

CHINA TELECOM CORP LTD

Form 20-F

June 20, 2003

Table of Contents

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 20-F

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2002

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 1-31517

(Exact Name of Registrant as Specified in Its Charter)

China Telecom Corporation Limited

(Translation of Registrant's Name into English)

People's Republic of China

(Jurisdiction of Incorporation or Organization)

31 Jinrong Street

Beijing, China 100032

(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange
On Which Registered	
American depository shares H shares, par value RMB1.00 per share	New York Stock Exchange, Inc. New York Stock Exchange, Inc.*

* Not for trading, but only in connection with the listing on the New York Stock Exchange, Inc. of American depository shares, each representing 100 H shares.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

As of December 31, 2002, 67,586,776,503 domestic shares and 8,027,410,000 H shares, par value RMB1.00 per share, were issued and outstanding. H shares are ordinary shares of the Company listed on The Stock Exchange of Hong Kong Limited.

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark which financial statement item the registrant has elected to follow. Item 17 Item 18

Table of Contents**CHINA TELECOM CORPORATION LIMITED****TABLE OF CONTENTS**

	Page
<u>Forward-Looking Statements</u>	3
<u>Certain Definitions</u>	4
<u>PART I</u>	5
Item 1. <u>Identity of Directors, Senior Management and Advisers.</u>	5
Item 2. <u>Offer Statistics and Expected Timetable.</u>	5
Item 3. <u>Key Information.</u>	5
Item 4. <u>Information on the Company.</u>	17
Item 5. <u>Operating and Financial Review and Prospects.</u>	47
Item 6. <u>Directors, Senior Management and Employees.</u>	65
Item 7. <u>Major Shareholders and Related Party Transactions.</u>	72
Item 8. <u>Financial Information.</u>	79
Item 9. <u>The Offer and Listing.</u>	80
Item 10. <u>Additional Information.</u>	81
Item 11. <u>Quantitative and Qualitative Disclosures about Market Risk.</u>	90
Item 12. <u>Description of Securities Other than Equity Securities.</u>	92
<u>PART II</u>	93
Item 13. <u>Defaults, Dividend Arrearages and Delinquencies.</u>	93
Item 14. <u>Material Modifications to the Rights of Security Holders and Use of Proceeds.</u>	93
Item 15. <u>Controls and Procedures.</u>	94
Item 16A. <u>Audit Committee Financial Expert.</u>	94
Item 16B. <u>Code of Ethics</u>	94
Item 16C. <u>Principal Accountant Fees and Services</u>	94
Item 16D. <u>Exemptions From the Listing Standards for Audit Committees</u>	94
<u>PART III</u>	95
Item 17. <u>Financial Statements.</u>	95
Item 18. <u>Financial Statements.</u>	95
Item 19. <u>Exhibits.</u>	95

Table of Contents

Forward-Looking Statements

This annual report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are, by their nature, subject to significant risks and uncertainties, and include, without limitation, statements relating to:

our business and operating strategies;

our network expansion and capital expenditure plans;

our operations and business prospects;

our financial condition and results of operations;

the industry regulatory environment as well as the industry outlook generally; and

future developments in the telecommunications industry in China.

The words anticipate, believe, could, estimate, expect, intend, may, plan, seek, will, would and similar expressions, as they are intended to identify a number of these forward-looking statements.

These forward-looking statements are subject to risks, uncertainties and assumptions, some of which are beyond our control. In addition, these forward-looking statements reflect our current views with respect to future events and are not a guarantee of future performance. We do not intend to update these forward-looking statements. Actual results may differ materially from the information contained in the forward-looking statements as a result of a number of factors, including, without limitation, the risk factors set forth in Item 3. Key Information D. Risk Factors and the following:

any changes in the regulatory policies of the Ministry of Information Industry and other relevant government authorities relating to, among other matters:

the granting and approval of licenses;

tariff policies;

interconnection and settlement arrangements;

capital investment priorities; and

numbering resources allocation;

the effects of competition on the demand for and price of our services;

the development of new technologies and applications or services affecting our current and future business;

changes in political, economic, legal and social conditions in China, including the Chinese government's specific policies with respect to foreign investment in the telecommunications industry, economic growth, inflation, foreign exchange and the availability of credit; and

Table of Contents

changes in population growth and gross domestic product, or GDP, growth and the impact of those changes on the demand for our services.

