CONSOLIDATED INCOME STATEMENT

(Prepared under Hong Kong financial reporting standards)
Year ended 31 December 2006

	Notes	**2006 RMB'000**	2005 RMB'000
REVENUE	5	**23,031,684**	21,575,920
Cost of sales		**(15,250,453)**	(14,101,720)
Gross profit		**7,781,231**	7,474,200
Other income and gains	5	**792,124**	681,646
Research and development costs		**(2,832,685)**	(1,959,543)
Selling and distribution costs		**(3,274,699)**	(3,186,442)
Administrative expenses		**(1,097,615)**	(1,095,400)
Other expenses		**(191,495)**	(128,605)
Finance costs	7	**(153,694)**	(175,884)
Share of profits and losses of:			
Jointly-controlled entities		**(652)**	(1,198)
Associates		**8,175**	(2,969)
PROFIT BEFORE TAX	6	**1,030,690**	1,605,805
Tax	10	**(127,078)**	(179,851)
PROFIT FOR THE YEAR		**903,612**	1,425,954
Attributable to:			
Equity holders of the parent	11	**766,972**	1,287,701
Minority interests		**136,640**	138,253
		903,612	1,425,954
DIVIDEND			
Proposed final	12	**143,928**	239,880
EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT	13		
Basic		**RMB0.80**	RMB1.34
Diluted		**RMB0.80**	N/A

CONSOLIDATED BALANCE SHEET

(Prepared under Hong Kong financial reporting standards)
31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	15	**3,053,019**	2,470,965
Prepaid land premiums/land lease payments	16	**55,146**	55,062
Intangible assets	17	**274,905**	335,835
Investments in jointly-controlled entities	19	**5,936**	6,588
Investments in associates	20	**51,257**	35,583
Available-for-sale investments	21	**43,488**	43,288
Long-term trade receivables	24	**372,703**	307,666
Factored long-term trade receivables	25	**1,399,206**	687,765
Deferred tax assets	36	**210,923**	59,587
Total non-current assets		**5,466,583**	4,002,339
CURRENT ASSETS			
Prepaid land premiums/land lease payments	16	**1,449**	1,418
Inventories	22	**2,481,155**	2,240,327
Amount due from customers for contract work	23	**5,833,480**	4,689,157
Trade and bills receivables	24	**6,988,034**	4,686,775
Factored trade receivables	25	**152,848**	36,416
Prepayments, deposits and other receivables	26	**1,497,323**	1,188,313
Loan receivables	27	**22,026**	46,165
Equity investments at fair value through profit or loss	28	**33,288**	—
Pledged bank deposits	29	**168,997**	175,899
Cash and cash equivalents	29	**4,142,063**	5,397,233
Total current assets		**21,320,663**	18,461,703
CURRENT LIABILITIES			
Trade and bills payables	30	**6,991,665**	6,269,792
Amount due to customers for contract work	23	**996,275**	733,455
Other payables and accruals	31	**2,732,572**	2,900,137
Interest-bearing bank borrowings	32	**945,726**	599,695
Bank advances on factored trade receivables	25	**152,848**	36,416
Tax payable		**297,913**	114,672
Dividend payables		**83,941**	163,008
Total current liabilities		**12,200,940**	10,817,175
NET CURRENT ASSETS		**9,119,723**	7,644,528
TOTAL ASSETS LESS CURRENT LIABILITIES		**14,586,306**	11,646,867

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CONSOLIDATED BALANCE SHEET

(Prepared under Hong Kong financial reporting standards)
31 December 2006

	Notes	**2006 RMB'000**	2005 RMB'000
TOTAL ASSETS LESS CURRENT LIABILITIES		**14,586,306**	11,646,867
NON-CURRENT LIABILITIES			
Interest-bearing bank borrowings	32	**1,679,242**	80,000
Bank advances on factored long-term trade receivables	25	**1,399,206**	687,765
Financial guarantee contract	42(g)	**3,689**	—
Provision for retirement benefits	33	**32,058**	30,459
Other long-term payables	34	**146,274**	127,402
Total non-current liabilities		**3,260,469**	925,626
Net assets		**11,325,837**	10,721,241
EQUITY			
Equity attributable to equity holders of the parent			
Issued capital	37	**959,522**	959,522
Reserves	39(a)	**9,660,495**	9,051,110
Proposed final dividend	12	**143,928**	239,880
		10,763,945	10,250,512
Minority interests		**561,892**	470,729
Total equity		**11,325,837**	10,721,241

