

Full year newsletter

# 2007

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## Delivering on our promise

**The world is changing, our customers lives are changing and Telstra is changing. Our customers want more than plain old telephone services (POTS), they want real-time access to information on the move, in the format they choose and where they choose.**

To meet these changing needs, Telstra is transforming into a world class media communications company. Telstra is transforming its networks and systems to meet our customer needs. We have a plan and our transformation is in full swing.

During the financial year we built on our track record of delivering on our promises. We:

- Launched the national Next G™ mobile broadband network, no other mobile network in the world is faster, larger or more advanced;
- Launched the Next IP™ network which, together with the Next G™ network, is the world's largest fully integrated wireline and wireless national Internet Protocol (IP) network;
- Became Australia's 3G market leader;
- Trained 12,000 people at the Telstra Learning Academy in its first 11 months;
- Improved workforce culture, with record numbers of employees responding to the 2007 Employee Engagement Survey and employees rating Telstra more favourably than last year.

But this is only the start, we still have a lot to do. We are bringing world class capabilities to Australia, and we are leading the world.

Our broadband business, BigPond®, extended its market leadership through the launch of innovative applications and content for the new media world. During the year we launched or enhanced our interactive offerings including our Second Life presence, expanded the membership of our games arena with members up 40% year-on-year and our BigBlog™ site experienced more than 7,000 unique visitors per week.

BigPond® recently launched mobile BigPond TV and has embraced the web 2.0 world and our new home page personalisation tool I-Pond™ is spearheading our charge to the user-generated internet experience of the future.

In mobiles, we launched the Next G™ network in October, allowing our customers to change the game. Our customers have embraced the speed and simplicity of the Next G™ network and in the second half over 1 million video calls were made and Sensis search visitors were up 39%.

Our Sensis business is a cornerstone of our integrated media communications strategy and the emerging business asset portfolio grew strongly. This included our banner advertising business, Sensis MediaSmart®, and our mapping business, Whereis®. Our directories business continued to manage the migration from print to online while maintaining some of the best directory revenue growth rates and margins in the world.

Our network transformation is making integration a reality and we are building capability to deliver competitive advantage, leverage scale and reduce costs. We are creating a world class set of assets unmatched by our competition.

Our key productivity metrics continued to improve as we remove complexity and inefficiency. Technician productivity is up 17%, customer revisits are down 36% and we are equipping our staff with the skills required in the new Telstra.

We built top line momentum with a strong second half underlying sales performance. As we foreshadowed, transformation spend peaked this year as we invested in future revenue growth, simpler systems and world class networks to provide customers with compelling content, applications and integrated services. The benefits are already starting to emerge as customers vote with their wallets and we win where it matters – in the market.

Our strong performance was achieved despite the regulator helping our competitors. Notwithstanding the unlevel playing field, we will continue to compete hard and win in the market. We will continue to develop our long-term strategy to maximise the value of integrated assets as we become a true media communications player.

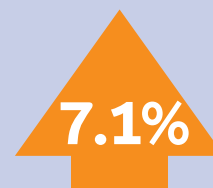
The new Telstra is about adding value to our customer's lives.

### KEY ACHIEVEMENTS:

- ✓ **launched world leading Next G™ mobile broadband network in October 2006**
- ✓ **launched Next IP™ network in April 2007**
- ✓ **3G market leader, 4 months ahead of schedule**
- ✓ **2 million 3G and over 1 million Next G™ customers**

### KEY FINANCIALS:

	2007 \$m	change %
<b>Sales revenue</b>	<b>23,673</b>	<b>4.2</b>
<b>EBITDA</b>	<b>9,861</b>	<b>3.0</b>
<b>EBIT</b>	<b>5,779</b>	<b>5.1</b>
<b>Free cash flow</b>	<b>2,899</b>	<b>(36.7)</b>
<b>Ordinary dividends (cents per share)</b>	<b>28</b>	<b>-</b>



**EBIT**

(excludes Trading Post write-down)

**We are changing the way we communicate with shareholders - for more information see the enclosed flyer**



# Earnings momentum gathers pace...

The results for the financial year ended 30 June 2007 signal the beginning of the financial turnaround as the transformation starts to drive real benefits across the business. Our profit for the year grew 2.9% to \$3.3 billion.

