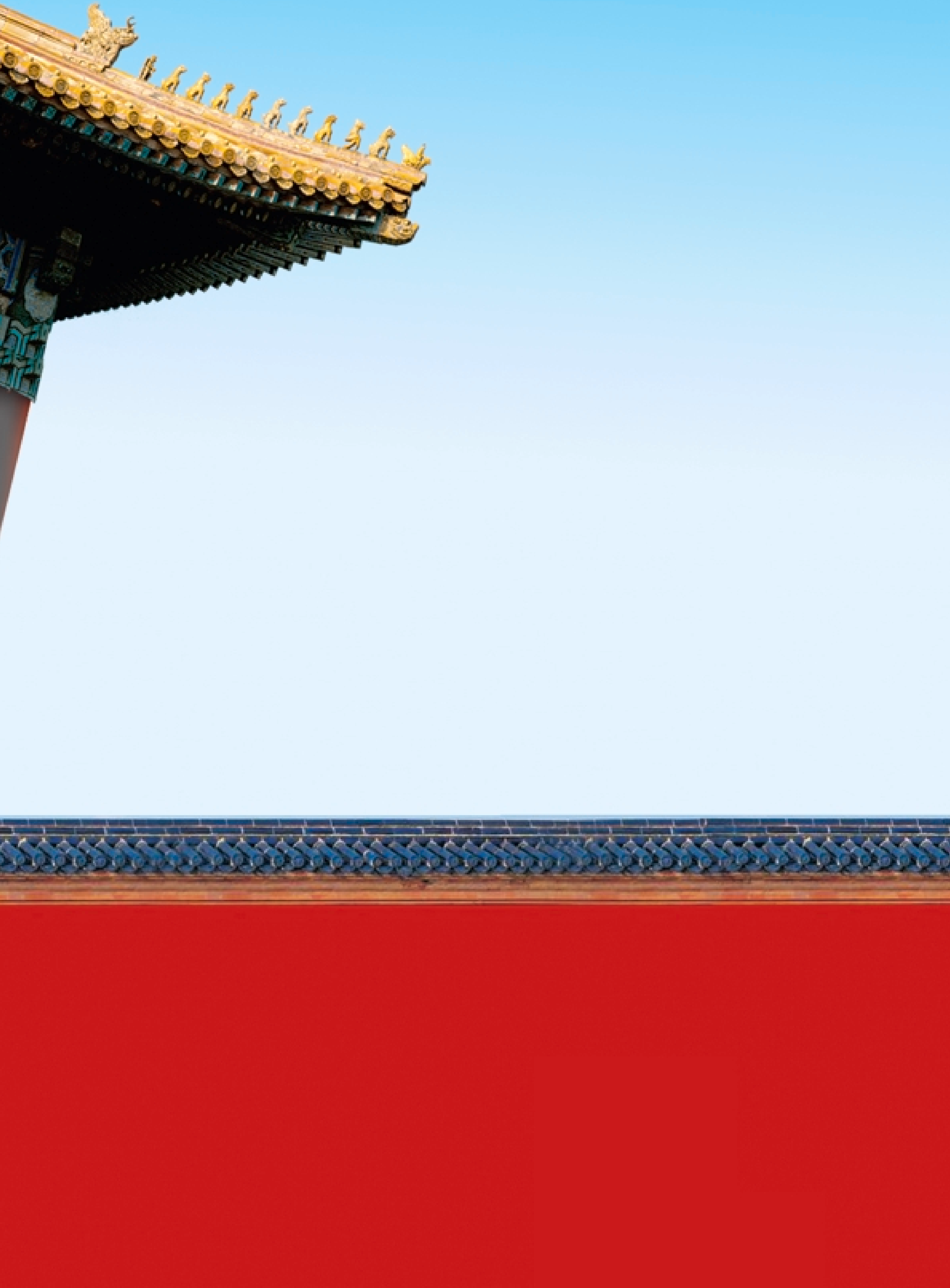
# 2007 Interim Report


北京2008年奧運會合作夥伴
OFFICIAL PARTNER OF THE BEIJING 2008 OLYMPIC GAMES

**China Netcom Group Corporation (Hong Kong) Limited**

(incorporated in Hong Kong with limited liability
under the Companies Ordinance)

HKSE : 906 NYSE : CN



# Contents

# Chairman's Statement

Dear Shareholders,

In the first half of 2007, the Company continued to proactively pursue its strategic transformation to become a "broadband communications and multimedia services provider" and achieved remarkable results. Revenue from our high-growth businesses grew rapidly at a growth rate of 39.4% in the first half of 2007, reaching RMB13,029 million. We are confident that the Company will persistently increase value for its shareholders as we progress towards our strategic goals.

## Strategic Transformation

China's telecommunications industry has experienced a drastic turn since 2006. As a result of increasing mobile substitution, fixed-line operators have seen revenue growth slow down drastically and in some cases all but disappear. The trend was further accelerated in the first half of 2007 as mobile telecommunications services providers continued to aggressively adjust their tariff and marketing strategies, prompting us to accelerate our transformation.

As you know by now, this transformation strategy is focused on "broadband and broadband-enabled services". Leveraging technological progress and network convergence, the Company is committed to deliver broadband access and bandwidth-intensive content and applications to individual customers and ICT services to business customers to meet changing market demand. We aim to become a "leading ICT service provider in China" and a "network information & communication expert" for our government and corporate customers.

In the first half of 2007, our strategic transformation progressed satisfactorily. Our broadband subscriber base continued to grow rapidly. The total number of broadband subscribers increased from 12,968 thousand in the same period last year to 17,123 thousand, representing an increase of 32.0%. Revenue from ICT services contributed 3.5% towards total revenue, while the contribution of the high-growth businesses towards total revenue grew to 32.0% from 23.1% a year earlier, representing an increase of 8.9 percentage points.

As a century-old traditional telecommunications operator we are facing unprecedented challenges in our transformation. As we move from a fixed-line, voice centric focus into the new broadband content and applications and IT regimes, we are facing new competitors that are technologically ahead and have accumulated extensive market experience. We need to create demand and anticipate changing customer needs effectively, innovate faster, master marketing techniques and customer service and use all our resources more effectively so we can fund our future while continuing to increase shareholder value. Our organizational structure and corporate culture need to change so that we can reinforce our core competitiveness in this new environment. I am confident that we have the necessary vision, the ability and the will to reform ourselves and inject vitality into this time-honored company.

## Olympic Opportunities

As an official partner of the Beijing 2008 Olympic Games, we have shaped and pursued our "Broadband Olympics" vision to make the Beijing 2008 Olympic Games the first "Broadband Olympics" and "Digital Olympics" in history. After more than two years of intense preparation, we are close to turning our vision into reality. On July 25, 2007, we launched the "Broadband Olympics" products series, which enable us to best meet customer demand for network stability, security and convenience to the fullest possible extent and more importantly, to create demand and satisfy the diversified needs of our subscribers for Olympics-related telecommunications, content and applications, and IT support services, and to promote rapid growth in the broadband and ICT businesses. These products address the diversified needs of all our customers and provide:

- Convenient, high-speed and reliable Internet access through a seamless network and include Olympic broadband cards which provide users with high-speed Internet access anytime anywhere; VLAN-based private networks for news agencies with real-time multimedia feeds; and Olympic high-definition video transmission;
- Diversified and exclusive broadband contents to our subscribers to stimulate and satisfy the demand for Olympics-related content and applications of the public. e.g., CNC MAX Olympic channel, "Hello 2008" Olympic content push.
- Reliable telecommunications and high quality integrated solutions to BOCOG and the media, and integrated solutions to business customers looking to grow and build their brands through the Olympics. Our products include Olympic Call Center, Olympic Network Surveillance System, Olympic Events Management System, Olympic Fixed-line Telecommunications Command System, 2008 Smart Traffic, and 2008 Convenient Medicare.

# Chairman's Statement

As our Olympic products allow our individual customers to learn, experience and enjoy our Olympic telecommunications services, we expect to gain recognition as a high quality and reliable "broadband communications and multimedia services provider". Furthermore, the Olympics are a unique opportunity to enhance our ability to offer IT-CT integrated solutions to government and corporate customers and establish ourselves as a "leading ICT service provider in China" while providing comprehensive and high quality telecommunications solutions to BOCOG, the media and our business customers.

The implementation of our "Broadband Olympics" vision will help us achieve great progress in our transformation into a "broadband communications and multimedia services provider".

## Corporate Governance Improvement

In the first half of 2007, the Board continued to refine the Company's corporate governance. Based on the results of the performance assessment of the Board and its Directors in 2006, the Company has developed a focused plan to enhance the performance of the Board. A specific training program will allow both internal and external Directors to gain a deeper understanding of the Company's operations and of their responsibilities and obligations under the rules of the various stock exchanges where the shares of the Company are listed. The Board has also begun in-depth research in areas such as Director selection and succession procedures, as well as management succession planning and compensation. This will allow the Company to develop open and transparent Director selection and succession processes and more effectively appraise the performance and potential of senior executives.

## Changes of Directors and Management

On July 12, 2007, Dr. Edward Tian Suning resigned from his positions as Non-Executive Director and Vice President as well as member of the Strategy Committee of the Board. On the same day, Mr. Miao Jianhua also resigned from his positions as Executive Director and Chairman and member of the Supervision Committee of the Board. On the same day, Ms. Li Jianguo was appointed Executive Director and Chairman and member of the Supervision Committee. The Board fully acknowledges and value the outstanding contributions made by Dr. Edward Tian Suning and Mr. Miao Jianhua during their service on the Board, and welcome Ms. Li Jianguo as a member of the Board.

## Prospects

In the second half of 2007, the Company will continue to pursue innovation and growth. In support of its transformation into a "broadband communications and multimedia services provider", the Company will continue to reform its organizational structure, operation model, human resources structure and corporate governance and reinforce core competitive advantages in a new competitive landscape. We firmly believe that only continuous innovation will enable the Company to compete and enhance value for its shareholders.

Last but not least, I would like to extend our most sincere gratitude to all of you for your support and trust.

**Zhang Chunjiang**
*Chairman*

Hong Kong, August 22, 2007

# Chief Executive Officer's Statement

Dear Shareholders,

In the first half of 2007, the major business strategies of the Company were to vigorously develop its high-growth businesses, stabilize its traditional fixed-line business, refine management quality and improve cash flow. The first half of 2007 witnessed escalating imbalances in the competitive landscape in China's telecommunications industry and intensifying mobile substitution. Although our traditional fixed-line business declined, our strategic transformation showed satisfactory results, our high-growth businesses maintained rapid growth and the ratio of free cash flow over total revenue improved.

## I. Financial Performance

In the first half of 2007, revenue from continuing operations reached RMB41,508 million, which included upfront connection fees of RMB855 million. Excluding upfront connection fees, revenue from continuing operations amounted to RMB40,653 million, an increase of 0.43% compared with the same period last year (unless otherwise specified, all figures are net of the effect of upfront connection fees and our discontinued operations). EBITDA* was RMB21,907 million and EBITDA margin was 53.9%. Consolidated net profit was RMB5,858 million, which included RMB624 million from discontinued operations. As a result of mobile substitution, revenue growth slowed down in the first half of 2007. However, our high-growth businesses continued to develop strongly. With the rapid development of new businesses such as ICT and broadband content and applications, revenue from high-growth businesses reached RMB13,029 million in the first half of 2007, an increase of 39.4% compared with the same period last year, highlighting their potential to strongly contribute to future growth.

In the first half of 2007, the Company continued to optimize its budget and CAPEX management processes. We further strengthened our control over CAPEX and increased the utilization efficiency of resources, while at the same time ensuring sufficient investments in high-growth businesses. By the end of the first half of 2007, the Company's CAPEX totaled RMB8,454 million, a decrease of 16.2% compared with the same period last year. As a result of the decrease in CAPEX, our free cash flow continued to grow, reaching RMB8,126 million, an increase of 13.3% compared to the same period last year.

## II. Business Performance

### Traditional Fixed-line Business

In 2007, the Company's development strategy for the traditional fixed-line business is to retain subscribers, stimulate voice traffic, increase ARPU and eventually stabilize its traditional fixed-line business by implementing bundled services such as "Family 1+". In April 2007, the Company completed the upgrading of its local network to embrace intelligent functions and the upgrading of its supporting systems in all service regions, and began to promote "Family 1+" bundled service on a large scale. By the end of the first half of 2007, the number of "Family 1+" subscribers reached 4,444 thousand.

The "Family 1+" bundled services mitigated the decline in the number of local telephone subscribers to a certain extent. In the first half of 2007, the Company was able to restore growth in the number of local telephone subscribers. The total number of subscribers reached 115,077 thousand, representing a net increase of 1,105 thousand from the end of 2006. The full-scale implementation of "Family 1+" bundled services also effectively stimulated the growth of our broadband subscriber base and increased usage of value-added services and broadband content and applications, thereby significantly increasing the value of our existing subscriber base.