Hou Weigui
Director

Yin Yimin
Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(Prepared under Hong Kong financial reporting standards)
Year ended 31 December 2006

		Attributable to equity holders of the parent								
	Note	Issued capital RMB'000	Capital reserve RMB'000	Statutory reserves RMB'000	Exchange fluctuation reserve RMB'000	Retained profits RMB'000	Proposed final dividend RMB'000	Total RMB'000	Minority interests RMB'000	Total equity RMB'000
At 1 January 2005		959,522	5,462,515	985,356	3,786	1,566,093	239,880	9,217,152	478,380	9,695,532
Exchange realignments and other income recognised directly in equity		—	5,306	—	(19,767)	—	—	(14,461)	(3,111)	(17,572)
Total income and expense for the year recognised directly in equity		—	5,306	—	(19,767)	—	—	(14,461)	(3,111)	(17,572)
Profit for the year		—	—	—	—	1,287,701	—	1,287,701	138,253	1,425,954
Total income and expense for the year		—	5,306	—	(19,767)	1,287,701	—	1,273,240	135,142	1,408,382
Final 2004 dividend declared		—	—	—	—	—	(239,880)	(239,880)	—	(239,880)
Acquisition of subsidiaries		—	—	—	—	—	—	—	19,115	19,115
Disposal of subsidiaries		—	—	—	—	—	—	—	(11,555)	(11,555)
Acquisition of minority interests		—	—	—	—	—	—	—	(9,704)	(9,704)
Dividends declared to and paid to minority shareholders		—	—	—	—	—	—	—	(165,876)	(165,876)
Capital contributions by minority shareholders		—	—	—	—	—	—	—	25,227	25,227
Transfer from retained profits		—	38,603	278,704	—	(317,307)	—	—	—	—
Proposed final 2005 dividend	12	—	—	—	—	(239,880)	239,880	—	—	—
At 31 December 2005		959,522	5,506,424	1,264,060	(15,981)	2,296,607	239,880	10,250,512	470,729	10,721,241

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CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(Prepared under Hong Kong financial reporting standards)
Year ended 31 December 2006

		Attributable to equity holders of the parent									
	Notes	Issued capital RMB'000	Capital reserve RMB'000	Share incentive scheme reserve RMB'000	Statutory reserves RMB'000	Exchange fluctuation reserve RMB'000	Retained profits RMB'000	Proposed final dividend RMB'000	Total RMB'000	Minority interests RMB'000	Total equity RMB'000
At 1 January 2006		959,522	5,506,424	—	1,264,060	(15,981)	2,296,607	239,880	10,250,512	470,729	10,721,241
Exchange realignments and other income recognised directly in equity		—	760	—	—	(16,899)	—	—	(16,139)	(7,429)	(23,568)
Total income and expense for the year recognised directly in equity		—	760	—	—	(16,899)	—	—	(16,139)	(7,429)	(23,568)
Profit for the year		—	—	—	—	—	766,972	—	766,972	136,640	903,612
Total income and expense for the year		—	760	—	—	(16,899)	766,972	—	750,833	129,211	880,044
Final 2005 dividend declared		—	—	—	—	—	—	(239,880)	(239,880)	—	(239,880)
Disposal of subsidiaries		—	—	—	—	—	—	—	—	(100)	(100)
Acquisition of minority interests		—	—	—	—	—	—	—	—	(31,069)	(31,069)
Dividends declared to minority shareholders		—	—	—	—	—	—	—	—	(37,245)	(37,245)
Capital contributions by minority shareholders		—	—	—	—	—	—	—	—	30,366	30,366
Transfer from retained profits		—	—	—	66,999	—	(66,999)	—	—	—	—
Proposed final 2006 dividend	12	—	—	—	—	—	(143,928)	143,928	—	—	—
Equity settled share expense	38	—	—	2,480	—	—	—	—	2,480	—	2,480
At 31 December 2006		959,522	5,507,184*	2,480*	1,331,059*	(32,880)*	2,852,652*	143,928	10,763,945	561,892	11,325,837

* These reserve accounts comprise the consolidated reserves of approximately RMB9,660,495,000 (2005: RMB9,051,110,000) in the consolidated balance sheet.

