

Letter to Shareholders

Dear Shareholder

Telstra today announced a new strategy to lead the Australian market by simplifying its operations and product set, improving customer experience and reducing its cost base.

The strategy, named Telstra2022, has four key pillars:

- Radically simplify our product offerings, eliminate customer pain points and create all digital experiences
- Establish a standalone infrastructure business to drive performance and set up optionality post the nbn rollout
- Greatly simplify our structure and ways of working to empower our people and serve our customers
- Industry leading cost reduction programme and portfolio management

The changes form a three-year plan building on the strategic investments Telstra announced in 2016.

We have attached the market release to this letter which provides further information. Material from the day including the presentations and videos can also be found at www.exchange.telstra.com

On behalf of the board and management, we would like to thank you for your loyalty as a Telstra shareholder. We understand there are challenges in the short term but we remain confident of the long-term outlook for our company and believe the changes we are making will help ensure Telstra's success in the future.

Members of our management team will be speaking about these important changes at our retail shareholder information meetings which will be held in September this year. We encourage our shareholders to attend in person where possible or watch the Melbourne event which will be webcast live online at www.telstra.com.au/shareholdermeetings

The details are as follows:

Date	Time (local)	Location
17 September	10am – 12pm	MELBOURNE: Grand Hyatt – 123 Collins Street
18 September	10am – 12pm	BRISBANE: Hilton Hotel – 190 Elizabeth Street
20 September	10am – 12pm	ADELAIDE: Hilton Hotel – 233 Victoria Square
21 September	10am – 12pm	PERTH: Hyatt Hotel – 99 Adelaide Terrace

To register, please visit www.telstra.com.au/shareholdermeetings or email shareholder.meetings@team.telstra.com

As always, we welcome your feedback which can be given through our Investor Relations Department who can be reached via email at investor.relations@team.telstra.com, via the phone on 1800 880 679 or by writing to Level 28, 242 Exhibition Street, Melbourne VIC 3000.

A handwritten signature in black ink, appearing to read "John P Mullen".

John P Mullen
Chairman

A handwritten signature in blue ink, appearing to read "Andrew R Penn".

Andrew R Penn
CEO and Managing Director

20 June 2018



Telstra sets new strategy to improve customer experience, simplify structure and cut costs

- **Creation of a new wholly owned infrastructure business unit, 'InfraCo' to drive performance and provide future optionality for a demerger or the entry of a strategic investor in a post-nbn rollout world**
- **Radical transformation of customer plans and pricing to deliver improved customer experience**
- **Increase of our productivity program by a further \$1 billion to \$2.5 billion cost out by FY22**
- **8,000 net reduction in employees and contractors and reduction in 2-4 layers of management**
- **Monetisation of up to \$2 billion in assets over the next two years to strengthen the balance sheet**
- **Telstra to remain premium brand and lead and win in 5G**
- **FY19 EBITDA guidance¹ of \$8.7 - \$9.4 billion expected excluding restructuring costs of approximately \$600 million**

Wednesday 20 June 2018 – Telstra today announced a new strategy to lead the Australian market by simplifying its operations and product set, improving customer experience and reducing its cost base.

The strategy, named Telstra2022, has four key pillars:

- Radically simplify our product offerings, eliminate customer pain points and create all digital experiences
- Establish a standalone infrastructure business to drive performance and set up optionality post the nbn rollout
- Greatly simplify our structure and ways of working to empower our people and serve our customers
- Industry leading cost reduction programme and portfolio management

The changes form a three-year plan building on the strategic investments Telstra announced in 2016.

Telstra CEO Andrew Penn said the strategy would fundamentally change the nature of telecommunication products and services in Australia by eliminating many pain points for customers.

"We will take a bolder stance and use the disruption in the telecommunications industry to lead the market for the benefit of our customers, employees and shareholders," Mr Penn said.

"The rate and pace of change in our industry is increasingly driven by technological innovation and competition. In this environment traditional companies that do not respond are most at risk. We have worked hard preparing Telstra for this market dynamic while ensuring we did not act precipitously. However, we are now at a tipping point where we must act more boldly if we are to continue to be the nation's leading telecommunications company."

A consequence of the plan is an expected net reduction in employee and contractor numbers of 8,000, including removing one in four executive and middle management roles to flatten the structure.