As a result of continuous mobile substitution and the adjustments of the tariff policies adopted by mobile operators in China, in the first half of 2007, the local voice traffic of the Company dropped by 7.4% compared with the same period last year. In the second half of the year, we will undertake further market segmentation and review resource allocation and tariff model, as well as fully leverage our advantages in network resources with a view to mitigating the decline in local voice traffic.

* EBITDA refers to profit before finance costs, interests income, dividend income, deficit on revaluation of fixed assets, income tax, depreciation and amortization, share of profit of associated companies. To supplement our consolidated financial statements presented in accordance with the Hong Kong GAAP, we use the non-Hong Kong GAAP measure of EBITDA, which is adjusted from our results based on Hong Kong GAAP. We believe that EBITDA provides useful information to both management and investors to further analyze our operating results since we, as a company operating in the capital intensive telecommunications industry, incurred significant capital expenditure and finance costs which have significant impact to our results based on Hong Kong GAAP. EBITDA should only be considered in addition to our Hong Kong GAAP results. It should not be considered a substitute for or superior to our Hong Kong GAAP results as it cannot be used to measure operation results and liquidity and does not represent operation cash flows. In addition, our EBITDA may not be comparable to similar indicators of other companies.

# Chief Executive Officer's Statement

## High-growth Businesses

In 2007, the Company's development strategies for high-growth businesses are: to further increase the broadband subscriber base, to generate revenues from content and applications as well as broadband access and develop the "PC+TV" multi-terminal model; to strengthen marketing for value-added services for its fixed-line subscribers and the bundling of value-added services with basic voice service; to consolidate internal resources in order to accelerate growth in the ICT business. In the first half of 2007, as a result of sound strategic implementation, our high-growth businesses experienced sustained rapid growth. Revenue from high-growth businesses accounted for 32.0% of the Company's total revenue, up by 8.9 percentage points over the same period last year.

By the end of the first half of 2007, we had a total number of 17,123 thousand broadband subscribers, representing an increase of 32.0% over the same period last year and a net increase of 2,694 thousand compared with the end of 2006. Revenue attributable to broadband and Internet-related services increased by 33.8% over the same period last year, reaching RMB6,632 million. The ARPU of broadband services was RMB67.4, an increase of 3.4% over the same period last year.

On May 17, 2007, the Company started the trials of "CNC MAX" Navigator, aiming to provide broadband subscribers with diversified broadband content and application services with both national and local features, in the provincial capitals and Olympic cities within its service regions. "CNC MAX" Navigator was fully extended to all the service regions of the Company on August 8, 2007. In the second half of the year, with the continuous promotion of "CNC MAX" Navigator and the enrichment of the broadband content and application services offered by the Company solely or developed with partners, we expect that the penetration of broadband content and application services will be further enhanced.

In the first half of 2007, the Company increased its efforts to promote value-added services to its fixed-line subscribers and strengthen the development of "Phone Navigation" services, and launched such services as public service hotlines, call centers and product authentification service. By the end of June 2007, the number of "Personalized Ring" subscribers increased from 10,365 thousand at the same period last year to 23,911 thousand, an increase of 130.7%; the number of "Phone Navigation" subscribers reached 196 thousand. Revenue attributable to value-added services for the first half of 2007 reached RMB3,129 million, an increase of 24.2% over the same period last year.

During the first half of 2007, the Company set its long-term goal at becoming the "leading ICT services provider in China" by capitalizing on its strengths in network service, resources integration and customer relationship maintenance. Based on the size of different ICT niche markets, the Company's capabilities to meet the needs of these niche customers, and its ability to bundle and support core telecommunication businesses, the Company decided to focus on such key customer segments as governmental authorities, securities houses and educational and medical institutions, providing subscribers with long-term leases and services which the Company has competitive edges such as platform lease, network maintenance and IT outsourcing and hosting. In the first half of 2007, the Company entered into a number of important ICT contracts, including the National Electronic Administration Network, an online inspection and monitoring platform for national educational examinations at provincial level, and digital urban management system. For the first half of 2007, revenue attributable to the ICT business was RMB1,438 million, accounting for 3.5% of the Company's total revenue.

# Chief Executive Officer's Statement

## III. Operation Management

The Company has been building a world-class operation and management system to improve operational efficiency. Centralized management has been applied to budget management, human resources, procurement, information system, network operation maintenance and network construction to centralize resource allocation. In the first half of 2007, the Company set up a market-oriented and budget-based resource allocation system, shifting less cost-effective resources from traditional segments to broadband and ICT services.

The Company continued its stringent control of CAPEX to improve resource utilization efficiency. In the first half of 2007, the Company formulated a CAPEX enhancement plan, which optimized the pre-project evaluation of fixed assets investments and investment decision-making processes. Integrated analysis and comprehensive scientific evaluation improve decision-making, enhancing resource utilization efficiency.

On May 31, 2007, the Company completed the testing of its internal control over financial reporting as at December 31, 2006. The company became the first PRC telecommunications operator to be in compliance with Section 404 of the Sarbanes-Oxley Act. Over the past three years, the Company has built an internal control system which is based on comprehensive risk management and is in line with domestic and foreign regulatory and legal requirements.

## IV. Prospects

In the second half of the year, the Company will intensify its efforts to retain growth in its traditional businesses while promoting development in high-growth businesses such as broadband, value-added services and ICT services. At the same time, the Company will shift its business model from product-oriented to customer-oriented and focus on the following aspects:

- optimizing the bundling components and pricing of "Family 1+" service, attempting to reform and adjust the tariff model for voice services, and slowing down the decline in voice traffic while achieving moderate growth in the number of local telephone subscribers;
- increasing broadband subscribers and the penetration of broadband content and applications through the bundling of services, promoting "CNC MAX" Navigator to deliver more personalized and more diversified broadband content and applications through self-operated and co-operative means to customers' desktops, and promoting further growth in broadband access, content and applications;
- promoting and marketing Olympics-related products fully so as to lay a sound foundation for rapid growth in the broadband and ICT businesses in 2008;
- adjusting organizational structures and marketing and management models to accelerate the Company's transformation, shifting from a product-oriented business model to a customer-oriented business model to allow the Company to better respond to market changes and improve its competitiveness; increasing analysis of the Company's existing resources and product profitability to better allocate resources and price its products; and further optimizing budgeting and investment management processes to improve resource utilization efficiency.

The Company is expecting more opportunities and challenges in 2007. However, it is my belief that through the joint efforts of the Board of Directors, the management and all of our staff, we will be able to deliver satisfactory results for our shareholders.

**Zuo Xunsheng**
*Chief Executive Officer*

Hong Kong, August 22, 2007

# Independent Review Report

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**REPORT ON REVIEW OF INTERIM FINANCIAL INFORMATION**
**TO THE BOARD OF DIRECTORS OF CHINA NETCOM GROUP CORPORATION (HONG KONG) LIMITED**
*(incorporated in Hong Kong with limited liability)*

## Introduction

We have reviewed the interim financial information set out on pages 8 to 49, which comprises the consolidated condensed balance sheet of China Netcom Group Corporation (Hong Kong) Limited (the "Company") and its subsidiaries (together, the "Group") as at June 30 2007 and the related consolidated condensed statements of income, changes in equity and cash flows for the six-month period then ended, and a summary of significant accounting policies and other explanatory notes. The Rules Governing the Listing of Securities on the Main Board of The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and Hong Kong Accounting Standard 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants. The directors of the Company are responsible for the preparation and presentation of this interim financial information in accordance with Hong Kong Accounting Standard 34 "Interim Financial Reporting". Our responsibility is to express a conclusion on this interim financial information based on our review and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## Scope of Review

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the interim financial information is not prepared, in all material respects, in accordance with Hong Kong Accounting Standard 34 "Interim Financial Reporting".

**PricewaterhouseCoopers**
*Certified Public Accountants*

Hong Kong, August 22 2007

# Unaudited Consolidated Condensed Income Statement

For the six months ended June 30 2007

| | Note | Six months ended June 30 | |
|---|---|---|---|
| | | **2007** | 2006 |
| | | **RMB million** | RMB million |
| | | **Unaudited** | Unaudited |
| | | | Restated |
| | | | Note 2 |
| **Continuing operations:** | | | |
| Revenues | 4 | **41,508** | 41,808 |
| Operating expenses | | | |
| Depreciation and amortisation | | **(12,616)** | (12,282) |
| Networks, operations and support | | **(6,642)** | (5,640) |
| Staff costs | | **(5,722)** | (5,764) |
| Selling, general and administrative | | **(4,854)** | (5,751) |
| Other operating expenses | | **(1,528)** | (670) |
| Total operating expenses | 5 | **(31,362)** | (30,107) |
| Interest income | | **66** | 50 |
| Profit from operations | | **10,212** | 11,751 |
| Finance costs | 6 | **(1,770)** | (1,886) |
| Profit before taxation | | **8,442** | 9,865 |
| Taxation | 7 | **(2,353)** | (2,671) |
| Profit for the period from continuing operations | | **6,089** | 7,194 |
| **Discontinued operations:** | | | |
| Profit/(loss) for the period from discontinued operations | 17 | **624** | (100) |
| **Profit for the period attributable to shareholders of the Company** | | **6,713** | 7,094 |
| Earnings per share for profit from continuing operations attributable to shareholders of the Company for the period | 9 | | |
| - Basic earnings per share | | **RMB0.92** | RMB1.09 |
| - Diluted earnings per share | | **RMB0.90** | RMB1.08 |
| Earnings/(loss) per share for profit/(loss) from discontinued operations attributable to shareholders of the Company for the period | 9 | | |
| - Basic earnings/(loss) per share | | **RMB0.09** | RMB(0.02) |
| - Diluted earnings/(loss) per share | | **RMB0.09** | RMB(0.02) |
| Earnings per share for profit attributable to shareholders of the Company for the period | | | |
| - Basic earnings per share | 9 | **RMB1.01** | RMB1.07 |
| - Diluted earnings per share | 9 | **RMB0.99** | RMB1.06 |

The notes on pages 14 to 49 are an integral part of these consolidated condensed financial statements.

# Unaudited Consolidated Condensed Balance Sheet

As at June 30 2007

| | Note | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|---|
| | | **RMB million Unaudited** | RMB million Audited |
| **Assets** | | | |
| Current assets | | | |
| Cash and bank deposits | 10 | **4,524** | 7,571 |
| Accounts receivable | 11 | **8,425** | 8,283 |
| Inventories and consumables | | **304** | 416 |
| Prepayments, other receivables and other current assets | | **990** | 1,437 |
| Due from holding companies and fellow subsidiaries | 12 | **242** | 352 |
| Total current assets | | **14,485** | 18,059 |
| Non-current assets | | | |
| Fixed assets | 13 | **156,026** | 168,044 |
| Construction in progress | | **6,645** | 6,355 |
| Lease prepayments | 14 | **2,540** | 2,364 |
| Intangible assets | 15 | **1,492** | 1,588 |
| Deferred tax assets | 21 | **2,849** | 3,459 |
| Other non-current assets | 16 | **3,574** | 3,966 |
| Total non-current assets | | **173,126** | 185,776 |
| **Total assets** | | **187,611** | 203,835 |

The notes on pages 14 to 49 are an integral part of these consolidated condensed financial statements.

# Unaudited Consolidated Condensed Balance Sheet

As at June 30 2007

| | Note | As at June 30 2007 RMB million Unaudited | As at December 31 2006 RMB million Audited |
|---|---|---|---|
| **Liabilities and equity** | | | |
| Current liabilities | | | |
| Accounts payable | 18 | **16,788** | 17,654 |
| Accruals and other payables | | **3,996** | 3,056 |
| Short-term commercial paper | 19(a)(i) | **19,973** | 9,811 |
| Short-term bank loans | 19(a)(ii) | **13,593** | 30,980 |
| Current portion of long-term bank and other loans | 19(b) | **4,637** | 7,304 |
| Due to holding companies and fellow subsidiaries | 12 | **6,523** | 7,519 |
| Current portion of deferred revenues | 20 | **6,981** | 7,733 |
| Current portion of provisions | | **3,400** | 3,736 |
| Taxation payable | | **2,776** | 3,009 |
| Total current liabilities | | **78,667** | 90,802 |
| Net current liabilities | | **64,182** | 72,743 |
| Total assets less current liabilities | | **108,944** | 113,033 |
| Non-current liabilities | | | |
| Long-term bank and other loans | 19(b) | **17,031** | 23,219 |
| Corporate bonds | 19(c) | **2,000** | — |
| Due to holding companies and fellow subsidiaries | 12 | **4,900** | 5,880 |
| Deferred revenues | 20 | **5,243** | 6,198 |
| Provisions | | **2,253** | 2,586 |
| Deferred tax liabilities | 21 | **884** | 1,156 |
| Other non-current liabilities | | **15** | 16 |
| Total non-current liabilities | | **32,326** | 39,055 |
| Total liabilities | | **110,993** | 129,857 |
| Financed by: | | | |
| Share capital | 22 | **2,201** | 2,199 |
| Reserves | | **74,417** | 71,779 |
| Shareholders' equity | | **76,618** | 73,978 |
| **Total liabilities and equity** | | **187,611** | 203,835 |

The notes on pages 14 to 49 are an integral part of these consolidated condensed financial statements.