Certain Definitions

As used in this annual report, references to us, we, the Company and China Telecom are to China Telecom Corporation Limited. Unless the context otherwise requires, these references include all of our subsidiaries. In respect of any time prior to our incorporation, references to us, we and China Telecom are to the telecommunications businesses in which our predecessors were engaged and which were subsequently assumed by us. All references to China Telecom Group are to China Telecommunications Corporation, our controlling shareholder. Unless the context otherwise requires, these references include all of its subsidiaries, including us and our subsidiaries.

Table of Contents

PART I

Item 1. Identity of Directors, Senior Management and Advisers.

Not applicable.

Item 2. Offer Statistics and Expected Timetable.

Not applicable.

Item 3. Key Information.

A. Selected Financial Data

The following table presents our selected financial data. The selected balance sheet data as of December 31, 2001 and 2002, and the selected income statement data and cash flow data for the years ended December 31, 2000, 2001 and 2002, are derived from, and should be read in conjunction with, our audited financial statements and operating and financial review and prospects included elsewhere in this annual report. The selected balance sheet data as of December 31, 1999 and 2000 and the selected income statement and cash flow data for the year ended December 31, 1999 are derived from our audited financial statements, which are not included in this annual report. Our audited financial statements are prepared and presented in accordance with International Financial Reporting Standards, or IFRS, which differ in certain significant respects from accounting principles generally accepted in the United States, or US GAAP. For a discussion of significant differences between IFRS and US GAAP, as they relate to us, see Note 32 to the audited financial statements included elsewhere in this annual report.

The selected financial data reflect the restructuring described under Item 4. Information on the Company A. History and Development of the Company Our Restructuring and Initial Public Offering and have been prepared as if our current structure had been in existence throughout the relevant periods. Since China Telecom Group controlled the telecommunications operations and the related assets transferred to us prior to our restructuring and continues to control us after our restructuring, the financial data of the telecommunications operations in Shanghai Municipality, Guangdong Province, Jiangsu Province and Zhejiang Province transferred to us by China Telecom Group for periods prior to our incorporation have been combined in a manner similar to a pooling-of-interests. The assets and liabilities of the entities being combined are carried forward at their recorded historical amounts, and the book value of the assets and liabilities, as well as the revenue and expenses of each of these entities for the periods prior to our incorporation, are added together to prepare our financial statements.

Following our restructuring, China Telecom Group retained the ownership of certain assets that were historically associated with our operations, which had a carrying amount of RMB11,285 million as of December 31, 2001 and primarily consisted of investments in non-telecommunications industries, the inter-provincial optic fibers, international gateway and international transmission equipment, telecommunications equipment for special communications services, and certain office equipment, properties and buildings. Except for the income statement data for the year ended December 31, 2002, the income statement data for the other periods include the results of the assets

Edgar Filing: CHINA TELECOM CORP LTD - Form 20-F

retained by China Telecom Group. The results of such assets are not reflected in our income statement for future periods ending after December 31, 2001. Except for the balance sheet data as of December 31, 2001 and 2002, the balance sheet data include data related to the assets retained by China Telecom Group. These assets are not reflected in our balance sheet after December 31, 2001.

Table of Contents

We have not included the selected financial data as of and for the year ended December 31, 1998. As described under Item 4. Information on the Company A. History and Development of the Company, the Chinese government undertook a comprehensive restructuring of the telecommunications industry in China in 1999, including wireline, mobile, paging and satellite communications businesses, and China Telecom Group, our parent company, was reorganized in May 2000 as part of the restructuring to operate the wireline telecommunication business in China. In connection with our restructuring in preparation for our initial public offering in 2002, China Telecom Group transferred to us its assets, rights and liabilities in connection with its telecommunications operations in Shanghai Municipality, Guangdong Province, Jiangsu Province and Zhejiang Province. Therefore, preparation of selected financial data as of and for the year ended December 31, 1998 in accordance with IFRS would involve unreasonable effort and expense.

