terminals with more diversified functions, the Group actively promoted the sale of handsets through open channels, so its sales of handsets continued to decrease. Revenue from the sales of products and others was RMB65.9 billion, down by 8.7% compared to the previous year. The Group's terminal sale business mainly serves to facilitate the expansion of the core telecommunications services, and hence its profit contribution is relatively low.

OPERATING EXPENSES

The Group continued to adhere to the principles of “forward-looking planning, effective resources allocation, rational investment and refined management” in cost control, strived to decrease expenditure and increase efficiency, reduced per unit business costs, and maintained a favorable profitability.

In 2018, the Company’s operating expenses were RMB615.4 billion, down by 0.8% compared to the previous year. Operating expenses represented 83.5% of operating revenue.

	2018 RMB million	2017 RMB million	Change
Operating expenses	615,432	620,388	-0.8%
Leased lines and network assets	47,470	46,336	2.4%
Interconnection	20,692	21,762	-4.9%
Depreciation	152,545	149,780	1.8%
Employee benefit and related expenses	93,939	85,513	9.9%
Selling expenses	60,326	61,086	-1.2%
Cost of products sold	66,231	73,668	-10.1%
Other operating expenses	174,229	182,243	-4.4%

Leased Lines and Network Assets

Leased lines and network assets expenses were RMB47.5 billion, up by 2.4% compared to the previous year and representing 6.5% of operating revenue. To maintain the Group’s advantages in the quality and coverage of its networks, the towers leasing fee increased continuously to RMB39.0 billion, up by 5.5% compared to the previous year. The leasing fees for TD-SCDMA network capacity were RMB0.4 billion, down by 61.6% compared to the previous year. The leasing fees of “Village Connect” assets were RMB2.2 billion, down by 11.2% compared to the previous year.

Interconnection

Interconnection expenses were RMB20.7 billion, down by 4.9% compared to the previous year and representing 2.8% of operating revenue.

Depreciation

Depreciation was RMB152.5 billion, up by 1.8% compared to the previous year and representing 20.7% of operating revenue. The growth rate of depreciation has slowdown mainly because the Group has made provisions for the impairment of 2G wireless network equipment in the previous year.

Employee Benefit and Related Expenses

Employee benefit and related expenses were RMB93.9 billion, up by 9.9% compared to the previous year and representing 12.7% of operating revenue. The Group continued to adjust and optimize its personnel structure, and reallocate its compensation and incentives in favor of primary frontline employees, leading to an increase in employee benefit and related expenses.

Selling Expenses

Selling expenses were RMB60.3 billion, down by 1.2% compared to the previous year and representing 8.2% of operating revenue. The Group actively promoted the transformation of its marketing model, enhanced its precision marketing to customers, and endeavored to improve the efficiency of its utilization of marketing resources. The ratio of selling expenses to telecommunications services revenue remained industry-lowest.

Cost of Products Sold

Cost of products sold was RMB66.2 billion, down by 10.1% compared to the previous year. With the Group’s promotion of the sale of handsets through open channels, cost of products sold decreased.

Other Operating Expenses

Other operating expenses were RMB174.2 billion, down by 4.4% compared to the previous year and representing 23.6% of operating revenue. Among these, maintenance expenses, operating lease charges and utilities expenses totaled RMB102.7 billion, up by 1.3% compared to the previous year, due mainly to the expansion of assets scale and increase in resources prices. In order to support network transformation, business innovation and implementation, the Group increased its expenses in operation support, research & development and related cost, which reached RMB44.0 billion, up by 15.7% compared to the previous year. Administrative expenses such as conference, office, travelling and business entertainment expenses were under strict control, remaining flat.

PROFITABILITY

In 2018, the Group's profitability continued to be industry-leading. Profit from operations was RMB121.4 billion, up by 1.0% compared to the previous year. EBITDA was RMB275.5 billion and EBITDA margin was 37.4%, up by 0.9 percentage points compared to the previous year. Profit attributable to equity shareholders was RMB117.8 billion and its margin was 16.0%.

	2018 RMB million	2017 RMB million	Change
Profit from operations	121,387	120,126	1.0%
Other gains	2,906	2,389	21.6%
Interest and other income	15,885	15,883	0.0%
Finance costs	144	210	-31.4%
Income from investments accounted for using the equity method	13,861	9,949	39.3%
Taxation	35,944	33,723	6.6%
Profit attributable to equity shareholders	117,781	114,279	3.1%

CAPITAL STRUCTURE

The Group's financial position continued to remain steady. As at the end of 2018, total assets and total liabilities were RMB1,535.9 billion and RMB480.1 billion, respectively. The liabilities to assets ratio was 31.3%.

The Group consistently and firmly adhered to its prudent financial risk management policies and maintained sound repayment capabilities. The effective interest coverage multiple was 959 times.

	As at 31 December 2018 RMB million	As at 31 December 2017 RMB million	Change
Current assets	535,116	558,196	-4.1%
Non-current assets	1,000,794	963,917	3.8%
Total assets	1,535,910	1,522,113	0.9%
Current liabilities	474,398	529,982	-10.5%
Non-current liabilities	5,703	3,250	75.5%
Total liabilities	480,101	533,232	-10.0%
Non-controlling interests	3,404	3,245	4.9%
Total equity attributable to shareholders	1,052,405	985,636	6.8%
Total equity	1,055,809	988,881	6.8%

FUND MANAGEMENT AND CASH FLOW

The Group consistently and firmly adhered to its sound and prudent financial policies and stringent fund management systems and strived to maintain a healthy cash flow level, thereby ensuring the safety and integrity of its funds through its highly centralized management of investing and financing activities. Meanwhile, the Group continued to reinforce its centralized fund management efforts and made appropriate allocations of its funds, thereby enhancing the efficiency of funds utilization.

In 2018, the Group's cash flow remained healthy. Net cash inflow from operating activities, net cash outflow from investing activities and net cash outflow from financing activities were RMB206.2 billion, RMB212.2 billion and RMB57.8 billion, respectively. Free cash flow was RMB39.1 billion. As at the end of 2018, the Group's cash and bank balances were RMB361.6 billion, of which 96.7%, 1.8% and 1.4% were denominated in Renminbi, U.S. dollars and Hong Kong dollars, respectively. The steady fund management and healthy cash flow provided a solid foundation for the sustainable healthy development of the Group.

	2018 RMB million	2017 RMB million	Change
Net cash inflow from operating activities	206,151	245,514	-16.0%
Net cash outflow from investing activities	212,231	106,533	99.2%
Net cash outflow from financing activities	57,820	108,231	-46.6%
Free cash flow	39,076	67,981	-42.5%

CREDIT RATINGS

Currently, the Company's corporate credit ratings are equivalent to China's sovereign credit ratings, namely, A+/Outlook Stable from Standard & Poor's and A1/Outlook Stable from Moody's. These ratings reflect that the Group's sound financial strength, favourable business potential and solid financial management are highly recognized by the market.