| **Zuo Xunsheng** | **Li Fushen** |
|---|---|
| Director | Director |

# Unaudited Consolidated Condensed Statement of Changes in Equity

For the six months ended June 30 2007

| | Attributable to shareholders of the Company(unaudited) | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Share premium | Capital reserve | Statutory reserve | Revaluation reserve | Other reserve | Retained earnings | Total equity |
| | RMB million<br>Note 22 | RMB million | RMB million | RMB million | RMB million | RMB million | RMB million | RMB million |
| Balance as at January 1, 2007 | 2,199 | 43,295 | 389 | 11,811 | 2,886 | (5,333) | 18,731 | 73,978 |
| Transfers to statutory reserve (Note 8 (iii)) | — | — | — | 855 | — | — | (855) | — |
| Transfers to retained earnings in respect of depreciation differences on revalued assets | — | — | — | — | (1,016) | (50) | 1,066 | — |
| Transfers to retained earnings in respect of revaluation reserve relating to the Guangdong and Shanghai branches | — | — | — | — | (69) | 20 | 49 | — |
| Movement of deferred tax upon changes in statutory taxation rate (Note 7, 21) | — | — | — | — | 111 | (664) | — | (553) |
| Currency translation differences | — | — | — | — | — | (7) | — | (7) |
| Net income/(expense) recognized directly in equity | — | — | — | 855 | (974) | (701) | 260 | (560) |
| Profit for the period | — | — | — | — | — | — | 6,713 | 6,713 |
| Total income/(expense) recognized for the period | — | — | — | 855 | (974) | (701) | 6,973 | 6,153 |
| Dividends for 2006 distributed during the period (Note 8 (i)) | — | — | — | — | — | — | (3,600) | (3,600) |
| Issue of shares upon exercise of share options (Note 22) | 2 | 62 | (9) | — | — | — | — | 55 |
| Share-based compensation (Note 23) | — | — | 32 | — | — | — | — | 32 |
| Balance as at June 30, 2007 | 2,201 | 43,357 | 412 | 12,666 | 1,912 | (6,034) | 22,104 | 76,618 |

The notes on pages 14 to 49 are an integral part of these consolidated condensed financial statements.

# Unaudited Consolidated Condensed Statement of Changes in Equity

For the six months ended June 30 2007

| | Attributable to shareholders of the Company(unaudited) | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Share premium | Capital reserve | Statutory reserve | Revaluation reserve | Other reserve | Retained earnings | Total equity |
| | RMB million<br>Note 22 | RMB million | RMB million | RMB million | RMB million | RMB million | RMB million | RMB million |
| Balance as at January 1, 2006 | 2,181 | 42,750 | 387 | 8,550 | 4,101 | (5,203 ) | 10,244 | 63,010 |
| Transfers to statutory reserve (Note 8 (iii)) | — | — | — | 1,330 | — | — | (1,330 ) | — |
| Transfers to retained earnings in respect of depreciation differences on revalued assets | — | — | — | — | (954 ) | (37 ) | 991 | — |
| Currency translation differences | — | — | — | — | — | (48 ) | — | (48 ) |
| Net income/(expense) recognised directly in equity | — | — | — | 1,330 | (954 ) | (85 ) | (339 ) | (48 ) |
| Profit for the period | — | — | — | — | — | — | 7,094 | 7,094 |
| Total income/(expense) recognised for the period | — | — | — | 1,330 | (954 ) | (85 ) | 6,755 | 7,046 |
| Dividends for 2005 distributed during the period (Note 8 (i)) | — | — | — | — | — | — | (3,196 ) | (3,196 ) |
| Issue of shares upon exercise of share options (Note 22) | 6 | 173 | (23 ) | — | — | — | — | 156 |
| Share-based compensation (Note 23) | — | — | 38 | — | — | — | — | 38 |
| Balance as at June 30, 2006 | 2,187 | 42,923 | 402 | 9,880 | 3,147 | (5,288 ) | 13,803 | 67,054 |

The notes on pages 14 to 49 are an integral part of these condensed consolidated financial statements.

# Unaudited Consolidated Condensed Statement of Cash Flows

For the six months ended June 30 2007

| | Note | Six months ended June 30 | |
|---|---|---|---|
| | | **2007** | 2006 |
| | | **RMB million** | RMB million |
| | | **Unaudited** | Unaudited |
| | | | Restated |
| | | | (Note 2) |
| **Continuing operations:** | | | |
| Net cash inflow from operating activities | | **16,580** | 17,256 |
| Net cash outflow from investing activities | | **(7,074)** | (10,050) |
| Net cash outflow from financing activities | | **(16,155)** | (6,420) |
| **Net cash (outflow)/inflow from continuing operations** | | **(6,649)** | 786 |
| **Net cash inflow from discontinued operations** | 17 | **3,491** | 88 |
| **(Decrease)/increase in cash and cash equivalents** | | **(3,158)** | 874 |
| **Cash and cash equivalents at beginning of period** | | **7,569** | 4,874 |
| **Cash and cash equivalents at end of period** | | **4,411** | 5,748 |
| - Continuing operations | 10 | **4,411** | 5,471 |
| - Discontinued operations | | **—** | 277 |

The notes on pages 14 to 49 are an integral part of these consolidated condensed financial statements.

# Notes to the Interim Financial Statements

## 1 The group and its principal activities

### Background of the group

China Netcom Group Corporation (Hong Kong) Limited (the "Company") was incorporated in the Hong Kong Special Administrative Region ("Hong Kong") of the People's Republic of China ("PRC") as a limited liability company under the Hong Kong Companies Ordinance, the shares of the Company were listed on The Stock Exchange of Hong Kong Limited on November 17, 2004 and the ADSs were listed on New York Stock Exchange Inc. on November 16, 2004.

The Company, China Netcom (Holding) Company Limited and China Network Communications Group Corporation (the "China Netcom Group") underwent reorganisation on June 30, 2004 ("Listing Reorganisation"). Immediately after the Listing Reorganisation, China Netcom Group became the ultimate holding company of the Company.

Pursuant to a resolution passed at the extraordinary general meeting of the shareholders on October 25, 2005, the Company acquired the principal telecommunications operations, assets and liabilities in the four Northern provinces/autonomous region, namely Shanxi Province, Neimenggu Autonomous Region, Jilin Province and Heilongjiang Province from China Netcom Group (the "Acquisition of New Horizon"). The consideration for the Acquisition of New Horizon was determined at RMB 12,800 million. The consideration consists of an initial cash payment of RMB3, 000 million and deferred payments of RMB 9,800 million. The deferred payments will be settled in half-yearly installments over five years. The interest charged on the deferred payments is to be calculated at 5.265% per annum.

Following the Listing Reorganisation and the Acquisition of New Horizon, the Group was the dominant provider of fixed line telephone services, broadband, other internet-related services, and business and data communications services in ten northern provinces, municipalities and autonomous region, namely Beijing Municipality, Tianjin Municipality, Hebei Province, Liaoning Province, Shandong Province, Henan Province, Shanxi Province, Neimenggu Autonomous Region, Jilin Province, and Heilongjiang Province. The Group also provided telecommunications services to selected business and residential customers in two southern municipality and province, namely Shanghai Municipality and Guangdong Province in the PRC.

On June 2, 2006, the Group entered into an agreement with third party buyers to dispose of its entire interest in the Asia Netcom Corporation Limited ("ANC Group") for an aggregate cash consideration of US$168.84 million, at fair value determined by both parties. The transaction was completed on August 22, 2006. Please see the 2006 annual report for the details of the disposal of ANC Group.

On January 15, 2007, the wholly own subsidiary of the Company, China Netcom (Group) Corporation Limited ("CNC China") entered into an assets transfer agreement with it's ultimate holding Company, China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality branches ("Guangdong and Shanghai branches") in the PRC for a consideration of RMB3.5 billion. On February 14, 2007, the independent shareholders passed an ordinary resolution to approve the disposal. The disposal was completed on February 28, 2007 upon the approval granted from the Ministry of Information Industry ("MII"). After the disposal of the Southern municipality and province, The Group only provides the telecommunication operations in the ten northern provinces, municipalities and autonomous region.

# Notes to the Interim Financial Statements

## 1 The group and its principal activities *(continued)*

Currently, the Group's principal services consist of:

- Fixed line telephone services (including the personal handy phone system (PHS) services), comprising:

  (a) Local, domestic long distance and international long distance services;

  (b) Value-added services, including caller identity, telephone information services; and

  (c) Interconnection services provided to other domestic telecommunications service providers including the fellow subsidiary owned by China Netcom Group operating outside the ten service regions;

- Broadband services and other Internet-related services;

- Business and data communications services, including integrated regional data and voice communications services;

- Information Communications Technology Services, including system integration, software development, maintenance services, consultancy services, product sales and agency services, and equipment leasing services.

## 2 Basis of presentation

These unaudited consolidated condensed financial statements (the "interim financial statements") have been prepared in accordance with Hong Kong Accounting Standard ("HKAS") 34, "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants (the "HKICPA") and the disclosure requirements of the Hong Kong Companies Ordinance and the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

The interim financial statements include the financial information of the Company and its subsidiaries (collectively referred to as the "Group") and have been prepared in accordance with the same accounting policies adopted in the 2006 financial statements and the new accounting policies as set out in Note 3 below. These interim financial statements should be read in conjunction with the Group's 2006 financial statements.

A significant percentage of the Group's funding requirements is achieved through short term borrowings. Consequently, the balance sheet indicates a significant working capital deficit. In the past, a substantial portion of the Group's short term borrowings have been rolled over upon maturity. In addition, on July 20, 2006 and April 30, 2007, the Group issued commercial papers to raise additional fundings totalling RMB 20 billion. On June 8, 2007, the Group has issued corporate bonds to raise additional fundings of RMB 2 billion. Based on the Group's history of obtaining financing, its relationships with its bankers and its operating performance, the directors consider that the Group will continue to be able to roll over such short term financing, or will be able to obtain sufficient alternative sources of financing to enable it to operate and meet its liabilities as and when they fall due.

On June 2, 2006, the Group entered into an agreement with third party buyers to dispose of the entire interests in the ANC Group and the disposal was completed on August 22, 2006. On January 15, 2007, CNC China entered into an assets transfer agreement with China Netcom Group to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong and Shanghai branches in the PRC and the disposal was completed on February 28, 2007. In accordance with Hong Kong Financial Reporting Standard ("HKFRS") 5 "Non-current assets held for sales and discontinued operations" issued by the HKICPA, the results and cash flows of the operations of the ANC Group and Guangdong and Shanghai branches have been presented as discontinued operations. The first half year of 2006 comparative figures in the income statement and statement of cash flows were restated accordingly.

## 3 Changes in accounting policies

In 2007, the Group adopted the new and revised HKFRSs as listed below, which are relevant to its operations.

- HKFRS 7 - Financial Instruments : Disclosures
- HKAS 1 (Amendment) - Presentation of Financial Statements: Capital Disclosure
- HK(IFRIC) - Int 8 - Scope of HKFRS 2
- HK(IFRIC) - Int 10 - Interim Reporting and Impairment

The adoption of these new and revised HKFRSs by the Company did not have any significant impact on its results of operations and financial position.

## 4 Revenues

Revenues represent the turnover of the Group and are derived from the provision of fixed line telecommunications and related services, net of the PRC business taxes of RMB 1,161 million (For the six months ended June 30, 2006: RMB 1,191 million) and government levies. The Group's revenues by business nature can be summarized as follows:

| | **Six months ended June 30** | |
|---|---|---|
| | **2007** | 2006 |
| | **RMB million** | RMB million |
| | **Unaudited** | Unaudited |
| | | Restated |
| | | Note 2 |
| **Revenues** | | |
| Local usage fees | **10,281** | 11,356 |
| Monthly telephone services | **6,697** | 8,631 |
| Upfront installation fees | **653** | 691 |
| DLD usage fees | **4,471** | 4,764 |
| ILD usage fees | **411** | 414 |
| Value-added services | **3,129** | 2,519 |
| Interconnection fees | **4,203** | 3,949 |
| Upfront connection fees | **855** | 1,330 |
| Broadband services | **6,383** | 4,696 |
| Other internet-related services | **249** | 261 |
| Managed data services | **641** | 736 |
| Leased line income | **1,189** | 1,137 |
| Information communication technologies services | **1,438** | — |
| Other services | **908** | 1,324 |
| **Total** | **41,508** | 41,808 |

## 5 Operating expenses

Operating expenses mainly represent:

| | Six months ended June 30 | |
|---|---|---|
| | **2007** | 2006 |
| | **RMB million** | RMB million |
| | **Unaudited** | Unaudited |
| | | Restated |
| | | Note 2 |
| Staff costs | **5,722** | 5,764 |
| Depreciation and amortisation | **12,616** | 12,282 |
| Maintenance costs | **1,852** | 1,910 |
| Miscellaneous taxes and fees | **142** | 145 |
| Customer installation costs | **981** | 561 |
| Interconnection charges | **2,004** | 1,574 |
| Advertising and promotion expenses | **359** | 380 |
| Sales channel cost | **1,041** | 956 |
| Subscribers acquisition and retention costs | **955** | 1,784 |
| Auditor's remuneration | **10** | 11 |
| Bad and doubtful debt expenses | **239** | 530 |
| Operating leases | **950** | 903 |

# Notes to the Interim Financial Statements

## 6 Finance costs

| | Six months ended June 30 | |
|---|---|---|
| | **2007** | 2006 |
| | **RMB million** | RMB million |
| | **Unaudited** | Unaudited |
| | | Restated |
| | | Note 2 |
| Interest expenses on: | | |
| - Bank and other loans wholly repayable within five years | **1,524** | 1,616 |
| - Bank and other loans wholly repayable after more than five years | **112** | 124 |
| - Deferred consideration related to Acquisition of New Horizon | **199** | 251 |
| | **1,835** | 1,991 |
| Less: Interest expenses capitalised in construction in progress | **(89)** | (115) |
| | **1,746** | 1,876 |
| Exchange loss, net | **12** | 1 |
| Bank charges | **12** | 9 |
| | **1,770** | 1,886 |
| Interest expenses were capitalised in construction in progress using the following annual interest rates | **4.46%-5.49%** | 4.28%-5.03% |

## 7 Taxation

| | Six months ended June 30 | |
|---|---|---|
| | **2007** | 2006 |
| | **RMB million** | RMB million |
| | **Unaudited** | Unaudited |
| | | Restated |
| | | Note 2 |
| PRC enterprise income tax ("EIT") | **2,587** | 3,035 |
| Overseas profit tax | **11** | 1 |
| Deferred taxation - Continuing operations (Note 21) | **(194)** | (365) |
| Deferred taxation - Change in statutory taxation rate (Note 21) | **(51)** | — |
| Taxation charges | **2,353** | 2,671 |

The provision for EIT is calculated based on the statutory income tax rate of 33% on the assessable profit of each of the entities now comprising the Group in the PRC as determined in accordance with the relevant income tax rules and regulations in the PRC.