CONSOLIDATED CASH FLOW STATEMENT

(Prepared under Hong Kong financial reporting standards)
Year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax		**1,030,690**	1,605,805
Adjustments for:			
Finance costs	7	**153,694**	175,884
Share of profits and losses of jointly-controlled entities		**652**	1,198
Share of profits and losses of associates		**(8,175)**	2,969
Bank and other interest income	5	**(49,050)**	(54,870)
Government grants	5	**(22,544)**	(139,491)
Depreciation	6	**510,333**	386,859
Recognition of prepaid land lease payments	16	**1,418**	1,317
Write-down of inventories to net realisable value	6	**52,781**	96,185
Impairment of trade receivables	6	**111,611**	15,642
Impairment of goodwill	6	**—**	56,267
Amortisation of intangible assets	6	**101,558**	82,735
Loss on disposal of items of property, plant and equipment	6	**13,933**	6,163
Loss on disposal of intangible assets	6	**952**	70
Loss on disposal of interests in subsidiaries	6	**—**	2,057
Gain on deemed disposal of interests in a subsidiary	5	**—**	(3,655)
Gain on disposal of an equity investment at fair value through profit or loss	5	**(24,326)**	—
Fair value gain on an equity investment at fair value through profit or loss	5	**(16,595)**	—
Recognition of financial guarantee contracts	6	**3,689**	—
Excess over the cost of business combinations	5	**—**	(12,236)
Equity settled share expense	6	**2,480**	—
		1,863,101	2,222,899
Increase in long-term trade receivables		**(65,037)**	(307,578)
Increase in inventories		**(293,609)**	(733,796)
Increase in amount due from customers for contract work		**(1,144,323)**	(1,937,133)
Decrease/(increase) in trade and bills receivables		**(2,412,870)**	1,217,673
Increase in prepayments, deposits and other receivables		**(309,464)**	(526,433)
Decrease/(increase) in loan receivables		**24,139**	(46,165)
Increase in trade and bills payables		**721,873**	1,943,636
Increase/(decrease) in amount due to customers for contract work		**262,820**	(1,585,276)
Increase/(decrease) in other payables and accruals		**(194,162)**	121,791
Increase in factored trade receivables		**(116,432)**	(36,416)
Increase in factored long-term trade receivables		**(711,441)**	(687,765)
Bank advances on factored trade receivables		**827,873**	724,181
Cash generated from/(used in) operations		**(1,547,532)**	369,618
Interest received		**49,050**	54,870
Interest and other finance costs paid		**(153,694)**	(175,884)
Hong Kong profits tax paid		**(2,929)**	(6,588)
PRC taxes paid		**(82,400)**	(217,663)
Overseas taxes paid		**(12,591)**	(26,553)
Dividends paid		**(239,880)**	(239,880)
Dividends paid to minority shareholders		**(116,312)**	(43,789)
Net cash outflow from operating activities		**(2,106,288)**	(285,869)

continued/...