	As of or for the year ended December 31,				
	1999	2000	2001	2002	2002
	RMB	RMB	RMB	RMB	US\$
	(in millions, except share numbers and per share and per ADS data)				
Income Statement Data:					
IFRS					
Operating revenue	65,291	71,021	68,546	75,496	9,118
Operating expenses	(38,929)	(47,397)	(50,448)	(54,118)	(6,536)
Operating income	26,362	23,624	18,098	21,378	2,582
Income before income tax and minority interests ⁽²⁾	25,961	24,144	6,793	20,785	2,511
Income tax	(5,459)	(4,857)	69	(3,855)	(466)
Net income	20,409	19,219	6,883	16,864	2,037
Basic earnings per share ⁽¹⁾	0.30	0.28	0.10	0.24	0.03
Basic earnings per ADS ⁽¹⁾	29.87	28.13	10.08	24.36	2.94
U.S. GAAP					
Net income		19,219	14,785	15,794	1,908
Basic earnings per share ⁽¹⁾		0.28	0.22	0.23	0.03
Basic earnings per ADS ⁽¹⁾		28.13	21.64	22.81	2.76
Balance Sheet Data:					
IFRS					
Cash and cash equivalents	15,451	13,861	3,882	16,423	1,983
Accounts receivable, net	6,810	7,130	5,608	5,961	720
Property, plant and equipment, net ⁽²⁾	116,461	127,528	138,623	149,165	18,015
Total assets ⁽²⁾	182,367	197,401	189,334	210,852	25,465
Short-term debt ⁽³⁾	9,811	12,194	18,827	19,175	2,316
Accounts payable	6,952	10,214	14,919	14,399	1,739
Long-term obligations	12,395	10,144	7,112	4,853	586
Deferred revenue (excluding current portion)	32,604	30,304	26,353	21,612	2,610
Total liabilities	90,951	94,832	90,909	84,710	10,230
Shareholders' equity ⁽²⁾	90,550	101,619	97,485	125,008	15,098
U.S. GAAP					
Property, plant and equipment, net		127,528	146,399	155,344	18,761
Total assets		197,401	197,110	217,031	26,211
Shareholders' equity		101,619	102,603	129,056	15,587
Cash Flow Data:					
IFRS					
Cash flows from operating activities	37,379	38,255	32,761	37,102	4,481
Net cash used in investing activities ⁽⁴⁾	(25,234)	(31,736)	(35,399)	(29,095)	(3,514)
Capital expenditures ⁽⁴⁾	(25,773)	(30,618)	(34,610)	(28,169)	(3,402)
Net cash (used in) / from financing activities	(9,176)	(8,109)	(7,341)	4,534	547

Table of Contents

- (1) Basic earnings per share and per ADS have been computed by dividing net income by the weighted average number of shares issued and outstanding during the year of 2002, as if the 68,317,270,803 shares issued and outstanding upon our formation on September 10, 2002 had been outstanding for all relevant periods. Each ADS represents 100 H shares.
- (2) Includes the effect of the revaluation of property, plant and equipment as of December 31, 2001. See Note 7 to our audited financial statements.
- (3) Excludes current portion of long-term debt.
- (4) Capital expenditures are part of and not an addition to net cash used in investing activities.

Exchange Rate Information

Our financial statements are expressed in Renminbi. Solely for the convenience of the reader, this annual report contains translations of certain Renminbi and Hong Kong dollar amounts into U.S. dollars and vice versa at RMB 8.2800 = US\$1.00 and HK\$7.7988 = US\$1.00, the noon buying rate prevailing on December 31, 2002. These translations should not be construed as representations that the Renminbi or Hong Kong dollar amounts could actually be converted into U.S. dollars at such rates or at all.

The noon buying rates in New York City for cable transfers as certified for customs purposes by the Federal Reserve Bank of New York were RMB 8.2768 = US\$1.00 and HK\$7.7990 = US\$1.00, respectively, on June 17, 2003. The following table sets forth the high and low noon buying rates between Renminbi and U.S. dollars and between Hong Kong dollars and U.S. dollars for each month during the previous six months:

Noon Buying Rate

	RMB per US\$1.00			HK\$ per US\$1.00	
	High	Low		High	Low
December 2002	8.2800	8.2771	December 2002	7.7992	7.7980
January 2003	8.2800	8.2766	January 2003	7.8001	7.7988
February 2003	8.2800	8.2768	February 2003	7.8000	7.7989
March 2003	8.2776	8.2770	March 2003	7.7995	7.7987
April 2003	8.2774	8.2769	April 2003	7.7998	7.7991
May 2003	8.2771	8.2768	May 2003	7.7995	7.7985

The following table sets forth the average noon buying rates between Renminbi and U.S. dollars and between Hong Kong dollars and U.S. dollars for each of 1998, 1999, 2000, 2001 and 2002, calculated by averaging the noon buying rates on the last day of each month during each of the relevant years.