Taxation on profits derived from certain subsidiaries outside the PRC, including Hong Kong, has been calculated on the estimated assessable profit at the rates of taxation ranging from 17.50% to 34.00%, prevailing in the countries in which those entities operate.

On March 16, 2007, the National People's Congress approved the Enterprise Income Tax Law of the People's Republic of China (the "New EIT Law"). This New EIT Law reduces the enterprise income tax rate for domestic enterprises from 33% to 25% with effect from January 1, 2008. As a result of the new EIT Law, as at March 16, 2007, the carrying value of deferred tax assets has been written down by RMB 775 million, with RMB 111 million recognised in income statement and RMB 664 million recognised in equity. The carrying value of deferred tax liabilities has been written down by RMB 273 million, with RMB 162 million recognised in income statement and RMB 111 million recognised in equity. The change in deferred taxation recognised in current income statement or equity as a result of the New EIT Law corresponding to the related items previously recognised in income statement or equity.

The New EIT Law will provide further detailed measures and regulations on the determination of taxable profit. Detail of tax incentives and grandfathering provisions will be issued by the State Council in due course. As and when the State Council announces the additional details in respect of the above taxable profit, the Company will further assess the financial impact, if any, and this change in accounting estimate will be accounted for prospectively.

## 7 Taxation *(continued)*

The reconciliation between the Group's actual tax charge and the amount which is calculated based on the weighted average statutory tax rate is as follows:

| | Six months ended June 30 | |
|---|---|---|
| | **2007** | 2006 |
| | **RMB million** | RMB million |
| | **Unaudited** | Unaudited |
| | | Restated |
| | | Note 2 |
| Profit before taxation | **8,442** | 9,865 |
| Weighted average statutory taxation rate | **33%** | 33% |
| Tax calculated at the weighted average statutory taxation rate | **2,786** | 3,255 |
| Non-taxable income (See Note) | **(366)** | (535) |
| Expenses not deductible for tax purposes | **30** | 20 |
| Change in statutory taxation rate | **(51)** | — |
| Others | **(46)** | (69) |
| Taxation charges | **2,353** | 2,671 |

Note: Non-taxable income comprises primarily upfront connection fees charged to customers and amortised over the customer relationship period.

## 8 Profit distributions

| | Six months ended June 30 | | | |
|---|---|---|---|---|
| | **2007** | | 2006 | |
| | **HK$ million** | **RMB million** | HK$ million | RMB million |
| | **Unaudited** | **Unaudited** | Unaudited | Unaudited |
| Dividends distributed during the period | **3,678** | **3,600** | 3,073 | 3,196 |

Note:

(i) Pursuant to the shareholder's approval at the Annual General Meeting held on May 22, 2007, a final dividend of HK$0.553 per share totaling RMB 3,600 million in respect of the year ended December 31, 2006 was declared and was paid on June 12, 2007, which has been reflected as a reduction of retained earnings for the six months ended June 30, 2007.

(ii) No interim dividend has been proposed by the directors for the period ended June 30, 2007. The payment of any future dividends will be determined by the Board of Directors.

(iii) Appropriation to statutory reserve

According to a PRC tax approval document issued by the Ministry of Finance and State Administration of Taxation to the Group, the Group's upfront connection fees are not subject to EIT and an amount equal to the upfront connection fees recongised in the retained earnings should be transferred from retained earnings to a statutory reserve. At June 30, 2007, the Company has made an aggregated appropriation of RMB 10,044 million to the statutory reserve (At June 30, 2006: RMB 8,113 million). For the six months ended June 30, 2007, the Company made an appropriation of RMB855 million (For the six months ended June 30, 2006: RMB1,330 million).

## 9 Earnings per share

Basic earnings per share are computed using the weighted average number of ordinary shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of ordinary shares and potential ordinary shares outstanding during the period.

The following table sets forth the computation of basic and diluted net earnings/(loss) per share:

| | Six months ended June 30 | |
|---|---|---|
| | **2007** | 2006 |
| | (in RMB million except share and per share data) | |
| | **Unaudited** | Unaudited Restated Note 2 |
| Numerator: | | |
| Profit/(loss) for the period | | |
| - Continuing operations | **6,089** | 7,194 |
| - Discontinued operations | **624** | (100) |
| | **6,713** | 7,094 |
| Denominator: | | |
| Weighted average number of ordinary shares outstanding and shares used in computing basic earnings/(loss) per share | **6,651,863,638** | 6,596,123,569 |
| Diluted equivalent shares arising from share options | **79,595,001** | 50,441,318 |
| Shares used in computing diluted earnings/(loss) per share | **6,731,458,639** | 6,646,564,887 |
| Basic earnings/(loss) per share (RMB) | | |
| - Continuing operations | **0.92** | 1.09 |
| - Discontinued operations | **0.09** | (0.02) |
| - Profit for the period | **1.01** | 1.07 |
| Diluted earnings/(loss) per share (RMB) | | |
| - Continuing operations | **0.90** | 1.08 |
| - Discontinued operations | **0.09** | (0.02) |
| - Profit for the period | **0.99** | 1.06 |

## 10 Cash and bank deposits

| | As at June 30 2007 | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Cash and cash equivalents | **4,411** | 7,569 |
| Time deposits with original maturities over three months | **113** | 2 |
| Total cash and bank deposits | **4,524** | 7,571 |
| Effective interest rate of time deposits with original maturities over three months (%) | **2.25** | 0.72 |

Included in cash and bank deposits at the end of each of June 30, 2007 and December 31, 2006 were Renminbi-denominated balances kept in the PRC amounting to RMB 3,537 million and RMB 5,625 million respectively. The conversion of Renminbi-denominated balances into foreign currencies and the remittance of bank balances and cash out of the PRC are subject to the rules and regulations of foreign exchange control promulgated by the PRC government.

Included in the bank deposits were deposits in state-controlled banks amounting to RMB 3,781 million at June 30, 2007 (December 31, 2006: RMB 7,422 million ).For the six months ended June 30, 2007, interest income earned from these state-controlled banks deposits amounted to RMB 61 million (For the six months ended June 30, 2006: RMB 45 million ).

## 11 Accounts receivable

Amounts due from the provision of fixed line telecommunications services to residential and business customers are due within 30 days from the date of billing. Residential customers who have accounts overdue by more than 90 days will in normal circumstances have their services disconnected. Accounts receivable from other telecommunications operators and customers are due between 30 to 90 days from the billing date.

The ageing analysis of accounts receivable based on the billing date is as follows:

| | As at June 30 2007 | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| 0-30 days | **5,455** | 5,744 |
| 31-90 days | **1,743** | 1,557 |
| Over 90 days | **2,740** | 2,326 |
| Total | **9,938** | 9,627 |
| Less: Allowance for doubtful debts | **(1,513)** | (1,344) |
| Net carrying amounts | **8,425** | 8,283 |

The carrying value of accounts receivable approximates their fair values based on cash flows discounted using a rate based on the average short-term borrowing rate of 6.57% (December 31, 2006: 6.12%).

Included in the accounts receivable are amounts due from other state-controlled telecommunication operators amounting to RMB 1,044 million (December 31, 2006: RMB 1,079 million).

## 12 Amount due from/(to) holding companies and fellow subsidiaries

| | Note | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|---|
| | | **RMB million Unaudited** | RMB million Audited |
| Current: | | | |
| Due from ultimate holding company | (a) | **158** | 173 |
| Due from other holding companies | (a) | **6** | 3 |
| Due from fellow subsidiaries | (a) | **78** | 176 |
| Total | | **242** | 352 |
| Due to ultimate holding company | | | |
| - Deferred consideration | (b) | **1,960** | 1,960 |
| - Others | (a) | **3,004** | 3,282 |
| Due to fellow subsidiaries | (a) | **1,559** | 2,277 |
| Total | | **6,523** | 7,519 |
| Non-current: | | | |
| Due to ultimate holding company | | | |
| - Deferred consideration | (b) | **4,900** | 5,880 |

Note:

(a) These are interest free, unsecured and have no fixed terms of repayment.

(b) Balance represents the deferred payments arising from the Acquisition of New Horizon outstanding at the period end. The balance is charged at interest rate of 5.265 % per annum with final maturity through June 30, 2010. The deferred payment is analysed as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Within one year | **1,960** | 1,960 |
| In the second year | **1,960** | 1,960 |
| In the third to fifth year, inclusive | **2,940** | 3,920 |
| Total | **6,860** | 7,840 |

## 13 Fixed assets

| | Buildings | Telecommunications networks and equipment | Furniture, fixture, motor vehicles and other equipment | Total |
|---|---|---|---|---|
| | RMB million | RMB million | RMB million | RMB million |
| | Unaudited | Unaudited | Unaudited | Unaudited |
| Cost/valuation: | | | | |
| Balance at January 1, 2007 | 27,613 | 289,263 | 18,850 | 335,726 |
| Additions for the period | 21 | 164 | 175 | 360 |
| Transferred from construction in progress | 275 | 5,557 | 689 | 6,521 |
| Disposals/write off for the period | — | (116) | (97) | (213) |
| Disposal of Guangdong and Shanghai branches | (550) | (7,635) | (344) | (8,529) |
| Balance at June 30, 2007 | 27,359 | 287,233 | 19,273 | 333,865 |
| Accumulated depreciation: | | | | |
| Balance at January 1, 2007 | (7,142) | (151,127) | (9,413) | (167,682) |
| Charges for the period | (519) | (11,037) | (911) | (12,467) |
| Disposals/write off for the period | — | 85 | 87 | 172 |
| Disposal of Guangdong and Shanghai branches | 134 | 1,867 | 137 | 2,138 |
| Balance at June 30, 2007 | (7,527) | (160,212) | (10,100) | (177,839) |
| Net book value at June 30, 2007 | 19,832 | 127,021 | 9,173 | 156,026 |
| Net book value at January 1, 2007 | 20,471 | 138,136 | 9,437 | 168,044 |

# Notes to the Interim Financial Statements

## 13 Fixed assets *(continued)*

| | Buildings | Telecommunications networks and equipment | Furniture, fixture, motor vehicles and other equipment | Total |
|---|---|---|---|---|
| | RMB million Audited | RMB million Audited | RMB million Audited | RMB million Audited |
| Cost/valuation: | | | | |
| Balance at January 1, 2006 | 27,050 | 280,301 | 19,770 | 327,121 |
| Additions for the year | 52 | 755 | 635 | 1,442 |
| Transferred from construction in progress | 688 | 21,449 | 2,621 | 24,758 |
| Disposals/write off for the year | (5) | (1,947) | (543) | (2,495) |
| Disposal of ANC Group | (172) | (636) | (45) | (853) |
| Fixed assets revaluation deficit, net | — | (10,659) | (3,588) | (14,247) |
| Balance at December 31, 2006 | 27,613 | 289,263 | 18,850 | 335,726 |
| Accumulated depreciation: | | | | |
| Balance at January 1, 2006 | (6,201) | (142,639) | (9,618) | (158,458) |
| Depreciation charge for the year | (995) | (21,842) | (2,282) | (25,119) |
| Disposals/write off for the year | 3 | 1,315 | 443 | 1,761 |
| Disposal of ANC Group | 51 | 261 | 28 | 340 |
| Fixed assets revaluation deficit, net | — | 11,778 | 2,016 | 13,794 |
| Balance at December 31, 2006, | (7,142) | (151,127) | (9,413) | (167,682) |
| Net book value at December 31, 2006 | 20,471 | 138,136 | 9,437 | 168,044 |
| Net book value at January 1, 2006 | 20,849 | 137,662 | 10,152 | 168,663 |