"We are creating a new Telstra that is able to continue to lead the market. In the future our workforce will be a smaller, knowledge-based one with a structure and way of working that is agile enough to deal with rapid change. This means that some roles will no longer be required, some will change and there will also be new ones created," Mr Penn said.

"We understand the impact this will have on our employees and once we make decisions on specific changes, we are committed to talking to impacted staff first and ensuring we support them through this period."

¹ See Footnote 4

Telstra2022 pillars

The strategy leverages the significant capabilities already being built through Telstra's up to \$3 billion strategic investment announced in August 2016 in creating the Networks for the Future and digitising the business.

"The network investments have been critical as Telstra builds capability in software defined networking and prepares to lead the market and win in 5G. We will be network ready in the first half of FY19 with full rollout to capital cities, regional centres and other high demand areas by FY20," Mr Penn said.

The Telstra2022 strategy will therefore be underpinned by the largest, fastest, safest, smartest and most reliable next generation network. The digitisation program is delivering completely new technology stacks for Consumer and Small Business and Enterprise customer segments which will be the platform for the new products we are launching."

The four pillars of the program are:

Pillar 1: Radically simplify our product offerings, eliminate customer pain points and create all digital experiences

Telstra has announced it will transform the experience of its Consumer and Small Business customers.

This will be different to anything currently in the market, addressing the need to increase the simplicity, transparency and satisfaction that customers experience with telco products today. This will see a fundamental change to the way Telstra designs products, sells services and provides customers with support. Leveraging its investment in digitisation, Telstra will simplify its products by retiring all of its more than 1,800 consumer and small business plans and instead introducing 20 core plans backed up by an effortless digital service that removes complexity and provides cost certainty – addressing key pain points for customers.

Customers will start to benefit from this simplified approach in July when Telstra launches peace of mind data across a range of new post-paid plans, making excess data charges a thing of the past. Four more major product and service experiences will be progressively announced in the lead up to June 2019, the details of which will remain confidential at present for competitive reasons.

By June 2019 Telstra customers will experience a radically simplified experience made possible by new intuitive digital platforms, with all customers being moved to the new product range by 30 June 2021.

For Enterprise customers, Telstra already offers some of the best digital solutions in the market. Telstra will continue to be the best one-stop shop for all B2B technology needs, offering customers a modular, curated, self-service and simplified product portfolio. The program to remove complexity will be accelerated to reduce the existing product portfolio by more than half within three years. The approach will also include greater emphasis on a digital-first model, supported by software-based platforms and Internet of Things. It is expected this will bolster Telstra's historical strength with large customers and enable it to push firmly into the mid-market and increase market share.

Over the past year, Telstra has built a completely new technology stack for mid-market and Enterprise customers, which will enable these changes. Telstra will use the natural momentum in the business to migrate customers to the new product suite enabling it to stop the development of products on legacy systems, and aggressively rationalise old applications and services.

Pillar 2: Establish a standalone infrastructure business to drive performance and set up optionality post the nbn rollout

Effective from 1 July, Telstra will create a wholly owned standalone infrastructure business unit. It will have its own CEO reporting to Mr Penn. The business unit, called Telstra InfraCo will comprise Telstra's high quality fixed network infrastructure including data centres, non-mobiles related domestic fibre, copper, HFC, international subsea cables, exchanges, poles, ducts and pipes. Its services will be sold to Telstra, wholesale customers and nbn co.

Telstra InfraCo will also comprise Telstra's nbn co commercial works activities and Telstra Wholesale, with a total workforce of approximately 3,000. It is expected this new Business Unit will control assets with a book value of about \$11 billion and have annual revenues and EBITDA of about \$5.5 billion and \$3 billion respectively.

"As technology innovation is increasingly relying on connectivity, the role of telecommunications infrastructure is becoming more important. There is virtually no technological innovation happening today that does not rely on a high quality, reliable, safe and secure telecommunications network. In this

world our infrastructure assets are becoming more valuable. By creating a new infrastructure focused business unit we will better optimise and manage these assets," Mr Penn said.

The new business unit will not include the mobile network assets including spectrum, radio access equipment, towers and some elements of backhaul fibre, which will remain integrated with Telstra's core customer segment focused business to support the company's network differentiation. This is particularly important for Telstra's mobiles business as it executes its 5G strategy.