The first half momentum gathered pace in the second half, and for the full year our underlying earnings before interest and tax (EBIT) grew 7.1% (excluding the \$110 million Trading Post write-down) as we restored positive earnings growth.

Sales revenue increased 4.2% to \$23.7 billion. We continued to win in the key markets of mobiles, broadband and Sensis and further slowed the decline in fixed line revenue through our market-based management initiatives.

Profitability was up, driven by strong revenue growth and a decline in the labour expense, partially offset by an increase in operating expenses (before depreciation and amortisation). Costs associated with driving mobile and broadband growth, Trading Post write-down and additional expenses relating to various acquisitions not included in the prior year expenses increased operating expenses by 4.4% to \$14.1 billion.

Our balance sheet remains strong with net assets of \$12.6 billion as we maintain flexibility to react to market conditions.

The financial year was our peak capital expenditure year as we invested in transforming the business, including the launch of the world class Next G™ and Next IP™ networks. As a result free cash flow declined \$1.7 billion to \$2.9 billion.

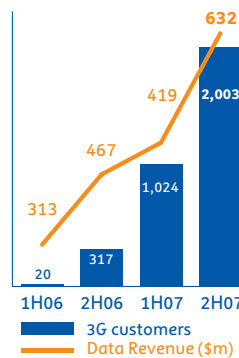
We declared a final fully franked ordinary dividend of 14 cents per share, bringing total ordinary dividends declared for the financial year to 28 cents per share.

## Mobiles

We have added over one million Next G™ customers since its launch in October. The simplicity and compelling integrated content, applications and services offered on the Next G™ network combined with the strong 3G customer growth increased data revenue by 50% to \$1.1 billion. Data now accounts for around 20% of total mobile revenue driven by:

- Number of SMS messages sent increasing by 62% to just under 5 billion;
- Non SMS data revenue up 92% driven by increased data usage following the launch of the Next G™ network, in particular increased use of laptop data cards.

Aside from data cards, non SMS revenue was driven by our active data customers increasing 28% since the launch of Next G™, Foxtel mobile streamed minutes tripled in the second half and video call minutes of use increased 40% to 580,000 minutes.

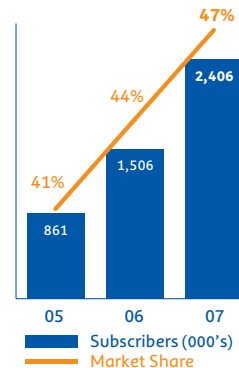


**13.9%**  
Mobile revenue increased 13.9% driven by speed, coverage and content advantage in 3G, with 1.7 million customers taking up 3G services in the year.

## Broadband

During the financial year we added a further 900,000 customers to Australia's leading internet service provider, BigPond®, an increase of 60%. At the end of the financial year, we had 2.4 million customers.

BigPond® services continued to innovate. We recently entered the web 2.0 world with the launch of I-Pond™, created the largest virtual universe amongst real world brands via our Second Life presence and recently launched on-demand mobile TV with BigPond® TV.



**66%**  
Retail broadband revenue grew 66% to \$1.2 billion with market share growing 3 percentage points to 47%.

## FINANCIAL HIGHLIGHTS

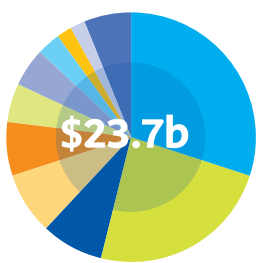
Year ended 30 June	2007 \$m	2006 \$m	change \$m	change %
Sales revenue	23,673	22,712	961	4.2
EBITDA <sup>(1)</sup>	9,861	9,575	286	3.0
EBIT <sup>(1)</sup>	5,779	5,497	282	5.1
Free cash flow	2,899	4,579	(1,680)	(36.7)
Ordinary dividends (cents per share) <sup>(2)</sup>	28	28	-	-

(1) includes transformation related costs.

(2) 2006 includes a 6 cent per share special dividend paid with the interim dividend.