CONSOLIDATED CASH FLOW STATEMENT

(Prepared under Hong Kong financial reporting standards)
Year ended 31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of leasehold land		**(1,533)**	(3,341)
Purchases of items of property, plant and equipment		**(1,135,742)**	(803,781)
Proceeds from disposal of items of property, plant and equipment		**20,851**	3,727
Additions to intangible assets		**(43,887)**	(206,768)
Receipt of government grants		**41,416**	133,999
Purchases of available-for-sale investments		**—**	(1,999)
Acquisition of an equity investment at fair value through profit or loss		**(39,459)**	—
Proceeds from disposal of an equity investment at fair value through profit or loss		**46,031**	—
Acquisition of associates		**(7,134)**	(16,307)
Acquisition of subsidiaries		**—**	(51,449)
Acquisition of minority interests		**(2,401)**	(3,200)
Disposal of subsidiaries	40	**(289)**	(31,224)
Decrease/(increase) in pledged bank deposits		**6,902**	(86,921)
Net cash outflow from investing activities		**(1,115,245)**	(1,067,264)
CASH FLOWS FROM FINANCING ACTIVITIES			
Capital contributions by minority shareholders		**30,366**	25,227
New bank loans		**3,093,148**	108,695
Repayment of bank loans		**(1,147,875)**	(868,967)
Net cash inflow/(outflow) from financing activities		**1,975,639**	(735,045)
NET DECREASE IN CASH AND CASH EQUIVALENTS		**(1,245,894)**	(2,088,178)
Cash and cash equivalents at beginning of year		**5,397,233**	7,509,245
Effect of foreign exchange rate changes, net		**(9,276)**	(23,834)
CASH AND CASH EQUIVALENTS AT END OF YEAR		**4,142,063**	5,397,233
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS			
Cash and bank balances	29	**3,168,658**	4,178,498
Non-pledged time deposits with original maturity of less than three months when acquired		**973,405**	1,218,735
		4,142,063	5,397,233

BALANCE SHEET

(Prepared under Hong Kong financial reporting standards)
31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment	15	**1,965,507**	1,718,547
Prepaid land premiums/land lease payments	16	**48,106**	49,406
Intangible assets	17	**207,692**	268,427
Investments in subsidiaries	18	**442,314**	408,868
Investments in jointly-controlled entities	19	**2,500**	2,500
Investments in associates	20	**27,314**	24,707
Available-for-sale investments	21	**41,488**	41,288
Long-term trade receivables	24	**328,166**	327,122
Factored long-term trade receivables	25	**1,394,970**	683,598
Deferred tax assets	36	**194,547**	55,113
Total non-current assets		**4,652,604**	3,579,576
CURRENT ASSETS			
Prepaid land premiums/land lease payments	16	**1,300**	1,300
Inventories	22	**1,179,105**	1,278,092
Amount due from customers for contract work	23	**5,809,647**	4,440,842
Trade and bills receivables	24	**7,370,341**	5,690,947
Factored trade receivables	25	**275,830**	5,007
Prepayments, deposits and other receivables	26	**2,858,750**	2,239,947
Pledged bank deposits	29	**35,201**	46,126
Cash and cash equivalents	29	**2,922,719**	4,212,810
Total current assets		**20,452,893**	17,915,071
CURRENT LIABILITIES			
Trade and bills payables	30	**8,891,921**	8,457,453
Amount due to customers for contract work	23	**991,612**	688,876
Other payables and accruals	31	**2,202,881**	2,590,981
Interest-bearing bank borrowings	32	**741,827**	500,000
Bank advances on factored trade receivables	25	**275,830**	5,007
Tax payable		**162,004**	63,974
Dividend payables		**378**	928
Total current liabilities		**13,266,453**	12,307,219
NET CURRENT ASSETS		**7,186,440**	5,607,852
TOTAL ASSETS LESS CURRENT LIABILITIES		**11,839,044**	9,187,428

continued/...

BALANCE SHEET

(Prepared under Hong Kong financial reporting standards)
31 December 2006

	Notes	2006 RMB'000	2005 RMB'000
TOTAL ASSETS LESS CURRENT LIABILITIES		**11,839,044**	9,187,428
NON-CURRENT LIABILITIES			
Interest-bearing bank borrowings	32	**1,329,478**	—
Bank advances on factored long-term trade receivables	25	**1,394,970**	683,598
Financial guarantee contract	42(g)	**3,689**	—
Provision for retirement benefits	33	**32,058**	30,459
Other long-term payables	34	**94,404**	81,111
Total non-current liabilities		**2,854,599**	795,168
Net assets		**8,984,445**	8,392,260
EQUITY			
Issued capital	37	**959,522**	959,522
Reserves	39(b)	**7,880,995**	7,192,858
Proposed final dividend	12	**143,928**	239,880
Total equity		**8,984,445**	8,392,260

Hou Weigui
Director

Yin Yimin
Director

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

1. CORPORATE INFORMATION

ZTE Corporation (the "Company") is a limited liability company incorporated in the People's Republic of China (the "PRC").