The new infrastructure business unit will provide more flexibility and transparency in the management of Telstra's underlying infrastructure. Amongst other things, the arrangements will reinforce the discipline with which capital allocation occurs across the group.

Importantly, Telstra InfraCo will provide significant optionality for Telstra in the future for a potential demerger or the entry of a strategic investor once the nbn rollout concludes.

Telstra's H1 FY19 financial statements will contain detailed segment reporting for Telstra InfraCo.

Pillar 3: Greatly simplify our structure and ways of working to empower our people and serve our customers

Telstra will implement a new streamlined operating model and organisational structure to be announced in July. Ways of working are being simplified and re-aligned to increase the focus on best serving customers, increasing the focus on product leadership, breaking down silos and enabling the sizeable transformation to which Telstra is committing today.

In addition to Telstra InfraCo, one of the first changes to come into effect will be the creation of the Telstra Global Business Services group, also reporting to Mr Penn. This group will be a point of consolidation for all large scale "back of house" processes and functions using technology to reduce costs for large repeatable functions.

Telstra also intends to elevate its focus and capabilities in product development and management across the company increasing the leverage and sharing of technical efforts across all customer segments.

The implementation of Telstra Global Business Services combined with accelerated simplification of processes, moving to more agile ways of working and product simplification is expected to lead to an overall reduction in labour costs of around 30 per cent. This will result in a net reduction of 8,000 employees and contractors over the next three years. The initial focus will be on the reduction of executive and management roles and minimising any impact on customer facing teams. Telstra will also invest in approximately 1,500 new roles to build new capabilities required for the future, in particular the shift to new engineering capabilities including software engineering and information and cyber-security.

Recognising the significant impact these changes will have on employees, Telstra also announced two new programs. A Transitions Program for those leaving Telstra will provide enhanced outplacement support. For those remaining, Telstra will provide support to upskill and transition to new ways of working in a leaner and more agile organisation. To support the programs Telstra intends to make available initial funding of up to \$50 million.

Pillar 4: Industry leading cost reduction programme and portfolio management

Two years ago, Telstra narrowed its strategy to ensure all new growth investments were more closely focused on products and services close to the core of the business. Since then decisions have been made not to pursue international consumer opportunities such as in the Philippines, to sell the investment in Autohome for \$2.4 billion, to restructure the investment in Foxtel and to streamline the health business and Ooyala.

Telstra intends to monetise assets of up to \$2 billion over the next two years to strengthen the balance sheet. It is also increasing its target for its productivity program by a further \$1 billion to reduce underlying core fixed costs by \$2.5 billion by FY22. We expect Telstra's total costs will remain flat or reduce despite absorbing more than \$1.5 billion of increased nbn AVC/CVC costs that will be incurred as we migrate to the nbn.

The key drivers of the increased productivity targets include simplifying the product set, phasing out legacy products and systems and migrating customers to new products. Other drivers include further digitising sales and service channels and continuing to improve procurement practices.

Benefits

The Telstra2022 strategy will deliver benefits for all stakeholders - customers, shareholders and employees and will ensure that Telstra remains Australia's premium and most trusted brand in telecommunications.

It has six specific goals with tangible and clear milestones covering customer experience, simplifying the business, network superiority, people, cost improvements and strengthening the balance sheet. Details include:

- Reducing the number of consumer and small business plans from 1,800 to 20.
- Migrating all consumer and small business products and plans and 50 per cent of enterprise customers to completely new technology stacks within three years and leave the legacy behind.
- Establishing a standalone infrastructure business unit to drive improved performance and create optionality for the future including a potential demerger or the entry of a strategic investor post the rollout of the nbn.
- Reducing 2-4 layers of management across the organisation.
- Eliminating the need for one third of customer service calls within two years and two thirds by FY22.
- Leading in all key industry surveys for network performance.
- Increasing our productivity program by a further \$1 billion to \$2.5 billion by FY22.
- Monetising up to \$2 billion in assets over the next 24 months to strengthen the balance sheet.

The cost out target adds a further \$1 billion in productivity to Telstra's current announced target of \$1.5 billion taking core non DVCs from \$7 billion in 2017 to \$4.5 billion by 2022. Telstra expects to incur additional restructuring costs of approximately \$600 million in FY19 and further restructuring costs across the remaining years of the program including the potential acceleration of depreciation and amortisation from the early shutdown of legacy systems.