## Revenue

### Sales Revenue



Segment	Revenue (\$m)	% total revenue
PSTN	\$7,190m	30%
Mobiles	\$5,701m	24%
Sensis	\$1,968m	8%
International	\$1,921m	8%
IP & data access	\$1,627m	7%
Retail broadband	\$1,213m	5%
Business services & applications	\$1,053m	5%
ISDN	\$749m	3%
Wholesale broadband	\$568m	2%
Pay TV bundling	\$344m	2%
Other	\$1,339m	6%

**4.2%**

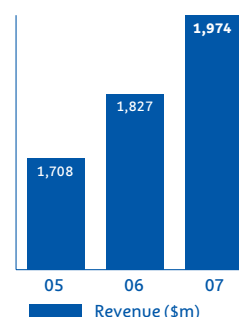
Sales revenue grew 4.2%, ahead of our full year guidance of 2.5% to 3.0%. Our Australian operations were strong, with underlying sales revenue up 3.5% for the year.

## Sensis

Sensis had another strong year of revenue growth. The directories business grew 4% to \$1.5 billion. Yellow Pages® directory revenue increased 2.6% to \$1.2 billion and White Pages® directory revenue increased 9.6% to \$331 million.

Our emerging businesses delivered another strong result, and accounted for 40% of the total Sensis growth. Whereis® location and navigation revenues grew by 75% and Sensis MediaSmart® display advertising revenues grew by 93%.

The classifieds business revenue declined 12%, with print revenue down and online revenue up – which is consistent across the industry.



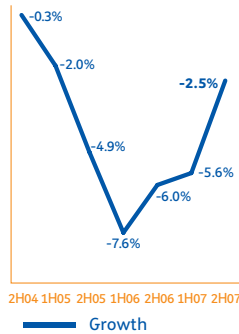
**8%**

Sensis total revenue increased 8.0%, driven by our directories, emerging businesses and \$49 million contribution from SouFun.

## PSTN

PSTN revenue declined 4.1% to \$7.2 billion, and slowed to a decline of 2.5% in the second half. This represents the third consecutive half the PSTN revenue decline has slowed – a 5 percentage point improvement over the past 18 months.

Our PSTN line loss trends are truly world class. We added 54,000 residential customers during the year, losing 1,000 customers in the first half and grew customers by 55,000 in the second half. Our market based management led initiatives such as subscription based pricing and value based segmented offers is helping deliver a more tailored customer experience which is flowing through to the financials.



**4.1%**  
PSTN revenue decline slowed to 4.1% and we added residential customers for the year, a world class performance.

## Expenses

Selected items from the <b>INCOME STATEMENT</b>			
Year ended 30 June	2007 \$m	2006 \$m	change %
Labour	4,017	4,364	(8.0)
Goods and services purchased	5,151	4,701	9.6
Other expenses	4,924	4,427	11.2
Total operating expenses	14,092	13,492	4.4
Depreciation and amortisation	4,082	4,078	0.1
Total expenses	18,174	17,570	3.4

Labour costs decreased 8% to \$4 billion as the workforce reduction initiatives start to flow into the financials. The overall workforce declined a further 1,887 during the year and has fallen 5,746 since June 2005 (excluding any impact from any acquisition and divestment activity over the past 2 years).

Salary and associated costs were flat and redundancy costs decreased 72% as the majority of the \$186 million provision raised at the end of last financial year was used to fund the redundancies in the current year.

Goods and services purchased increased 9.6% as we invested in the mobile market. The main drivers of this increase were:

- increased marketing campaign around the launch of the Next G™ mobile broadband network in October;
- costs of acquiring and retaining customers through the subsidisation of higher value 3G mobile handsets;
- higher volumes associated with the strong growth in both 3G and broadband customers.

**9.6%**

Goods and services purchased up 9.6% to support the increased volumes which have driven revenue growth, in particular 3G and broadband.

This was partially offset by a fall in the costs we pay other telecommunication providers to finish (terminate) a call on their network. The biggest driver of this fall was when the ACCC dropped the mobile terminating rate from 18 cents per minute to 15 cents per minute.