The registered office of the Company is located at ZTE Plaza, Keji Road South, Hi-Tech Industrial Park, Nanshan District, Shenzhen 518057, the PRC.

During the year, the Company and its subsidiaries (the "Group") were principally involved in the design, development, manufacture and sale of telecommunications systems equipment and solutions.

In the opinion of the directors, the holding company and the ultimate holding company of the Group is Shenzhen Zhongxingxin Telecommunications Equipment Company, Limited ("Zhongxingxin"), a limited liability company registered in the PRC.

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention except for an equity investment, which has been measured at fair value. These financial statements are presented in Renminbi ("RMB") and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended 31 December 2006. The results of subsidiaries are consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

The acquisition of subsidiaries during the year has been accounted for using the purchase method of accounting. This method involves allocating the cost of the business combinations to the fair value of the identifiable assets acquired, and liabilities and contingent liabilities assumed at the date of acquisition. The cost of the acquisition is measured at the aggregate of the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition.

Minority interests represent the interests of outside shareholders not held by the Group in the results and net assets of the Company's subsidiaries. Acquisitions of minority interests are accounted for using the parent entity extension method whereby the difference between the consideration and the book value of the share of the net assets acquired is recognised as goodwill.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.2 IMPACT OF NEW AND REVISED HONG KONG FINANCIAL REPORTING STANDARDS

The Group has adopted the following new and revised HKFRSs for the first time for the current year's financial statements. Except for in certain cases, giving rise to new and revised accounting policies and additional disclosures, the adoption of these new and revised standards and interpretation has had no material effect on these financial statements.

HKAS 21 Amendment	Net Investment in a Foreign Operation
HKAS 39 & HKFRS 4 Amendments	Financial Guarantee Contracts
HKAS 39 Amendment	The Fair Value Option
HK(IFRIC)-Int 4	Determining whether an Arrangement contains a Lease

The principal changes in accounting policies are as follows:

(a) HKAS 21 *The Effects of Changes in Foreign Exchange Rates*

Upon the adoption of the HKAS 21 Amendment regarding a net investment in a foreign operation, all exchange differences arising from a monetary item that forms part of the Group's net investment in a foreign operation are recognised in a separate component of equity in the consolidated financial statements irrespective of the currency in which the monetary item is denominated. This change has had no material impact on these financial statements as at 31 December 2006 or 31 December 2005.

(b) HKAS 39 *Financial Instruments: Recognition and Measurement*

(i) Amendment for financial guarantee contracts

This amendment has revised the scope of HKAS 39 to require financial guarantee contracts issued that are not considered insurance contracts, to be recognised initially at fair value and to be remeasured at the higher of the amount determined in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets* and the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 *Revenue*. Approximately RMB4 million has been recognised upon the adoption of this amendment at 31 December 2006 and disclosed in note 42(g) to the financial statements and has had no impact on these financial statements as at 31 December 2005.

(ii) Amendment for the fair value option

This amendment has changed the definition of a financial instrument classified as fair value through profit or loss and has restricted the use of the option to designate any financial asset or any financial liability to be measured at fair value through the income statement. The Group had not previously used this option, and hence the amendment has had no effect on the financial statements.

(c) HK(IFRIC)-Int 4 *Determining whether an Arrangement contains a Lease*

The Group has adopted this interpretation as of 1 January 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This interpretation has had no material impact on these financial statements.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.3 IMPACT OF ISSUED BUT NOT YET EFFECTIVE HONG KONG FINANCIAL REPORTING STANDARDS

The Group has not applied the following new and revised HKFRSs, that have been issued but are not yet effective, in these financial statements.