## 14 Lease prepayment

| | As at June 30 2007 RMB million Unaudited | As at December 31 2006 RMB million Audited |
|---|---|---|
| Lease prepayments for land (i) | **2,224** | 2,046 |
| Lease prepayments for network capacity (ii) | **316** | 318 |
| Total | **2,540** | 2,364 |

### (i) Lease prepayments for land

This represents land use rights held in the PRC and their net book value is analysed as follows:

| | As at June 30 2007 RMB million Unaudited | As at December 31 2006 RMB million Audited |
|---|---|---|
| Held for | | |
| Lease of between 10 to 50 years | **2,205** | 2,024 |
| Lease of less than 10 years | **19** | 22 |
| Balance at end of period/year | **2,224** | 2,046 |

The movement of the lease prepayments for land is as follows:

| | As at June 30 2007 RMB million Unaudited | As at December 31 2006 RMB million Audited |
|---|---|---|
| Balance at beginning of period/year | **2,046** | 1,949 |
| Additions for the period/year | **213** | 165 |
| Amortization for the period/year | **(27)** | (68) |
| Disposal of Guangdong and Shanghai branches | **(8)** | — |
| Balance at end of period/ year | **2,224** | 2,046 |

## 14 Lease prepayment *(continued)*

### (ii) Lease prepayments for network capacity

The net book value is analysed as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million** | RMB million |
| | **Unaudited** | Audited |
| Held for | | |
| Lease of between 10 to 50 years | **316** | 318 |

The movement of the lease prepayments for network capacity is as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million** | RMB million |
| | **Unaudited** | Audited |
| Balance at beginning of period/year | **318** | — |
| Additions for the period/year | **—** | 318 |
| Amortization for the period/year | **(2)** | — |
| Balance at end of period/ year | **316** | 318 |

# Notes to the Interim Financial Statements

## 15 Intangible assets

| | Purchased software | Sponsorship fees | Total |
|---|---|---|---|
| | RMB million | RMB million | RMB million |
| | Unaudited | Unaudited | Unaudited |
| | | Note 26(xvi) | |
| Cost: | | | |
| Balance at January 1,2007 | 1,887 | 540 | 2,427 |
| Additions for the period | 66 | — | 66 |
| Transferred from construction in progress | 153 | — | 153 |
| Write off for the period | (15) | — | (15) |
| Disposal of Guangdong and Shanghai branches | (75) | — | (75) |
| Balance at June 30, 2007 | 2,016 | 540 | 2,556 |
| Accumulated amortisation: | | | |
| Balance at January 1, 2007 | (569) | (270) | (839) |
| Amortisation for the period | (192) | (68) | (260) |
| Write off for the period | 15 | — | 15 |
| Disposal of Guangdong and Shanghai branches | 20 | — | 20 |
| Balance at June 30, 2007 | (726) | (338) | (1,064) |
| Net book value at June 30, 2007 | 1,290 | 202 | 1,492 |
| Net book value at January 1, 2007 | 1,318 | 270 | 1,588 |

## 15 Intangible assets *(continued)*

| | Goodwill | Purchased software | Sponsorship fees | Total |
|---|---|---|---|---|
| | RMB million Audited | RMB million Audited | RMB million Audited | RMB million Audited |
| Cost: | | | | |
| Balance at January 1, 2006 | 3 | 1,913 | 540 | 2,456 |
| Additions for the year | — | 94 | — | 94 |
| Transferred from construction in progress | — | 572 | — | 572 |
| Write off for the year | (3) | (692) | — | (695) |
| Balance at December 31, 2006 | — | 1,887 | 540 | 2,427 |
| Accumulated amortisation: | | | | |
| Balance at January 1, 2006 | (3) | (925) | (135) | (1,063) |
| Amortisation for the year | — | (336) | (135) | (471) |
| Write off for the year | 3 | 692 | — | 695 |
| Balance at December 31, 2006 | — | (569) | (270) | (839) |
| Net book value at December 31, 2006 | — | 1,318 | 270 | 1,588 |
| Net book value at January 1, 2006 | — | 988 | 405 | 1,393 |

## 16 Other non-current assets

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Installation cost | **3,182** | 3,525 |
| Others | **392** | 441 |
| Total | **3,574** | 3,966 |

## 17 Discontinued operations

(i) The disposal of Guangdong and Shanghai branches (Note1) was completed on February 28, 2007. The results and cash flows of the Guangdong and Shanghai branches of the Group for the period ended June 30, 2007 and 2006 are presented as discontinued operations.

As at the completion date, the carrying value of assets related to the Guangdong and Shanghai branches of the Group are set out below:

| | **As at February 28, 2007** |
|---|---|
| | **RMB million** |
| | **Unaudited** |
| Net assets sold (excluding: cash and cash equivalents): | |
| Accounts receivable and other current assets | **416** |
| Fixed assets and other non-current assets | **7,630** |
| Current portion of deferred revenue | **(183)** |
| Accounts payables | **(2,046)** |
| Long-term loans | **(3,000)** |
| Other liabilities | **(267)** |
| | **2,550** |
| Gain on disposal of discontinued operations | **927** |
| Net Cash inflow from disposal of Guangdong and Shanghai branches | **3,477** |
| Analysis of net cash inflow from disposal of Guangdong and Shanghai branches | |
| Cash proceeds received | **3,500** |
| Less: cash and cash equivalents disposed | **(23)** |
| Net cash inflow | **3,477** |

(ii) On June 2, 2006, the Group entered into an agreement to dispose of its entire interest in the ANC Group. The transaction was completed on August 22, 2006. The results and cash flows of the ANC Group are presented as discontinued operations for the six months ended June 30, 2006.

## 17 Discontinued operations *(continued)*

(iii) The condensed income statements and cash flow statements related to the discontinued operations are as follows:

| | Disposal of Guangdong & Shanghai branches (i) | | Disposal of ANC Group (ii) | | Total | |
|---|---|---|---|---|---|---|
| | **For the period from January 1 2007 to February 28 2007** | For the six months ended June 30 2006 | **For the six months ended June 30 2007** | For the six months ended June 30 2006 | **For the six months ended June 30 2007** | For the six months ended June 30 2006 |
| | **RMB million Unaudited** | RMB million Unaudited | **RMB million Unaudited** | RMB million Unaudited | **RMB million Unaudited** | RMB million Unaudited |
| **Discontinued operations:** | | | | | | |
| Revenues | **615** | 1,477 | **—** | 726 | **615** | 2,203 |
| Expenses | **(618)** | (1,549) | **—** | (776) | **(618)** | (2,325) |
| Loss before taxation of discontinued operations | **(3)** | (72) | **—** | (50) | **(3)** | (122) |
| Taxation | **1** | 23 | **—** | (1) | **1** | 22 |
| Loss for the period of discontinued operations | **(2)** | (49) | **—** | (51) | **(2)** | (100) |
| Gain on disposal of discontinued operations before taxation | **927** | — | **—** | — | **927** | — |
| Taxation | **(301)** | — | **—** | — | **(301)** | — |
| Gain on discontinued operations after taxation | **626** | — | **—** | — | **626** | — |
| Profit/(loss) for the period from discontinued operations | **624** | (49) | **—** | (51) | **624** | (100) |

## 17 Discontinued operations *(continued)*

| | Disposal of Guangdong & Shanghai branches (i) | | Disposal of ANC Group (ii) | | Total | |
|---|---|---|---|---|---|---|
| | **For the period from January 1 2007 to February 28 2007** | For the six months ended June 30 2006 | **For the six months ended June 30 2007** | For the six months ended June 30 2006 | **For the six months ended June 30 2007** | For the six months ended June 30 2006 |
| | **RMB million Unaudited** | RMB million Unaudited | **RMB million Unaudited** | RMB million Unaudited | **RMB million Unaudited** | RMB million Unaudited |
| **Discontinued operations:** | | | | | | |
| Net cash inflow from operating activities | **388** | 703 | **—** | 215 | **388** | 918 |
| Cash outflow from investing activities | **(374)** | (704) | **—** | (126) | **(374)** | (830) |
| Cash inflow from disposal of Discontinued operations | **3,477** | — | **—** | — | **3,477** | — |
| Net cash inflow/outflow for investing activities | **3,103** | (704) | **—** | (126) | **3,103** | (830) |
| Net cash inflow from financing activities | **—** | — | **—** | — | **—** | — |
| Cash flow from discontinued operations | **3,491** | (1) | **—** | 89 | **3,491** | 88 |

## 18 Accounts payable

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| 0-30 days | **4,085** | 5,762 |
| 31-60 days | **1,784** | 2,236 |
| 61-90 days | **1,690** | 1,449 |
| 91-180 days | **3,236** | 2,989 |
| Over 180 days | **5,993** | 5,218 |
| Total | **16,788** | 17,654 |

Included in accounts payable were amounts due to other state-controlled telecommunications operators amounting to RMB 25 million (December 31, 2006: RMB 97 million).

## 19 Bank and other loans

(a) (i) On April 30, 2007, the Group issued RMB 10 billion one-year unsecured commercial paper in the PRC capital market and raised net cash proceeds of RMB 10 billion interesting bearing at 3.34% per annum from this exercise. The commercial paper has an effective rate of 3.34%.

On July 20, 2006, the Group issued RMB10 billion one-year unsecured non interesting bearing commercial paper in the PRC capital market and raised net cash proceeds of RMB9,676 million from this offering. The commercial paper has an effective rate of 3.35%.

The carrying value of commercial papers approximate their fair values which are based on cash flow discounted using rates based on the borrowing rate of 3.35%.

(ii) As at June 30, 2007, the short term bank loans were Renminbi-denominated and unsecured and comprised:

| **Interest rate and final maturity** | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Interest rates ranging from 4.86% to 6.00% per annum with maturity through June 28, 2008 | **13,593** | 30,980 |

The carrying values of short term bank loans approximate their fair values which are based on cash flows discounted using rates based on the borrowing rate of 4.86%-6.00% (December 31, 2006: 4.86%-5.51%).

Included in the short-term bank loans were loans from state-controlled holding banks amounting to RMB 12,983 million as at June 30, 2007 (December 31, 2006: RMB 29,700 million).

## 19 Bank and other loans *(continued)*

(b) The Group's long term bank and other loans comprised:

| | Note | As at June 30 2007 | As at December 31 2006 |
|---|---|---|---|
| | | RMB million Unaudited | RMB million Audited |
| Long term bank loans | (i) | 21,448 | 29,560 |
| Finance lease obligations | (ii) | 220 | 963 |
| | | 21,668 | 30,523 |
| Less: Current portion | | (4,637) | (7,304) |
| | | 17,031 | 23,219 |

The carrying values of the current portion of long term bank loans approximate their fair values which are based on cash flows discounted using a rate based on the borrowing rate of 6.57% (December 31, 2006: 6.12%).

Included in the long term bank loans were loans from state-controlled banks amounting to RMB 21,448 million as at June 30, 2007 (December 31, 2006: RMB 29,560 million).

(i) *Long term bank loans*

| | As at June 30 2007 | As at December 31 2006 |
|---|---|---|
| | RMB million Unaudited | RMB million Audited |
| Loans | | |
| Unsecured | 21,281 | 29,220 |
| Secured | 167 | 340 |
| Total | 21,448 | 29,560 |
| Less: Current portion | (4,469) | (6,446) |
| Long term bank loans | 16,979 | 23,114 |

## 19 Bank and other loans *(continued)*

(b) The Group's long term bank and other loans comprised: *(continued)*

(i) *Long term bank loans (continued)*

The Group's long term bank loans were repayable as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Within one year | **4,469** | 6,446 |
| In the second year | **7,100** | 6,491 |
| In the third to fifth year, inclusive | **7,012** | 9,723 |
| After the fifth year | **2,867** | 6,900 |
| | **21,448** | 29,560 |

As at June 30, 2007, secured bank loans totaled RMB 167 million (December 31, 2006: RMB 340 million) which were secured by the following:

- Corporate guarantees granted by China Netcom Group to the extent of RMB 8 million (December 31, 2006: RMB 65 million); and
- Corporate guarantees granted by third parties to the extent of RMB 159 million (December 31, 2006: RMB 275 million).

(ii) *Finance lease obligations*

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Obligation under finance leases | **220** | 963 |
| Less: current portion | **(168)** | (858) |
| | **52** | 105 |

The accumulated finance lease obligation payable to related party as at June 30, 2007 amounted to RMB 220 million. (December 31, 2006: RMB 963 million).

The interest rates charged on finance lease are ranging from 5.18%-6.88% with maturity through December 8, 2008 (December 31, 2006: 2.68% - 6.83% with maturity through December 8, 2008).