Other expenses increased 11.2% to \$4.9 billion. The main drivers of this include:

- service contracts and agreements increased 18.6% driven by IT costs related to the transformation and extra call centre staff to respond to the increased volumes flowing from the rise in 3G and broadband customers including activation of services and billing enquiries;
- promotions and advertising costs increased 18.5% relating to BigPond® and Sensis campaigns and launch of the Next IP™ network;

- general and administrative costs increased 19.8% as we invested in training and equipping our staff with the right skills to serve our customers including the opening of the Telstra Learning Academy, transformation costs and accommodation costs such as power and maintenance costs associated with operating multiple mobile telephone networks;
- write-down of the Trading Post mastheads.

Depreciation and amortisation (D&A) was relatively flat, but if transformation related accelerated D&A is excluded then D&A grew 3.5%. This increase was expected following the launch of the \$1.1 billion Next G™ mobile network in October and launch of the \$1.5 billion Next IP™ core network in April this year, with more enhancements to come.

## Balance sheet

Selected items from the <b>BALANCE SHEET</b>			
As at 30 June	2007 \$m	2006 \$m	change \$m
Current assets	5,353	4,899	454
Property, plant & equipment	24,607	23,592	1,015
Total non-current assets	32,522	31,325	1,197
Total assets	37,875	36,224	1,651
Total liabilities	25,295	23,390	1,905
Net assets/equity	12,580	12,834	(254)

Total assets increased \$1,651 million due to the net impact of:

- a \$1,015 million increase in property, plant and equipment as we invested in new networks including the Next G™ and Next IP™ networks as part of the transformation;
- a \$449 million increase in other intangibles mainly due the development and acquisition of software assets as part of the IT transformation;

The increase in total liabilities of \$1,905 million was due to the net impact of:

- a \$938 million increase in total borrowings to help fund our capital expenditure requirements in this, our peak transformation capital investment year and to pay dividends;
- a \$774 million increase in other current liabilities, including accruals and payables due to higher levels of construction activity as part of our network and IT system transformation.

## Cash flow

Selected items from the <b>CASH FLOW STATEMENT</b>			
Year ended 30 June	2007 \$m	2006 \$m	change \$m
Net cash provided by operating activities	8,520	8,553	(33)
Capital expenditure	(5,982)	(4,303)	(1,679)
Free cash flow	2,899	4,579	(1,680)

Free cash flow declined \$1,680 million to \$2,899 million mainly due to:

- a \$1,397 million increase in capital expenditure as we invested in the transforming our business to provide our customers with better applications and services including the construction of the Next G™ and Next IP™ networks and upgrading our IT systems;
- a \$282 million increase in investing cash flows as we acquired 55% (on an undiluted basis) of the issued capital in SouFun, a leading real estate web site in China;

We used our free cash flow to:





- pay dividends to our shareholders totalling \$3,479 million, representing 28 cents per share;
- pay finance costs of \$1,056 million to our debt holders.

## Outlook

At the end of the financial year, we were only 19 months into our 5 year transformation strategy announced back in November 2005. Fiscal 2007 was the peak transformation spend year as we invested in building next generation platforms to reduce complexity and improve our customer experience.

We have laid a solid foundation since we started the transformation, but the company is experiencing a combination of regulator driven wholesale price reductions and Government subsidisation of competitors, and as a result, we have set prudent guidance and in fiscal 2008 we expect: revenue growth of between 2.0% to 3.0%, EBITDA growth of between 2.0% to 3.0% and EBIT growth between 3.0% to 5.0%.