HKAS 1 Amendment	Capital Disclosures
HKFRS 7	Financial Instruments: Disclosures
HKFRS 8	Operating Segments
HK(IFRIC)-Int 7	Applying the Restatement Approach under HKAS 29 *Financial Reporting in Hyperinflationary Economies*
HK(IFRIC)-Int 8	Scope of HKFRS 2
HK(IFRIC)-Int 9	Reassessment of Embedded Derivatives
HK(IFRIC)-Int 10	Interim Financial Reporting and Impairment
HK(IFRIC)-Int 11	Group and Treasury Share Transactions
HK(IFRIC)-Int 12	Services Concession Arrangements

The HKAS 1 Amendment shall be applied for annual periods beginning on or after 1 January 2007. The revised standard will affect the disclosures about qualitative information about the Group's objective, policies and processes for managing capital; quantitative data about what the Company regards as capital; and compliance with any capital requirements and the consequences of any non-compliance.

HKFRS 7 shall be applied for annual periods beginning on or after 1 January 2007. The standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments.

HKFRS 8 shall be applied for annual periods beginning on or after 1 January 2009. The standard requires disclosures of information about the operating segments of the Group, the products and services provided by the segments, the geographical areas in which the Group operates, and revenue from the Group's major customers. This standard will supersede HKAS 14 *Segment Reporting*.

HK(IFRIC)-Int 7, HK(IFRIC)-Int 8, HK(IFRIC)-Int 9, HK(IFRIC)-Int 10, HK(IFRIC)-Int 11 and HK(IFRIC)-Int 12 shall be applied for annual periods beginning on or after 1 March 2006, 1 May 2006, 1 June 2006,1 November 2006, 1 March 2007 and 1 January 2008, respectively.

The Group is in the process of making an assessment of the impact of these new and revised HKFRSs upon initial application. So far, it has concluded that while the adoption of the HKAS 1 Amendment, HKFRS 7 and HKFRS 8 may result in new or amended disclosures, these new and revised HKFRSs are unlikely to have a significant impact on the Group's results of operations and financial position.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Subsidiaries

A subsidiary is an entity whose financial and operating policies the Company controls, directly or indirectly, so as to obtain benefits from its activities.

The results of subsidiaries are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in subsidiaries are stated at cost less any impairment losses.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Joint ventures

A joint venture is an entity set up by contractual arrangement, whereby the Group and other parties undertake an economic activity. The joint venture company operates as a separate entity in which the Group and the other parties have an interest.

The joint venture agreement between the venturers stipulates the capital contributions of the joint venture parties, the duration of the joint venture entity and the basis on which the assets are to be realised upon its dissolution. The profits and losses from the joint venture's operations and any distributions of surplus assets are shared by the venturers, either in proportion to their respective capital contributions, or in accordance with the terms of the joint venture agreement.

A joint venture is treated as:

(a) a subsidiary, if the Group/Company has unilateral control, directly or indirectly, over the joint venture;

(b) a jointly-controlled entity, if the Group/Company does not have unilateral control, but has joint control, directly or indirectly, over the joint venture;

(c) an associate, if the Group/Company does not have unilateral or joint control, but holds, directly or indirectly, generally not less than 20% of the joint venture's registered capital and is in a position to exercise significant influence over the joint venture; or

(d) an equity investment accounted for in accordance with HKAS 39, if the Group/Company holds, directly or indirectly, less than 20% of the joint venture's registered capital and has neither joint control of, nor is in a position to exercise significant influence over, the joint venture.

Jointly-controlled entities

A jointly-controlled entity is a joint venture that is subject to joint control, resulting in none of the participating parties having unilateral control over the economic activity of the jointly-controlled entity.

The Group's share of the post-acquisition results and reserves of jointly-controlled entities is included in the consolidated income statement and consolidated reserves, respectively. The Group's investments in jointly-controlled entities are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

The results of jointly-controlled entities are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in jointly-controlled entities are treated as non-current assets and are stated at cost less any impairment losses.

Associates

An associate is an entity, not being a subsidiary or a jointly-controlled entity, in which the Group has a long-term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Associates (continued)

The Group's share of the post-acquisition results and reserves of associates is included in the consolidated income statement and consolidated reserves, respectively. The Group's investments in associates are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

The results of associates are included in the Company's income statement to the extent of dividends received and receivable. The Company's investments in associates are treated as non-current assets and are stated at cost less any impairment losses.

Goodwill

Goodwill arising on acquisition of subsidiaries represents the excess of the cost of the business combination over the Group's interest in the net fair value of the acquirees' identifiable assets acquired, and liabilities and contingent liabilities assumed as at the date of acquisition.