Average Noon Buying Rate

RMB per	HK\$ per US\$1.00
--------------------	--------------------------

	<u>US\$1.00</u>	
1998	8.2969	7.7465
1999	8.2785	7.7599
2000	8.2784	7.7936
2001	8.2772	7.7996
2002	8.2772	7.7996

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

Table of Contents

D. Risk Factors

Risks Relating to Our Business

We face increasing competition, which may adversely affect our business growth and results of operations.

The telecommunications industry in China is rapidly evolving. Until the mid-1990s, we were the sole provider of wireline telecommunications services in our service regions and, as a result, had a dominant market position. We began to operate in a competitive market as the Chinese government started to implement a number of measures to restructure the telecommunications industry and encourage fair and orderly competition in the industry in the mid-1990s. We face increasing competition from other telecommunications service providers in China, including the newly formed China Netcom Group. We expect our competitors to expand further their network coverage and increase their sales and marketing efforts in our service regions. See Item 4. Information on the Company B. Business Overview Competition. In particular:

we face indirect competition in our local wireline telephone services from China's two mobile telephone service providers, China Mobile Communications Corporation, or China Mobile, and China United Telecommunications Corporation, or China Unicom, and have begun to face direct competition from China Railways Communications Ltd., or China Railcom;

we face increasingly intense competition in our long distance telephone services from other providers of long distance services using public switched telephone networks, including China Unicom, China Railcom, and, potentially, China Netcom Group, and other providers of long distance services using the voice-over-Internet-protocol, or VoIP, technology, including China Mobile, China Netcom Group, China Unicom and China Railcom;

we face increasing competition in our data and Internet services from many competitors, including, primarily, China Unicom, China Netcom Group and China Railcom; and

we may face additional competition from new entrants or providers of new telecommunications services, such as telephone and Internet services offered over cable TV networks.

Moreover, as a result of China's accession to the World Trade Organization, or the WTO, and China's commitment under its WTO Accession Protocol, the Chinese government will gradually open up the telecommunications market in China to foreign operators. See Item 4. Information on the Company B. Business Overview Regulatory and Related Matters Licensing. Foreign operators may have greater financial, managerial and technical resources and more expertise in network management and sales and marketing. Furthermore, advances in technology, as well as changes in the regulatory environment, may further intensify competition.

Our ability to compete effectively may be constrained by a number of factors. For example, under the Chinese government's policy of promoting fair and orderly competition in the telecommunications industry, certain competitors of ours, such as China Unicom and China Railcom, continue to enjoy certain preferential treatment from the Chinese government in tariff setting. They may set their respective tariffs for long distance services using public switched telephone networks and leased line services with the annual approval of the regulatory authorities. This preferential treatment is not available to us. As a result, our competitors who enjoy this preferential treatment may be able to provide their services at prices that are more competitive than ours. In addition, we are not yet permitted to provide mobile communications

Table of Contents

services. We, through China Telecom Group, are, however, actively seeking the issuance of a license for mobile communications in the PRC. We can provide no assurances, however, as to whether or when we may be able to receive any benefit of any license for mobile communications in China.

As a result, our customers may choose to use other providers' services. Increased competition from those providers may force us to lower our tariffs, may reduce or reverse the growth of our customer base and may reduce usage of our networks. Any of these developments could materially adversely affect our business growth and results of operations.

China Netcom Group's control of the last-mile access network in ten northern provinces in China may adversely affect our ability to provide end-to-end services.

As a result of the recent restructuring of China's wireline telecommunications sector, most wireline telecommunications assets except for the nationwide inter-provincial optic fibers, including the last-mile access network, formerly owned by China Telecom Group in ten northern provinces in China were allocated to China Netcom Group. China Telecom Group and China Netcom Group own 70% and 30%, respectively, of the nationwide inter-provincial optic fibers after the restructuring. As we and China Telecom Gr