## 19 Bank and other loans *(continued)*

(b) The Group's long term bank and other loans comprised: *(continued)*

(ii) *Finance lease obligations (continued)*

The Group's liabilities under finance leases are analyzed as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Within one year | **173** | 888 |
| In the second year | **53** | 106 |
| | **226** | 994 |
| Less: future finance charges on finance leases | **(6)** | (31) |
| Present value of finance lease liabilities | **220** | 963 |

The present value of finance lease liabilities is is as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| Within one year | **168** | 858 |
| In the second year | **52** | 105 |
| | **220** | 963 |

(c) On June 8, 2007, the Group issued RMB 2 billion ten-year corporate bonds, bearing interest at 4.5% per annum. The corporate bonds are secured by a corporate guarantee granted by Bank of China Limited.

(d) The fair value of the Group's non-current portion of long term bank and other loans at June 30, 2007 and December 31, 2006 were as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Long term bank loans | **15,197** | 21,209 |
| Finance lease obligations | **45** | 85 |
| Corporate bonds | **2,000** | — |
| | **17,242** | 21,294 |

The fair value is based on cash flows discounted using rates based on the borrowing rates of ranging from 1.69%-6.48% (December 31, 2006: 3.75%-8.33%).

## 20 Deferred revenues

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Balance at beginning of period/year: | | |
| - upfront installation fees | **5,767** | 6,769 |
| - upfront connection fees | **3,099** | 5,505 |
| - advances from network capacity sales | **—** | 2,354 |
| - prepaid telephony services | **5,065** | 4,272 |
| | **13,931** | 18,900 |
| Additions for the period/year: | | |
| - upfront installation fees | **117** | 357 |
| - upfront connection fees | **—** | — |
| - advances from network capacity sales | **—** | 236 |
| - prepaid telephony services | **14,250** | 30,360 |
| | **14,367** | 30,953 |
| Reductions for the period/year: | | |
| - upfront installation fees | **(650)** | (1,359) |
| - upfront connection fees | **(855)** | (2,406) |
| - advances from network capacity sales | **—** | (2,590) |
| - prepaid telephony services | **(14,569)** | (29,567) |
| | **(16,074)** | (35,922) |
| Included: Disposal of discontinued operations: | | |
| - advances from network capacity sales | **—** | (2,450) |
| - prepaid telephony services | **(183)** | (144) |
| | **(183)** | (2,594) |
| Balance at end of period/year: | | |
| - upfront installation fees | **5,234** | 5,767 |
| - upfront connection fees | **2,244** | 3,099 |
| - advances from network capacity sales | **—** | — |
| - prepaid telephony services | **4,746** | 5,065 |
| | **12,224** | 13,931 |
| Representing: | | |
| - Current portion | **6,981** | 7,733 |
| - Non-current portion | **5,243** | 6,198 |
| | **12,224** | 13,931 |

## 21 Deferred taxation

Movements of the deferred tax assets and liabilities are as follows:

| | Balance at December 31 2006 | Recognised in Income Statement: Discontinued operations | Recognised in Income Statement: Continuing operations Note 7 | Recognised in Income Statement: Change in statutory Taxation rate Note 7 | Balance Recognized in Equity Note 7 | Disposal of Guangdong and Shanghai branches | Balance at June 30 2007 |
|---|---|---|---|---|---|---|---|
| | RMB million Audited | RMB million | RMB million | RMB million | RMB million | RMB million | RMB million Unaudited |
| **Deferred tax assets:** | | | | | | | |
| Deferred revenue, primarily advances from customers | 127 | — | (16) | (24) | — | — | 87 |
| Temporary differences from allowance for doubtful debts | 314 | (5) | 71 | (38) | — | (13) | 329 |
| Unrecognised revaluation surplus/(deficit) | 2,810 | — | (50) | — | (664) | 20 | 2,116 |
| Others | 208 | — | 162 | (49) | — | (4) | 317 |
| Balance at end of year/period | 3,459 | (5) | 167 | (111) | (664) | 3 | 2,849 |
| **Deferred tax liabilities:** | | | | | | | |
| Interest capitalised | (789) | — | 56 | 168 | — | — | (565) |
| Depreciation fixed assets | (301) | — | (29) | (15) | 111 | (28) | (262) |
| Others | (66) | — | — | 9 | — | — | (57) |
| Balance at end of year/period | (1,156) | — | 27 | 162 | 111 | (28) | (884) |
| The amount in consolidated condensed balance sheet includes the following: | | | | | | | |
| Deferred tax assets to be recovered after more than 12 months | 2,860 | | | | | | 2,134 |
| Deferred tax liabilities to be settled after more than 12 months | (1,014) | | | | | | (847) |

## 21 Deferred taxation *(continued)*

| | Balance at December 31 2005 | Recognised in Income Statement: Discontinued operations | Recognised in Income Statement: Continuing operations | Balance Recognised in Equity | Balance at December 31 2006 |
|---|---|---|---|---|---|
| | RMB million Audited | RMB million | RMB million | RMB million | RMB million Audited |
| **Deferred tax assets:** | | | | | |
| Deferred revenue, primarily advances from customers | 170 | — | (43) | — | 127 |
| Temporary differences from allowance for doubtful debts | 350 | (4) | (32) | — | 314 |
| Unrecognised revaluation surplus/(deficit) | 2,861 | 2 | (53) | — | 2,810 |
| Others | 99 | 4 | 105 | — | 208 |
| Balance at end of year | 3,480 | 2 | (23) | — | 3,459 |
| **Deferred tax liabilities:** | | | | | |
| Interest capitalised | (1,261) | — | 472 | — | (789) |
| Depreciation of fixed assets | — | 62 | (10) | (353) | (301) |
| Others | (63) | — | (3) | — | (66) |
| Balance at end of year | (1,324) | 62 | 459 | (353) | (1,156) |
| The amount in consolidated condensed balance sheet includes the following: | | | | | |
| Deferred tax assets to be recovered after more than 12 months | 2,906 | | | | 2,860 |
| Deferred tax liabilities to be settled after more than 12 months | (1,190) | | | | (1,014) |

## 22 Share capital

**Authorised**

| | Ordinary shares of US$0.04 each | | | Convertible preference shares of US$0.04 each | | | Total | |
|---|---|---|---|---|---|---|---|---|
| | No. of shares | US$ | RMB in million | No. of shares | US$ | RMB in million | US$ | RMB in million |
| As at January 1, 2006 and 2007 and as at June 30, 2007 | 25,000,000,000 | 1,000,000,000 | 8,277 | 7,741,782 | 309,671 | 3 | 1,000,309,671 | 8,280 |

**Issued**

| | Ordinary shares of US$0.04 each | | | Convertible preference shares of US$0.04 each | | | Total | |
|---|---|---|---|---|---|---|---|---|
| | No. of shares | US$ | RMB in million | No. of shares | US$ | RMB in million | US$ | RMB in million |
| As at January 1, 2006 | 6,593,529,000 | 263,741,160 | 2,181 | — | — | — | 263,741,160 | 2,181 |
| Issue of shares upon exercise of share options (See Note) | 57,114,500 | 2,284,580 | 18 | — | — | — | 2,284,580 | 18 |
| As at December 31, 2006 | 6,650,643,500 | 266,025,740 | 2,199 | — | — | — | 266,025,740 | 2,199 |
| As at January 1, 2007 | 6,650,643,500 | 266,025,740 | 2,199 | — | — | — | 266,025,740 | 2,199 |
| Issue of shares upon exercise of share options (See Note) | 6,742,100 | 269,684 | 2 | — | — | — | 269,684 | 2 |
| As at June 30, 2007 | 6,657,385,600 | 266,295,424 | 2,201 | — | — | — | 266,295,424 | 2,201 |

Note: The Group issued new shares for the options exercised during this period. During the six month ended June 30, 2007, the Company issued 6,742,100 shares (2006: 57,114,500 shares) upon the exercise of options by participants in the Share Option Scheme. The total consideration received amounting to RMB 55 million and the portion that exceeds the nominal value of the shares issued was recorded as share premium of the company.

# Notes to the Interim Financial Statements

## 23 Share option scheme

A share option scheme was approved pursuant to a directors' resolution on September 30, 2004 ("Share Option Scheme"). Share options are granted to directors of the Company and to certain employees of the Group at the directors' discretion. Share options can be exercised at least 18 months from the later of the date of grant or the date of the listing of the shares of the Company on the Hong Kong Stock Exchange and are subject to certain vesting restrictions on timing.

On October 22, 2004, 158,640,000 share options with an exercise price of HK$ 8.40 each were granted to the directors of the Company and certain employees of the Group (the "First Grant").

Pursuant to the Company's share option plan, the Company granted 158,640,000 options to certain of its directors and employees immediately prior to the closing of the Company's initial global offering, to subscribe for its ordinary shares at the initial public offering price under the Hong Kong public offering, excluding brokerage and trading fees, and transaction and investor compensation levies. The First Grant has an exercise period of six years from the date of grant. The grantees can exercise 40 percent of the options granted from May 17, 2006, and a further 20 percent of the options from May 17, 2007; all unexercised share options will be expired on November 16, 2010.

On December 6, 2005, the board of directors approved the grant of 79,320,000 share options to certain management personnel and other professional personnel designated by the Compensation Committee ("Second Grant").

The fair value at the grant date of the share options granted in the First Grant is determined using the Black-scholes valuation model based on the following assumptions: expected dividend pay-off ratio of 35%, expected vesting period of 5 years, expected fluctuation rate of 23.6% and risk-free interest rate of 4.3%. The weighted average fair value of each share option on grant date was determined as HK$ 1.22 per share (RMB 1.28 per share); the fair value at the grant date of the share options granted in the Second Grant is determined using the Black-scholes valuation model based on the following assumptions: expected dividend pay-off ratio of 35%, expected vesting period of 4 years, expected fluctuation rate of 21.46% and risk-free interest rate of 4.3%. The weighted average fair value of each share option on grant date was determined as HK$ 1.28 per share (RMB 1.34 per share). Since there is judgment exercised in the valuation model adopted and the underlying assumptions on which the fair value of the share options are determined, and any change in these subjective assumptions may have a significant impact to the fair value of the share options, the Black-Scholes Model adopted may not be a reliable determinant of the fair value of the share options.

A modification to certain clauses of the share option schemes already granted was approved on May 16, 2006, pursuant to a directors' resolution. The modifications are related to certain aspects including eligible participants, exercise of options and vesting schedules, rights upon cessation of employment, right upon death, rights upon loss of capacity, performance targets, and cancellation of options. The modification did not have any impact on the interim financial statements.

The movement of the share options during the period/year is summarised as follows:

| | No. of share options | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | As at January 1 2006 | Granted | Exercised | Lapsed | Cancelled | As at December 31 2006 | Exercise price (HK$) | Weighted average closing price per share at respective days immediately before the exercises of options (HK$) | No. of share option exercisable as at December 31 2006 |
| First Grant | 156,703,000 | — | 57,114,500 | 300 | 1,975,500 | 97,612,700 | 8.40 | 14.46 | 5,670,084 |
| Second Grant | 79,320,000 | — | — | — | 285,800 | 79,034,200 | 12.45 | — | — |
| Total | 236,023,000 | — | 57,114,500 | 300 | 2,261,300 | 176,646,900 | | | 5,670,084 |

## 23 Share option scheme *(continued)*

| | No. of share options | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | As at January 1 2007 | Granted | Exercised | Lapsed | Cancelled | As at June 30 2007 | Exercise price (HK$) | Weighted average closing price per share at respective days immediately before the exercises of options (HK$) | No. of share option exercisable as at June 30 2007 |
| First Grant | 97,612,700 | — | 6,742,100 | — | 1,827,190 | 89,043,410 | 8.40 | 21.16 | 30,169,890 |
| Second Grant | 79,034,200 | — | — | — | — | 79,034,200 | 12.45 | — | — |
| Total | 176,646,900 | — | 6,742,100 | — | 1,827,190 | 168,077,610 | | | 30,169,890 |

The company uses historical data to estimate pre-vesting option forfeitures and record share-based compensation cost only for those awards that are expected to vest.

The compensation cost recognised in staff cost during six months ended June 30, 2007 was RMB 32 million (For six months ended June 30, 2006: RMB 39 million). As at June 30, 2007, there was RMB 74 million (As at December 31, 2006: RMB 106 million) of unrecognised compensation cost, adjusted for estimated forfeitures, related to non-vested share-based awards granted to the Company's employees. This cost is expected to be recognised over a weighted-average period of 1.5 years. Total unrecognised compensation cost may be adjusted for future changes in estimated forfeitures.

There was no capitalised share-based compensation cost during the six months ended June 30, 2007 and 2006.

The intrinsic value for the options exercised amounted to HK$ 432 million and was calculated as the difference between the market value on the date of exercise and the exercise price of the shares. The intrinsic value of options outstanding as of June 30, 2007 amounted to HK$ 1,899 million (December 31, 2006: HK$ 1,879 million), which was calculated as the difference between the closing stock price as of June 30 2007 and the exercise price of the share options.

The weighted average remaining contractual life for outstanding options, vested and expected to vest options, and options exercisable as of June 30, 2007 were 3.88 years, 3.38 years and 3.38 years (as of December 31, 2006 was 4.35 years, 3.88 years and 3.88 years), respectively.