Goodwill on acquisitions for which the agreement date is on or after 1 January 2005

Goodwill arising on acquisition is recognised in the consolidated balance sheet as an asset, initially measured at cost and subsequently at cost less any accumulated impairment losses.

The carrying amount of goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and
- is not larger than a segment based on either the Group's primary or the Group's secondary reporting format determined in accordance with HKAS 14 *Segment Reporting*.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised.

Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

An impairment loss recognised for goodwill is not reversed in a subsequent period.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Excess over the cost of business combinations

Any excess of the Group's interest in the net fair value of the acquirees' identifiable assets, liabilities and contingent liabilities over the cost of the acquisition of subsidiaries (previously referred to as negative goodwill), after reassessment, is recognised immediately in the income statement.

Impairment of non-financial assets other than goodwill

Where an indication of impairment exists, or when annual impairment testing for an asset is required (other than inventories, construction contract assets, deferred tax assets, financial assets and goodwill), the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's or cash-generating unit's value in use and its fair value less costs to sell, and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets, in which case, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is charged to the income statement in the period in which it arises in those expense categories consistent with the function of the impaired asset.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss of an asset other than goodwill is reversed only if there has been a change in the estimates used to determine the recoverable amount of that asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years. A reversal of such impairment loss is credited to the income statement in the period in which it arises.

Related parties

A party is considered to be related to the Group if:

(a) the party, directly or indirectly through one or more intermediaries, (i) controls, is controlled by, or is under common control with, the Group; (ii) has an interest in the Group that gives it significant influence over the Group; or (iii) has joint control over the Group;

(b) the party is an associate;

(c) the party is a jointly-controlled entity;

(d) the party is a member of the key management personnel of the Group or its parent;

(e) the party is a close member of the family of any individual referred to in (a) or (d);

(f) the party is an entity that is controlled, jointly controlled or significantly influenced by or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (d) or (e); or

(g) the party is a post-employment benefit plan for the benefit of the employees of the Group, or of any entity that is a related party of the Group.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment and depreciation

Property, plant and equipment, other than construction in progress, are stated at cost less accumulated depreciation and any impairment losses. The cost of an item of property, plant and equipment comprises its purchase price and any directly attributable costs of bringing the asset to its working condition and location for its intended use. Expenditure incurred after items of property, plant and equipment have been put into operation, such as repairs and maintenance, is normally charged to the income statement in the period in which it is incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property, plant and equipment and where the cost of the item can be measured reliably, the expenditure is capitalised as an additional cost of that asset or as a replacement.

Depreciation is calculated on the straight-line basis to write off the cost of each item of property, plant and equipment to its residual value over its estimated useful life. The principal annual rates used for this purpose are as follows:

Buildings	2 to 30 years
Leasehold improvements	Over the shorter of the lease terms and 10 years
Machinery, computer and office equipment	5 to 10 years
Motor vehicles	5 to 10 years

Where parts of an item of property, plant and equipment have different useful lives, the cost of that item is allocated on a reasonable basis among the parts and each part is depreciated separately.

Residual values, useful lives and the depreciation method are reviewed, and adjusted if appropriate, at each balance sheet date.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss on disposal or retirement recognised in the income statement in the year the asset is derecognised is the difference between the net sales proceeds and the carrying amount of the relevant asset.

Construction in progress represents buildings, plant and machinery and other fixed assets under construction or installation, which is stated at cost less any impairment losses, and is not depreciated. Cost comprises the direct costs of construction and installation during the period of construction. Construction in progress is reclassified to the appropriate category of property, plant and equipment when completed and ready for use.

Intangible assets (other than goodwill)

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each balance sheet date.

Technology know-how

Purchased technology know-how is stated at cost, less any impairment losses, and is amortised on the straight-line basis over its estimated useful life of not more than 10 years.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Intangible assets (other than goodwill) (continued)

Computer software

Purchased computer software is stated at cost less any impairment losses and is amortised on the straight-line basis over its estimated useful life of five years.