Telstra is committed to the previously announced more than \$500 million of incremental benefits from its strategic investment program. Telstra2022 would not have been possible without these investments.

Telstra confirms there is no change to its capital management framework and expects its capex to sales ratio to be 16 to 18 per cent in FY19.^{2,3} Capex to sales over the medium term is expected to be 14 per cent.^{2,3}

Mr Penn said Telstra2022 was developed in response to anticipated changing market dynamics, which initiated the investments announced in 2016.

"The Australian telco market is entering an extremely challenging period driven by a number of factors including the nbn transition and increased mobile competition. We are seeing this play out in our financial performance and therefore the impact on the economics of the company are very significant. Against that background, we announced in May that FY18 earnings will be at or around the bottom end of guidance. We expect the trends to continue in to FY19. In our guidance for FY19 we have assumed the market will decline 2 to 3 per cent in mobile and fixed revenue," he said.

Telstra advised the transition under the program is also likely to eliminate up to \$500 million in revenues for its services over the next three years, with excess data charges being the first example. However, over the longer term Telstra believes these moves are in the best interests of customers as they accelerate a trajectory already underway and will drive long-term value. They are expected to be more than offset by more services per customer and lower costs from simplicity and leadership shown by Telstra translating into new sources of growth.

"These trends are not dissimilar to that which we have seen in global telecommunications markets, including the US and Europe particularly after the entrance of new mobile operators," said Mr Penn.

² Capex is measured on an accrued basis and excludes expenditure on spectrum and externally funded capex.

³ The guidance assumes the nbn™ rollout and migration in FY19 is broadly in accordance with management's current best estimates and may be updated for any material changes, including after taking account of the nbn Corporate Plan 2019 when it is published.

Telstra also provided the following financial guidance for FY19⁴.

- Income to be in the range of \$26.6 billion to \$28.5 billion
- EBITDA to be in the range of \$8.7 billion to \$9.4 billion (before restructuring costs of approximately \$600 million)
- Net one-off Definitive Agreements receipts less nbn net cost to connect in the range of \$1.8 billion to \$1.9 billion
- Restructuring costs of approximately \$600 million
- Capex to be in the range of \$3.9 billion to \$4.4 billion

Telstra's dividend policy is set out in its capital management framework and is to pay a fully franked ordinary dividend of 70 to 90 per cent of underlying earnings^{5,6} and return in the order of 75 per cent of net one-off nbn receipts over time via fully franked special dividends.^{7,6}

While Telstra does not provide forward guidance on the dividend, it is reconfirming today that the total dividend for FY18 will be 22 cents per share⁶. Dividend decisions for FY19 will be announced in FY19.

Mr Penn said he was confident the strategy would set Telstra up well for the future.

"Customers will have more choice than ever in a post-nbn world with increasing mobile competition. We are committed to leading the market in a period of transition and positioning ourselves to create a strong platform for growth. At its core, this strategy is about placing customers at the centre of everything we do and delivering simpler, more flexible products with a beautiful digital service experience," he said.

Media contact: Jon Court, +61 (0) 408 423 516

Email: media@team.telstra.com

Investor contact: Nathan Burley, +61 (0) 457 529 334

Email: investor.relations@team.telstra.com

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⁴ This guidance also assumes wholesale product price stability and no impairments to investments, and excludes any proceeds on the sale of businesses, mergers and acquisitions and purchase of spectrum. The guidance also assumes the nbn™ rollout and migration in FY19 is broadly in accordance with management's current best estimates and may be updated for any material changes, including after taking account of the nbn Corporate Plan 2019 when it is published. The guidance is provided on a consistent basis with FY18 accounting standards. Guidance will be updated during FY19 to be consistent with IFRS15 under which we will report FY19 results. Capex is measured on an accrued basis and excludes expenditure on spectrum and externally funded capex.

⁵ Underlying earnings is defined as NPAT from continuing operations excluding net one-off nbn receipts (as defined in footnote 6).

⁶ Return subject to no unexpected material events, assumes the nbn rollout and migration is broadly in accordance with management's current best estimates, and is subject to Board discretion having regard to financial market conditions, business needs and maintenance of financial strength and flexibility consistent with Telstra's capital management framework.

⁷ "net one-off nbn™ receipts" is defined as net nbn one off Definitive Agreement receipts (consisting of PSAA, Infrastructure Ownership and Retraining) less nbn net cost connect less tax.