## 24 Commitments

### (a) Capital commitments

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Contracted but not provided for | | |
| - Leasehold land and buildings | **10** | 26 |
| - Telecommunications networks and equipment | **1,003** | 2,502 |
| - Others | **—** | 5 |
| Total | **1,013** | 2,533 |
| Authorised but not contracted for | | |
| - Leasehold land and buildings | **16** | — |
| - Telecommunications networks and equipment | **188** | 300 |
| - Others | **46** | — |
| Total | **250** | 300 |

### (b) Operating lease commitments

The Group has future minimum lease payments under non-cancelable operating leases in respect of premises and equipment as follows:

| | **As at June 30 2007** | As at December 31 2006 |
|---|---|---|
| | **RMB million Unaudited** | RMB million Audited |
| Within one year | **571** | 734 |
| In the second to fifth years, inclusive | **1,066** | 1,102 |
| After the fifth year | **534** | 517 |
| Total | **2,171** | 2,353 |

## 25 Contingent liabilities

As at June 30, 2007 and December 31, 2006, the Group has no contingent liabilities.

## 26 Related party transactions

All state-controlled enterprises, their subsidiaries, their key management and their close family, and their employees represent related parties of the Group as defined by HKAS 24. China Netcom Group, the Group's parent company, is a state-controlled enterprise directly controlled by the PRC government which controls different state-controlled enterprises driving the economy of the PRC. The Group is the dominant fixed line telecommunications service provider in northern China by virtue of its historical monopoly over these services. As a result, the Group has extensive transactions including sales to, purchases of services, goods and fixed assets from, leasing of assets from and banking transactions with other state-controlled parties in its ordinary course of business. These transactions are carried out at terms similar to those obtained by other state-controlled parties and have been reflected in the financial statements.

The Group's operations are subject to the supervision of and regulation by the PRC Government. The Ministry of Information Industry (MII), pursuant to the authority delegated by the PRC's State Council, is responsible for formulating the policies and regulations for the telecommunications industry in China, including granting licenses, allocating frequency spectrum, formulating interconnection and settlement arrangements between telecommunications operators, enforcing industry regulations and reviewing tariffs for domestic services. Other PRC governmental authorities also regulate tariff policies, capital investment and foreign investment in the telecommunications industry.

As a state-controlled telecommunication operator, the Group has extensive transactions with other state-controlled telecommunication operators in its ordinary course of business. These transactions are carried out in accordance with the rules and regulations stipulated by the MII of the PRC Government and disclosed below.

The Group has extensive transactions with other members of the China Netcom Group. It is possible that the terms of the transactions between the Group and other members of the China Netcom Group are not the same as those that would result from transactions with other related parties or wholly unrelated parties.

Management believes that meaningful information relative to related party disclosures has been adequately disclosed.

## 26 Related party transactions *(continued)*

| | Note | Six months ended June 30 **2007** RMB million Unaudited | 2006 RMB million Unaudited |
|---|---|---|---|
| Emolument to key management | | | |
| - salaries, welfare, and contributions to retirement scheme | (i) | **5** | 3 |
| Interconnection fees | | | |
| - from fellow subsidiaries | (iv)(b) | **300** | 145 |
| - from other state-controlled telecommunications operators | (iv)(b) | **3,206** | 3,352 |
| Subtotal | | **3,506** | 3,497 |
| Interconnection charges | | | |
| - to fellow subsidiaries | (iv)(b) | **316** | 394 |
| - to other state-controlled telecommunications operators | (iv)(b) | **732** | 830 |
| Subtotal | | **1,048** | 1,224 |
| Rental income from properties leased to fellow subsidiaries | (iv)(a),(iv)(c) | **9** | 1 |
| Purchase of materials | | | |
| - from fellow subsidiaries | (iv)(a),(iv)(c) | **281** | 668 |
| - from other related companies | (iv)(a),(iv)(c) | **33** | 70 |
| Subtotal | | **314** | 738 |

## 26 Related party transactions *(continued)*

| | Note | Six months ended June 30 **2007** RMB million Unaudited | 2006 RMB million Unaudited |
|---|---|---|---|
| Receipt of engineering, project planning, design, construction and information technology services | | | |
| - from fellow subsidiaries | (iv)(a),(iv)(b) | **683** | 836 |
| - from other related companies | (iv)(a),(iv)(b) | **74** | 138 |
| Subtotal | | **757** | 974 |
| Ancillary telecommunications support services | | | |
| - from fellow subsidiaries | (v) | **172** | 155 |
| - from other related companies | (v) | **24** | 18 |
| Subtotal | | **196** | 173 |
| Payment of operating lease rentals of premises | | | |
| - to fellow subsidiaries | (iv)(a),(iv)(c) | **308** | 333 |
| Property sub-lease rentals to fellow subsidiaries | (iv)(a),(iv)(c) | **6** | 6 |
| Common corporate services income from ultimate holding company | (vi) | **39** | 51 |
| Common corporate services expenditure paid to ultimate holding company | (vi) | **214** | 162 |

## 26 Related party transactions *(continued)*

| | Note | Six months ended June 30 **2007** RMB million Unaudited | 2006 RMB million Unaudited |
|---|---|---|---|
| Support services received | | | |
| - from fellow subsidiaries | (vii) | **232** | 373 |
| - from other related companies | (vii) | **7** | 40 |
| Subtotal | | **239** | 413 |
| Telecommunications rental income from other state-controlled telecommunications operators | (iv)(b) | **336** | 135 |
| Payment for lease of Telecommunications facility | | | |
| - to ultimate holding company | (viii) | **32** | 37 |
| - to fellow subsidiaries | (viii) | **110** | 153 |
| Subtotal | | **142** | 190 |
| Payment for purchase of long-term telecommunications capacity to fellow subsidiaries | (ix)(xii) | **—** | 36 |
| Payment for lease of long-term telecommunications capacity to fellow subsidiaries | (x)(xii) | **—** | 65 |
| Management fee received from fellow subsidiaries | (xi)(xii) | **—** | 23 |
| Information communication technologies service received | | | |
| - from ultimate holding company | (xix) | **30** | — |
| - from fellow subsidiaries | (xix) | **16** | — |
| Subtotal | | **46** | — |

Note:

(i) Represents the emoluments paid to all of the directors and the top management of the Group, who are considered as the related parties of the Group.

(ii) The Group entered into finance lease arrangements with a related party, details have been set out in Note 19(b)(ii).

(iii) Other related companies represent the non-listed investees of the fellow subsidiaries.

## 26 Related party transactions *(continued)*

Note: *(continued)*

(iv) Priced based on one of the following three criteria:

(a) market price;

(b) prices based on government guidance; or

(c) cost plus basis.

(v) Represents provision of ancillary telecommunications support services to the Group by the fellow subsidiaries and the related companies. These services include certain telecommunications pre-sale, on-sale and after-sale services, certain sales agency services, the printing and delivery of invoice services, the maintenance of certain air-conditioning, fire alarm equipment and telephone booths and other customer services.

(vi) The Group entered into a Master Service Sharing agreement with China Netcom Group pursuant to which expenses associated with common corporate services is allocated between the Group and China Netcom Group based on total asset as appropriate.

(vii) Represents the support services provided to the Group by the fellow subsidiaries and the related companies. These support services include equipment leasing services, motor vehicles services, safety and security services, conference services, basic construction agency services, equipment maintenance services, employee training services, advertising services, printing services and other support services.

(viii) The Group entered into a Telecommunications Facilities Leasing Agreement with China Netcom Group pursuant to which the Group leases the international telecommunications facilities and inter-provincial transmission optic fibers from China Netcom Group. The lease payment is based on the depreciation charge of the assets.

(ix) The Group entered into a Capacity Purchase Agreement with East Asia Netcom Limited (''EANL''), formerly a wholly owned subsidiary of China Netcom Group, pursuant to which the Group receives certain amounts of long-term telecommunications capacity from China Netcom Group at market prices as set out in the Capacity Purchase Agreement.

(x) The Group entered into a Capacity Lease Agreement with EANL, pursuant to which the Group leases certain amount of capacity of China Netcom Group's telecommunications network at market rates as set out in the Capacity Lease Agreement.

(xi) The Group entered into a Management Services Agreement with EANL, pursuant to which the Group provides certain management services to China Netcom Group either on a cost reimbursement basis or on the basis of cost plus reasonable profits not exceeding the market price as set out in the Management Service Agreement.

(xii) Due to the disposal of ANC Group on August 22, 2006, the Capacity Purchase Agreement, the Capacity Lease Agreement and the Management Services Agreement between the Group and East Asia Netcom Ltd (a formerly wholly owned subsidiary of China Netcom Group) were no longer related party transactions to the Group after August 22, 2006.

(xiii) In addition, pursuant to the Listing Reorganisation and the Acquisition, China Netcom Group have agreed to hold and maintain, for the Group's benefit, all licenses received from the MII in connection with the Restructured Businesses transferred to the Group. The licenses maintained by China Netcom Group were granted by the MII at nil or nominal costs. To the extent that China Netcom Group incurs a cost to maintain or obtain licenses in the future, the Company has agreed reimburse China Netcom Group for any such expense.

(xiv) China Netcom Group has also agreed to indemnify the Group in connection with any tax and deferred tax liabilities of New Horizon not recognised in the financial statements of the Group arising from transactions prior to the date of Listing Reorganisation and the Acquisition in relation to the business of the Group prior to the Acquisition by Telecom and the business of the newly required four provinces/autonomous region respectively.

(xv) As at June 30, 2007, China Netcom Group and Bank of China Limited granted corporate guarantee to the Group as set out in Note 19(b)(i) and Note 19(c).

## 26 Related party transactions *(continued)*

Note: *(continued)*

(xvi) China Netcom Group, the Group's ultimate holding company, entered into an agreement (the "Sponsorship Agreement") with Beijing Organizing Committee ("BOCOG") which designated China Netcom Group as the exclusive fixed-line telecommunications services partner in the People's Republic of China ("PRC") to sponsor the 2008 Beijing Olympic Games. China Netcom Group allocated the sponsorship fee to its members based on the estimated future benefits derived from the Sponsorship Agreement to respective members and the Group has contributed a portion of the required support under the Sponsorship Agreement through providing cash to BOCOG amounting to RMB 540 million. Accordingly, an intangible asset and a payable to the ultimate holding company of the said amount have been recognised on the Group's balance sheet.

(xvii) At June 30, 2007, the Group has balances with other state-controlled telecommunication service providers and loans granted from state-controlled banks as set out in Notes 10, 11, 18 and 19 respectively.

(xviii) For six months period, the deferred consideration related the Acquisition of New Horizon paid to China Netcom Group amounted to RMB 2,940 million, and the balance of deferred consideration amounted to RMB 6,860million at June 30 2007 (December 31, 2006: RMB 7,840 million) . The related interest charged for six months period ended June 30, 2007 amounted to RMB 766 million (for the six months period ended June 30, 2006: RMB 567 million).

(xix) China Netcom System Integration, an indirect wholly owned subsidiary of the Company, entered into an Information and Communications Technology Agreement on November 7, 2006 with China Netcom Group. Pursuant to the Information and Communications Technology Agreement, China Netcom System Integration (and its subsidiaries) will provide Information Communications Technology Services to China Netcom Group. China Netcom System Integration will also subcontract services ancillary to the provision of Information Communications Technology Services, namely the System Installation and Configuration Services to the subsidiaries and branches of China Netcom Group in China Netcom Group's southern service region in PRC.

(xx) On January 15, 2007, CNC China entered into an assets transfer agreement with its ultimate holding Company, China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality branches in the PRC for consideration of RMB 3.5 billion. On February 14, 2007, the independent shareholders passed an ordinary resolution to approve the disposal. The disposal was completed on February 28, 2007 upon the approval granted from MII.

## 27 Ultimate holding party

The ultimate holding company is China Netcom Group which is owned and controlled by PRC Government.

## 28 Approval of financial statements

The unaudited consolidated condensed financial statements were approved by the Board of Directors on August 22, 2007.

# Supplementary Information for American Depositary Share Holders

The consolidated financial statements of the Group have been prepared in accordance with HKFRS, which differs in certain material respects from those prepared under generally accepted accounting principles in the United States ("U.S.GAAP"). Differences between HKFRS and U.S.GAAP ("GAAP difference"), which may have significant impacts on the consolidated net income/(loss) and the consolidated shareholders' equity are described below.