# Transformation: Building world class capability

	STATUS	PROGRESS
<b>Next G™ network</b> Completed construction of the World's largest and fastest national mobile broadband network.	 LAUNCHED	<ul style="list-style-type: none"> <li>launched in October 2006</li> <li>over 1 million customers on the Next G™ network</li> <li>upgrade speeds for data cards to 7.2Mbps by end of calendar year 2007</li> </ul>
<b>Next Generation Network</b> Completed construction of the world class Next IP™ core network which is secure, scalable to improve network reliability and increase the services offered to customers.	 LAUNCHED	<ul style="list-style-type: none"> <li>launched core network in April 2007</li> <li>capped or exited a further 124 network platforms</li> <li>80%+ of Telstra's corporate and enterprise IP WAN networks now supported by Telstra's Next IP™ network</li> </ul>
<b>Simpler systems</b> Reducing and simplifying systems will deliver improved customer experience and lead to cost savings and efficiencies.	 ON TRACK	<ul style="list-style-type: none"> <li>exited a further 132 IT systems</li> <li>on track to achieve 80% target reduction by end of fiscal 2010</li> <li>deployed integrated desktop providing a single log in to our front of house systems, reducing log in time by 60%</li> </ul>
<b>Market Based Management</b> MBM puts the customer at the centre of everything we do and helps Telstra tailor products and services to the customer needs.	 ONGOING	<ul style="list-style-type: none"> <li>subscription pricing plans for consumer and business customers launched</li> <li>outbound strike rates have doubled with the use of segmented based offers and words that work</li> <li>rolled out 65 new branded retail locations, including the first dedicated Telstra Business Centre</li> </ul>
<b>Workforce excellence</b> Investing in our people to better serve our customers' needs.	 ON TRACK	<ul style="list-style-type: none"> <li>trained over 12,000 staff at the Telstra Learning Academy in first 11 months</li> <li>technician productivity up 17%</li> <li>customer revisits down 36%</li> </ul>

## Update on Telstra's high-speed broadband plan

Telstra remains firmly committed to investing in new infrastructure to provide Australians with world class telecommunications services. High-speed broadband is critical to Australia's future economic prosperity and social wellbeing.

Over the past two years, Telstra has put forward three separate, detailed high-speed broadband plans for Australia. The first plan was rejected by the Government; the second was not supported by the ACCC; and the third was rejected by the Government, after being blocked by the ACCC. Despite these setbacks, Telstra and its many supporters remain undaunted.

The Government has now established an Expert Taskforce to consider proposals to build a Fibre-to-the-Node (FTTN) network to deliver high-speed broadband. As the only company with a fully-developed FTTN plan, Telstra will participate in the review if it is conducted in a rigorous and objective way. However we will not get bogged down in a process that is not going to deliver a timely outcome.

Australia already lags behind other leading countries in the developed world in broadband penetration and speeds. With new fibre networks already planned for many other countries, Telstra feels a sense of urgency to deliver high-speed broadband to Australia. This sense of urgency is shared by our business customers,

and the increasing numbers of consumers who are demanding broadband.

We owe it to our shareholders to make sound and timely investments. In the meantime, we will continue to explore all the options we have to better serve our customers, wisely invest our shareholders savings, and serve the national interest.

### Help us protect your investment

We welcome shareholder's support and help to make Telstra's high-speed broadband plan a reality. Shareholders are especially invited to join our Telstra Active Supporters group where people who share Telstra's interests come together to voice their concerns and take positive action.

For more information, to register as a Telstra Active Supporter and to keep up to date with events as they happen, please visit our website: [www.nowwearetalking.com.au](http://www.nowwearetalking.com.au)



## Mini glossary

**ACCC** Australian Competition and Consumer Commission.

**ADSL** Asymmetric Digital Subscriber Line – is a broadband technology that provides access to the Internet at fast speeds.

**FTTN** Fibre to the node – infrastructure that delivers fibre close to the customer premises. FTTN can deliver broadband data and potentially television services to customer premises.

**IP** Internet Protocol – is a standard set of rules for the carriage of digital information such as voice, video, data and images, across a global network.

**IP core** The core element of a network which carries and logically splits voice, data and video using IP technology.

**Next G™ network** Telstra's trade mark name for its 3GSM 850 mobile network.

**PSTN** Public Switched Telephone Network - standard home telephone service, delivered over underground copper wires.

**ULL** Unconditioned Local Loop – The Local Loop is the copper wire that connects the Telstra exchange in your area to your house. Telstra is required to provide access to this wire to other operators.

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[www.telstra.com.au/abouttelstra/investor](http://www.telstra.com.au/abouttelstra/investor)

Telstra's interactive advocacy website:

[www.nowwearetalking.com.au](http://www.nowwearetalking.com.au)

## Key upcoming dates for 2007

Ex-dividend share trading commences	20 Aug
Record date for final dividend	24 Aug
Final dividend paid	21 Sep
Annual General Meeting	7 Nov

Note – Timing of events may be subject to change. Any changes will be notified to the Australian Stock Exchange (ASX).

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