

9 August 2007

### **Full year financial results ahead of guidance and earnings momentum gathers pace.**

Dear shareholder

It is my pleasure to write to you today about the job your team at Telstra is doing. The men and women of Telstra have delivered truly market-leading results...again. Our team is focused on the job at hand and determined to be world class as we continue into the 19th month of our 5-year transformation journey. We are not there yet, but I can assure you that we are fully committed to reaching the high standards of performance we have set for ourselves in the work we are doing for you.

I am pleased to send you this letter because our team at the New Telstra has delivered for shareholders and the consumer – including the businesses and communities that rely on us to help them stay connected to each other and the world around us.

What's the bottom line? Over the past 12 months the New Telstra has achieved world leading performance across the business. Even though we are only 19 months into our five-year transformation, I am encouraged and pleased about our progress. Think about the following:

- Earnings are up: sales revenues are up; and we are winning in key, highly-competitive markets;
- Full year revenue and earnings came in ahead of guidance – and second half earnings before interest and tax (EBIT) are up a whopping 42%;
- We report market share gains and revenue growth in broadband;
- We had strong revenue growth in mobiles;
- We now have positive residential PSTN (fixed home phone) customer growth;
- We have slowed the decline in overall PSTN; and
- We are creating market-leading innovative new products and services.

When our transformation plan was announced back in November 2005, it was considered by some to be too ambitious, involving too many moving parts. It is ambitious: The scale and scope of the transformation to the New Telstra are unprecedented amongst telecommunication companies around the world. The world is watching us, and now – less than two years after we started this journey – we are setting the new global benchmark. We've had ups and downs – and we have done better in some areas than in others. But, the benefits of transformation investment are starting to materialise and the results are clear for all to see.

During this period, many analysts and media commentators reflected negative sentiment toward Telstra's performance and future prospects...and every reporting period we exceeded the predictions of the sceptics. Our focus on customers and shareholders is the key to our steady improvement. Our people know what Telstra is about and they are delivering.

Our transformation investment peaked this financial year, as we highlighted in the T3 prospectus and again at the half-year results in February, but the pace of change will continue. As I said in November 2005 when we outlined the transformation strategy, we are on a 5-year journey – and we have a way to go yet.

Let me turn to some details of the financial year that ended 30 June 2007. During this year, we continued to win in the key markets – mobiles, broadband, Sensis and more recently PSTN – despite strong competition. We built on the solid operational and financial momentum generated in the first half of the financial year – and accelerated growth in the second half.

We have already achieved major milestones including the launch of the world-leading Next G™ mobile broadband and Next IP™ core networks. In addition, our second half included other world-class performances. Consider the following:

- world-leading revenue and margin performance in our directories business (Sensis);
- rapidly-increasing benefits of customer segmentation from market-based management (MBM) has improved both loyalty and satisfaction of customers as they buy and use our products and services;
- we achieved a double in broadband – growing market share by two percentage points to 47% and growing average revenue per user (ARPU) by 7.7% in the second half;
- we maintained the post-paid \$20 per month 3G versus 2G ARPU premium on a larger, and market leading, 3G customer base of 2 million, including 1 million Next G™ customers.
- growth in residential PSTN customers – the first time residential PSTN customers have grown in several years – as PSTN revenue decline slowed even further to just 2.5%;

I am most encouraged by our ability to innovate as we transform into an integrated media-comms company. We recently launched mobile BigPond TV and BigPond i-Pond, and we are the first major Australian company to enter the new internet world of Second Life. We boosted our Sensis online asset portfolio with the acquisition of a controlling stake in SouFun, a leading real estate and home furnishings web site in China. We also launched a number of “small screen” innovations – such as Sensis search by mobile, Yellow by mobile, Yellow@Home and entered into a partnership with ninemsn.

## Financial Results

We announced a full year profit after tax of \$3.3 billion, up \$92 million or 2.9% on the prior corresponding period. Our earnings before interest and tax (EBIT) grew 7.1% (excluding the Trading Post write-down) to \$5.9 billion, which beat our full year guidance of 3% to 5%. We restored positive earnings growth.

Our sales revenue grew 4.2% for the year, ahead of our full year guidance of 2.5% to 3.0% as we continue to win in the key markets of mobiles, broadband, Sensis and PSTN. Our Australian operations were strong, with underlying sales revenue growing 3.5% to \$21.7 billion.

- **Mobiles:** we continued to take a disproportionate share of 3G customer additions, adding 1.7 million 3GSM customers or growth of 532%. As a result of the strong mobiles customer growth, increased voice and data usage by our 3G customers, and handset sales, mobiles revenue grew 13.9% to \$5.7 billion;
- **Retail broadband:** our retail broadband customer base grew by 60% to 2.4 million, and revenue grew 66% to exceed \$1 billion for the first time. Our retail broadband customers spent 7.7% more per month (on average) in the second half, using our leading broadband applications, services and content;
- **Sensis:** total revenue grew by 8.0% to \$2 billion in a very competitive market, with online search usage up 15% and Emerging Business revenue up 34%.

We grew our residential PSTN customers by 1.1% or 54,000 during the financial year. Our traditional PSTN revenue decline slowed further in the second half, declining 2.5% and for the full year revenue declined 4.1% compared to 6.7% in the prior corresponding period.