The effect on net profit/ (loss) of significant differences between HKFRS and U.S.GAAP for the six months ended June 30, 2007 and 2006 is as follows:

| | **Six months ended June 30** | | |
|---|---|---|---|
| | **2006** | **2007** | **2007** |
| | Unaudited | Unaudited | Unaudited |
| | RMB million except per share data | | US$ million except per share data |
| | Restated Note 2 | | |
| Profit from continuing operations under HKFRS | 7,194 | 6,089 | 800 |
| U.S.GAAP adjustments: | | | |
| Revaluation of fixed assets | (2,400) | (2,389) | (314) |
| Tax effect on the above adjustments | 792 | 788 | 103 |
| Change in statutory taxation rate (Note a) | — | 349 | 46 |
| Profit from continuing operations under U.S.GAAP | 5,586 | 4,837 | 635 |
| (Loss)/profit from discontinued operations under HKFRS | (100) | 624 | 82 |
| U.S.GAAP adjustments: | | | |
| Revaluation of fixed assets | (36) | (10) | (1) |
| Tax effect on the above adjustments | 12 | 3 | — |
| Gain on disposal of Guangdong and Shanghai branches (Note b) | — | (626) | (82) |
| Loss from discontinued operations under US GAAP | (124) | (9) | (1) |
| Consolidated profit for the period under HKFRS | 7,094 | 6,713 | 882 |
| Consolidated profit for the period under U.S.GAAP | 5,462 | 4,828 | 634 |
| Shares used in computing basic earnings per share (in million) | 6,596 | 6,652 | 6,652 |
| Shares used in computing diluted earnings per share (in million) | 6,647 | 6,731 | 6,731 |

# Supplementary Information for American Depositary Share Holders

| | Six months ended June 30 | | |
|---|---|---|---|
| | **2006** | **2007** | **2007** |
| | Unaudited<br>RMB million except per share data<br>Restated<br>Note 2 | Unaudited | Unaudited<br>US$ million<br>except per<br>share data |
| Earnings per share for profit from continuing operations attributable to shareholders of the Company for the period under U.S. GAAP | | | |
| - Basic earnings per share | RMB 0.85 | RMB 0.73 | USD 0.10 |
| - Diluted earnings per share | RMB 0.84 | RMB 0.72 | USD 0.09 |
| Loss per share for loss from discontinued operations attributable to shareholders of the Company for the year under U.S. GAAP | | | |
| - Basic (loss) per share | RMB(0.02) | — | — |
| - Diluted (loss) per share | RMB(0.02) | — | — |
| Earnings per share for profit attributable to shareholders of the Company for the period under U.S. GAAP | | | |
| - Basic earnings per share | RMB 0.83 | RMB 0.73 | USD 0.10 |
| - Diluted earnings per share | RMB 0.82 | RMB 0.72 | USD 0.09 |

The effect on shareholders' equity of significant differences between HKFRS and U.S. GAAP as at December 31 2006 and June 30 2007 is as follows:

| | **As at December 31 2006** | **As at June 30 2007** | **As at June 30 2007** |
|---|---|---|---|
| | Unaudited<br>RMB million | Unaudited<br>RMB million | Unaudited<br>US$ million |
| Consolidated shareholders' equity under HKFRS | 73,978 | 76,618 | 10,061 |
| U.S.GAAP adjustments: | | | |
| Revaluation of fixed assets | 30,704 | 30,704 | 4,032 |
| Depreciation on revaluation of fixed assets | (13,258) | (15,657) | (2,056) |
| Tax effect on the above adjustments | (5,757) | (4,064) | (534) |
| Consolidated shareholders' equity under U.S.GAAP | 85,667 | 87,601 | 11,503 |

# Supplementary Information for American Depositary Share Holders

Note a: As set out in note 7 to the interim financial statements, the enterprise income tax rate for domestic enterprises will decrease from 33% to 25% with effect from January 1, 2008. Under U.S.GAAP, as at March 16, 2007, the accumulated deferred tax liabilities resulted from the difference in fixed assets valuation and its depreciation effect has been written down by RMB 902 million. The write-down is a direct credit to income statement. Besides, the write-down of net deferred tax assets of RMB 553 million recognised in equity under HK GAAP should be recognized in income statement under U.S. GAAP. Therefore, under U.S.GAAP, the net impact on the income statement reconciliation in respect of change in statutory tax rate is an increase in profit of RMB 349 million.

Note b: As set out in note 2 to the interim financial statements, the disposal of Guangdong and Shanghai branches was completed on February 28, 2007. It is a disposal under common control. Under HKFRS, the gain on disposal was recognised in the income statement while under U.S. GAAP, the gain was recognised directly in the shareholders' equity.

Apart from Notes a and b above, the details of other GAAP differences are set out in the Company's 2006 financial statements.

# Other Information

## Directors' and chief executive's interests in shares and short positions

Some of the directors and the chief executive of the Company personally hold options to subscribe for ordinary shares of the Company. Details of such options are disclosed under the paragraph "Directors', chief executive's and employees' rights to acquire shares" below. These share options were granted pursuant to the terms of the share option scheme adopted by the Company on September 30, 2004 and subsequently amended on December 6, 2005 and May 16, 2006 (the "Share Option Scheme").

Apart from those disclosed herein, as at June 30, 2007, none of the directors nor the chief executive of the Company had any interests or short positions in any of the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of the Securities and Futures Ordinance (the "SFO")) that is required to be recorded and kept in the register in accordance with section 352 of the SFO, any interests required to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code").

## Directors', chief executive's and employees' rights to acquire shares

### Share Option Scheme of the Company

During the six months ended June 30, 2007, no share option has been granted under the Share Option Scheme.

As at June 30, 2007, the directors and the chief executive of the Company, the employees of the Group and certain other persons had the following personal interests in options to subscribe for shares of the Company granted under the Share Option Scheme.

| | No. of shares involved in the options outstanding at the beginning of the period | No. of shares involved in the options outstanding at the period end | Date on which options were granted | No. of shares involved in the options cancelled during the period | No. of shares acquired on exercise of options during the period | Price per share to be paid on exercise of options HK$ |
|---|---|---|---|---|---|---|
| **Directors** | | | | | | |
| Zhang Chunjiang | 920,000 | 920,000 | October 22, 2004 | — | — | 8.40 |
| Zuo Xunsheng (also the chief executive officer) | 480,000 | 480,000 | October 22, 2004 | — | — | 8.40 |
| Zhang Xiaotie | 480,000 | 450,000 | October 22, 2004 | — | 30,000 | 8.40 |
| Miao Jianhua | 420,000 | 280,000 | October 22, 2004 | — | 140,000 | 8.40 |
| Li Fushen | 480,000 | 480,000 | October 22, 2004 | — | — | 8.40 |
| Tian Suning | 920,000 | 920,000 | October 22, 2004 | — | — | 8.40 |
| Yan Yixun | 354,000* | 354,000 | October 22, 2004 | — | — | 8.40 |
| **Employees and other persons granted with options after the date of listing of the Company's shares on the Hong Kong Stock Exchange** | 79,034,200 | 79,034,200 | December 6, 2005 | — | — | 12.45 |
| **Employees and other persons granted with options before the date of listing of the Company's shares on the Hong Kong Stock Exchange** | 93,558,700** | 85,159,410 | October 22, 2004 | 1,827,190 | 6,572,100 | 8.40 |
| **Total** | 176,646,900 | 168,077,610 | | 1,827,190 | 6,742,100 | |

* Mr. Yan Yixun has committed that all after-tax proceeds from the sale of shares acquired on the exercise of his options will be donated to the disadvantaged groups in society and people and groups in need of donations.

** The number of shares involved in the options outstanding at the beginning of the period included share options granted to Ms. Li Liming involving a total of 420,000 shares. Ms. Li Liming resigned as a non-executive director of the Company in January 2007.

# Other Information

Notes:

(a) The total number of shares involved in the options outstanding at period end represents 2.52 per cent. of the issued share capital of the Company as at June 30, 2007.

(b) Grantees of the share options granted on October 22, 2004 are entitled to exercise the options in the following periods:

(i) in respect of 40 per cent. of the options granted, from May 17, 2006 to November 16, 2010;

(ii) in respect of a further 20 per cent. of the options granted, from May 17, 2007 to November 16, 2010;

(iii) in respect of a further 20 per cent. of the options granted, from May 17, 2008 to November 16, 2010; and

(iv) in respect of the remaining 20 per cent. of the options granted, from May 17, 2009 to November 16, 2010.

(c) Grantees of the share options granted on December 6, 2005 are entitled to exercise the options in the following periods:

(i) in respect of 40 per cent. of the options granted, from December 6, 2007 to December 5, 2011;

(ii) in respect of a further 20 per cent. of the options granted, from December 6, 2008 to December 5, 2011;

(iii) in respect of a further 20 per cent. of the options granted, from December 6, 2009 to December 5, 2011; and

(iv) in respect of the remaining 20 per cent. of the options granted, from December 6, 2010 to December 5, 2011.

Details of share options exercised during the period:

| **Period during which options were exercised** | **Exercise price HK$** | **Weighted average closing price per share immediately before dates of exercise of options HK$** | **Proceeds received HK$** | **Number of shares involved in the options** |
|---|---|---|---|---|
| From January 2, 2007 to June 29, 2007 | 8.40 | 21.16 | 56,633,640 | 6,742,100 |

# Other Information

## Substantial interests in the share capital of the Company

The Company has been notified of the following interests in the Company's issued shares as at June 30, 2007 amounting to 5 per cent. or more of the ordinary shares in issue:

| | Capacity | Number of ordinary shares held | Percentage of total issued shares |
|---|---|---|---|
| China Network Communications Group Corporation | Interest of controlled corporations | 4,945,148,000[(1)(2)] | 74.28% |
| China Netcom Group Corporation (BVI) Limited | Beneficial owner | 4,647,449,014 | |
| | Interest of controlled corporations | 1 | |
| | Trustee | 297,698,985 | |
| | Total | 4,945,148,000[(1)(2)] | 74.28% |
| AllianceBernstein L.P. | Interest of controlled corporations | 41,514,400 | |
| | Investment manager | 357,326,792 | |
| | Total | 398,841,192 | 5.99% |

Notes:

(1) China Network Communications Group Corporation ("China Netcom Group") beneficially owns 4,647,449,014 shares held by its wholly-owned subsidiary, China Netcom Group Corporation (BVI) Limited ("CNC BVI") and 1 share held by CNC Cayman, Limited, a wholly-owned subsidiary of CNC BVI. The percentage of total issued share capital of the Company beneficially held by China Netcom Group is 69.81 per cent..

(2) China Netcom Group is deemed under the SFO to be interested in 297,698,985 shares held by CNC BVI as trustee on behalf of certain shareholders, representing 4.47 per cent. of the issued share capital of the Company.

Apart from the foregoing, as at June 30, 2007, no person or corporation is recorded in the registers required to be kept under section 336 of the SFO as having an interest in 5 per cent. or more of or any short position in the issued share capital of the Company.

## Discussion and analysis of the Company's performance

In compliance with paragraph 40(2) of Appendix 16 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules"), the Company confirms that, save for the completion of the disposal by the Company of the telecommunications assets, liabilities and business in Guangdong Province and Shanghai Municipality on February 28, 2007 (details of which are set out in the Company's announcement dated January 15, 2007), and the adjustment to tariffs for inter-district voice calls by the Company's subsidiaries in certain provinces as required by the relevant regulatory authorities of the government, the current information in relation to those matters set out in paragraph 32 of Appendix 16 to the Listing Rules as applicable to the Company has not changed materially from the information disclosed in the Company's 2006 Annual Report.

# Other Information

## Interim dividend

The board of directors of the Company have resolved that no interim dividend be paid for the six months ended June 30, 2007.

## Audit Committee

The Audit Committee reviewed with management the accounting policies and practices adopted by the Group and discussed auditing, internal control and financial reporting matters including the review of the unaudited interim financial statements for the six months ended June 30, 2007.

## Compliance with the code provisions set out in the Code on Corporate Governance Practices

The Company has complied with all code provisions of the Code on Corporate Governance Practices as set out in Appendix 14 to the Listing Rules throughout the six months ended June 30, 2007.

Under the amended Section 303A of the New York Stock Exchange Listed Company Manual, foreign issuers (including the Company) listed on the New York Stock Exchange, Inc. (the "NYSE") are required to disclose a summary of the significant differences between their domestic corporate governance rules and NYSE corporate governance rules that would apply to a U.S. domestic issuer. A summary of such differences appears on our website at http://www.china-netcom.com/english/inv/Corporate_Governance_Differences.htm.

## Compliance with the Model Code

The Company has adopted the Model Code as set out in Appendix 10 to the Listing Rules. All directors have confirmed, following enquiry by the Company, that they have complied with the required standard set out in the Model Code throughout the period from January 1, 2007 to June 30, 2007.

## Purchase, sale or redemption of the Company's listed securities

During the six months ended June 30, 2007, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

## Forward-looking statements

This interim report includes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Save for statements of historical facts, all statements in this interim report that address activities, events or developments which the Company expects or anticipates will or may occur in the future are hereby identified as forward looking statements for the purpose of the safe harbour provided by Section 27A of the U.S. Securities Act of 1933, as amended, and Section 21E of the U.S. Securities Exchange Act of 1934, as amended. The words such as believe, intend, expect, anticipate, project, estimate, predict, plan and similar expression are also intended to identify forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual performance, financial condition or results of operations of the Company to be materially different from any future performance, financial condition or results of operations implied by such forward-looking statements. Further information regarding these risks, uncertainties and other factors is included in the Company's Annual Report on Form 20-F filed with the U.S. Securities and Exchange Commission (the "SEC") and in the Company's other filings with the SEC.