

Dear Shareholders,

2004 was “the year of transformation” as well as a year of many key breakthroughs for us. Despite of challenges and competition in China’s telecommunications market, we successfully completed an internal restructuring and listed overseas. We streamlined our management and reporting system to improve efficiency and implemented an effective system to enhance corporate governance. With the trust and great support from the Board of Directors, and the tremendous effort of both the management team and the staff, we achieved excellent operating results in 2004.

1. Our financial results for 2004 were substantially improved

In 2004, as a result of restructuring and business innovations, we delivered a sequential growth in financial results and continuing improvement in operational efficiency. We generated revenue of RMB64,922 million and net profit of RMB9,248 million, representing an increase of RMB5,024 million and RMB20,359 million over previous year. According to the unaudited pro forma financials prepared in accordance with the relevant requirements under the US Securities Act, we recorded consolidated pro forma revenue (excluding upfront connection fees) of RMB61,055 million for 2004, an increase of 8.9% over 2003. Our unaudited consolidated pro forma EBITDA (excluding upfront connection fees) reached RMB30,379 million, an increase of RMB3,932 million over 2003. Our unaudited consolidated pro forma EBITDA margin (excluding upfront connection fees) reached 49.8%. Unaudited consolidated pro forma net profit (excluding upfront connection fees) was RMB6,623 million. After excluding the effects of reorganisation costs and a revaluation of deficits, unaudited consolidated pro forma net profit (excluding upfront connection fees) increased by RMB1,687 million or 34.2% over 2003.

In 2004, in addition to steadily growing our core business, we strengthened our internal controls for capital expenditure by implementing a stringent, centralized capex system. These measures helped ensure the robust growth of free cash flow. Already as a result, our free cash flow turned positive in 2004, representing a net increase of RMB8,827 million from 2003. With this major achievement, we laid a solid foundation for our company’s future growth.

2. Our business continued to grow rapidly

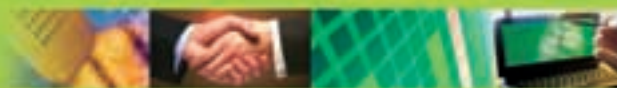
During the past year, China’s telecom industry remained very challenging due to increased competition and rising mobile substitution. In such an environment, we focused on the development of our broadband and local telephone businesses and intensified the promotion of value-added services through leveraging our network resources and customer base. We maintained our dominant position in the northern provinces and achieved further growth in the southern provinces and international markets.

In 2004, the successful implementation of our growth strategy for the PHS business resulted in a significant 15.5% year-to-year increase in our fixed-line telephone service subscribers. The total number of subscribers for our local telephone services reached 80.383 million, representing a 94.5% market share in our northern service region. With robust demand for broadband services, our broadband subscribers as of 31 December 2004 reached 6.218 million, representing a 145.3% increase over 2003. Our broadband market share in our northern service region reached a new high of 95.8% in 2004, representing a 6 percentage point gain over 2003. The broadband business has indeed become the new engine for our robust growth. While our core businesses continue to grow at a double digit pace, we devoted considerable effort to develop and promote value-added services as a new growth driver, which resulted in growing adoption and usage by our subscribers. Among which, PHS short messages recorded a growth of 1,503.4% over the same period of last year. The caller identification penetration rate reached 58.2%, representing a 8.6% increase over last year. The acquisition of certain businesses from Asia Global Crossing Limited at the end of 2003 allowed us to establish a unique pan-Asian network platform that is centered around China. Through further consolidation and integration of our Asian operations in our northern and southern service regions of China, we further enhanced our unique competitive advantage in providing one-stop data services to corporate customers, which contributed to the rapid growth in revenue in our southern service region as well as our international telecommunications services.

3. Our streamlined internal management structure generated positive results

In 2004, we achieved a major breakthrough by reorganizing our internal management structure transforming from the original "Parent-Subsidiary" structure to "Headquarter-Branch" structure. As a result, our corporate management can directly oversee the activities of provincial branches. This new structure provides a good base for effectively managing the organization and enhancing operational efficiency.

Under such "Headquarter-Branch" structure, we implemented new management processes in five areas, including finance, human resources, sales and marketing, network operation and maintenance, and construction planning, in order to realize operational synergies and increase efficiencies. Our customer satisfaction and loyalty were improved due to more coordinated marketing and sales efforts. At the same time, a series of measures were adopted to control costs and improve efficiency in network operation and maintenance. We achieved effective control over operating expenses. According to the unaudited pro forma financials prepared pursuant to the US Securities Act, the operating expenses accounted for 79.7% of the total revenues (being the unaudited consolidated revenues excluding upfront connection fees), representing a decrease of 2.4% over previous year. After excluding the effects of depreciation, the Company's ratio of operating expenses to revenue (calculated with the same standard as above) was 50.2%, dropped by 2.6% over previous year. Among which, the ratio of network, operations and support



expenses and staff cost to revenue dropped by 3.6% and 0.7% against previous year. The ratio of selling, general and administrative expenses to revenue increased by 1.9%. Although the Company has adopted proactive selling activities resulting in substantial growth in sales expenses, the general and administrative expenses recorded a greater drop over previous year.

In addition to achieving effective control over operating expenses, we also managed to keep capital expenditure at a reasonable level. We adopted stringent measures in controlling capital expenditure in 2004. We were able to balance long-term growth and investment return by focusing on businesses with high returns and great market potential such as broadband and data. This led to a reduction in capital expenditure of 25.6% in 2004.

Establishing effective internal controls and a sound management system have been one of the priorities on our management agenda. In October of 2004, we retained an international renowned consulting firm to help us design and implement a robust internal control system. Through these efforts, we intend to establish an internal control and management system that complies with the best international standards to further reduce our operating risks.

4. 2005 Outlook

2005 will be a year of both opportunities and challenges for the Company. China is expected to maintain its robust economic growth and demand for communications services, particularly broadband access, will continue to grow. With the increase in direct foreign investment in China and China's further integration into the world economy, demand for telecommunications services between China and the rest of the world will continue to increase. At the same time, we are facing strong challenges as mobile substitution continues and competition intensifies. In such an environment, we will continue focusing on promoting growth and efficiency within the Company and on executing our three core strategies, 'Broadband, Olympic and International'. We will further improve management efficiency, achieve sustainable growth and maximize value for our shareholders.

Looking into 2005, I sincerely believe that with the support of the Board of Directors and the joint efforts of our management and staff, we will continue to provide quality services to our customers and deliver superior return to our shareholders.

Lastly, I would like to take this opportunity to express my most sincere gratitude to our customers, our shareholders, the Board of Directors and our dedicated, hardworking employees for all your support in the last year.

Tian Suning
Vice Chairman and Chief Executive Officer

6 April 2005