Our revenue growth was strong; hence our operating expenses increased 4.4%. Expense increases were driven by higher marketing costs associated with the launch of the Next G™ and Next IP™ networks and higher customer acquisition and recontracting costs – which started to decline in the second half, as expected. This year was the peak spend year for the transformation, and we have laid the foundation to improve future earnings.

Following a review of our Trading Post classified business, we have written-down its carrying value by \$110 million, due to increasing competition in the traditional print classifieds markets.

I refer you to the attached shareholder newsletter for a more detailed analysis of the full year financial results.

## **Dividend**

Telstra's Board of Directors declared a final ordinary dividend of 14 cents per share, fully franked and payable on 21st September 2007. This brings the total ordinary dividend declared and paid for the year to 28 cents per share, or \$3.5 billion.

## **Outlook**

My commitment to you is clear: We will continue to build on the momentum achieved in the past financial year. As we have passed the peak spend year for capital expenditure, the earnings benefits should flow in the coming financial year. As a result, in the financial year ending 30 June 2008, you should expect to see:

- Revenue growth in the range of 2.0% to 3.0%;
- Earnings before interest tax amortisation and depreciation (EBITDA) growth in the range of 2.0% to 3.0%;
- EBIT growth in the range of 3.0% to 5.0%;
- Capital expenditure of between \$4.6 billion and \$4.9 billion (on an accrual basis);
- Dividends – the level of future dividends is a decision for the Board to make twice a year in its normal cycle having regard to earnings and cash flows as well as future regulatory impacts and other factors that affect operations.

We have made good progress in transforming our networks, systems, and corporate culture. However, this coming year will be equally challenging as we deploy the first phase of our IT systems transformation – scheduled for later this calendar year. We will continue to leverage the growth opportunities from our integrated portfolio of media communications assets – including BigPond, Sensis and Foxtel. We will continue to innovate, and lead from the front.

We have the right strategy along with a talented management team and dedicated, capable employees right across the business focused on achieving our strategic objectives – to improve the customer experience through innovation and service and to create long-term shareholder value.

## **Regulation and Government policy**

The regulatory environment and Government policy continue to impede Telstra's ability to invest your dollars confidently in new technology and to deploy advanced services to all Australians. During the year,

- **the regulator** – Australian Competition and Consumer Commission (ACCC) – announced dramatic reductions in the prices we can charge competitors for access to Telstra's copper network – what is called the Unbundled Local Loop (ULL – down 30%) and Line Sharing Service (LSS – down 70%) These decisions were made despite the rising cost of copper, fuel, vehicles, and labour over recent years. They enable competitors to access our copper network below cost and discourage future investment – both by Telstra and by our competitors. We have a case pending in the High Court over the validity of this decision.
- **the Government** announced a decision to hand over nearly \$1 billion of taxpayers' money to SingTel-OPEL to overbuild and compete with the Next G™ broadband network paid for by Telstra shareholders. I am confident we will meet and beat SingTel-OPEL in the marketplace where consumers, not governments, make the decisions. The Government also announced a process to evaluate Next G™ performance prior to the closure of the CDMA network in early 2008 and suggested it may regulate to require Ministerial approval of that closure.

## **High-speed broadband update**

As you know, Telstra is the only company with a fully-developed plan to build a Fibre-to-the Node (FTTN) network to deliver high-speed broadband in Australia. However, we have been stopped by regulatory settings that would subject your investment to unreasonable regulatory risk. When the Government announced the appointment of Expert Taskforce to consider proposals to build FTTN – including changes in the regulatory settings – we were encouraged. But this week we learned that the process is going to be stretched out well into 2008 – more delays.

Still, we will make good on our commitment to you to make sound and timely investments – as we continue to explore all the options we have to wisely invest your capital, better serve our customers, and advance the national interest in bringing high-speed broadband to everyone. I want to encourage you to keep up to date on progress with our high-speed broadband plan and other important matters affecting your company by visiting our consumer advocacy website, [www.nowwearetalking.com.au](http://www.nowwearetalking.com.au).

### **Broadband Services in the Bush**

As you know, we are committed to switching off the CDMA network, which is rapidly becoming obsolete, on 28 January 2008. We have also announced that our Next G™ mobile broadband network will provide the same or better coverage than CDMA in October 2007 – two months ahead of schedule. At the end of July, we had already migrated around 600,000 customers from our CDMA network and have a detailed plan to migrate all the remaining customers by January 2008. We have also launched several new Next G™ handsets specifically suited for regional and rural customers, including the Samsung 411 and LG TU550.

The Board and I remain committed to keeping you informed with regular updates about Telstra's transformation and performance. We also want to encourage you to become an electronic shareholder and help the environment. For more information visit our **new look** investor relations website at [www.telstra.com.au/abouttelstra/investor](http://www.telstra.com.au/abouttelstra/investor)

I also encourage you to go to Telstra's Next G™ and 3G mobile networks to watch a short video message on BigPondTV that I have recorded for you on the annual results, and which you can watch free of charge. Watching this video will enable you to experience first hand the power of the world's largest, fastest and most advanced mobile broadband network. We intend as part of our transformation journey to continue to deliver these kinds of innovative services to the market. Still, there is much yet to be done as we complete our 5-year transformation journey.

In the meantime, this has been a good year – for Telstra shareholders, such as you, and Telstra customers. I hope you are pleased.

Please contact us with any questions or comments at [investor.relations@team.telstra.com](mailto:investor.relations@team.telstra.com).

Yours sincerely



**Sol Trujillo**

**Chief Executive Officer**