Operating concession

Operating concession represents the right to operate a telecommunications operator, and is stated at cost less accumulated amortisation and any impairment losses. Amortisation is provided on the straight-line basis over 20 years, being the period that the operating concession granted to the Group.

Research and development costs

All research costs are charged to the income statement as incurred.

Expenditure incurred on projects to develop new products is capitalised and deferred only when the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete the project and the ability to measure reliably the expenditure during the development. Product development expenditure which does not meet these criteria is expensed when incurred.

Deferred development costs are stated at cost less any impairment losses and are amortised using the straight-line basis over the commercial lives of the underlying products not exceeding five years, commencing from the date when the products are put into commercial production.

Operating leases

Leases where substantially all the rewards and risks of ownership of assets remain with the lessor are accounted for as operating leases. Where the Group is the lessor, assets leased by the Group under operating leases are included in non-current assets, and rental receivables under the operating leases are credited to the income statement on the straight-line basis over the lease terms. Where the Group is the lessee, rentals payable under the operating leases are charged to the income statement on the straight-line basis over the lease terms.

Prepaid land premiums/land lease payments under operating leases are initially stated at cost and subsequently recognised on the straight-line basis over the lease terms.

Investments and other financial assets

Financial assets in the scope of HKAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables and available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group considers whether a contract contains an embedded derivative when the Group first becomes a party to it. The embedded derivatives are separated from the host contract which is not measured at fair value through profit or loss when the analysis shows that the economic characteristics and risks of embedded derivatives are not closely related to those of the host contract.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments and other financial assets (continued)

The Group determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at the balance sheet date.

All regular way purchases and sales of financial assets are recognised on the trade date, that is, the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading. Financial assets are classified as held for trading if they are acquired for the purpose of sale in the near term. Gains or losses on investments held for trading are recognised in the income statement.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are subsequently carried at amortised cost using the effective interest method. Amortised cost is calculated taking into account any discount or premium on acquisition and includes fees that are an integral part of the effective interest rate and transaction costs. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets in unlisted equity securities that are designated as available for sale or are not classified in any of the other two categories. After initial recognition, available-for-sale financial assets are measured at fair value, with gains or losses recognised as a separate component of equity until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously reported in equity is included in the income statement.

When the fair value of unlisted equity securities cannot be reliably measured because (a) the variability in the range of reasonable fair value estimates is significant for that investment or (b) the probabilities of the various estimates within the range cannot be reasonably assessed and used in estimating fair value, such securities are stated at cost less any impairment losses.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business at the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; a discounted cash flow analysis; and option pricing models.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced either directly or through the use of an allowance account. The amount of the impairment loss is recognised in the income statement.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. Any subsequent reversal of an impairment loss is recognised in the income statement, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Group will not be able to collect all the amounts due under the original terms of an invoice. The carrying amount of the receivables is reduced through the use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

Assets carried at cost

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Impairment losses on these assets are not reversed.

Available-for-sale financial assets

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is transferred from equity to the income statement. Impairment losses on equity instruments classified as available for sale are not reversed through the income statement.

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; or
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Financial liabilities at amortised cost (including interest-bearing loans and borrowings)

Financial liabilities including trade and other payables, an amount due to the ultimate holding company and interest-bearing loans and borrowings are initially stated at fair value less directly attributable transaction costs and are subsequently measured at amortised cost, using the effective interest method unless the effect of discounting would be immaterial, in which case they are stated at cost.

Gains and losses are recognised in the income statement when the liabilities are derecognised as well as through the amortisation process.

Financial guarantee contracts

Financial guarantee contracts in the scope of HKAS 39 are accounted for as financial liabilities. A financial guarantee contract is recognised initially at its fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial guarantee contract, except when such contract is recognised at fair value through profit or loss. Subsequent to initial recognition, the Group measures the financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 *Revenue*.

Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and a recognition of a new liability, and the difference between the respective carrying amounts is recognised in the income statement.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined on the weighted average basis and, in the case of work in progress and finished goods, comprises direct materials, direct labour, an appropriate proportion of overheads and/or subcontracting fee. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal.

Construction contracts

Contract revenue comprises the agreed contract amount and appropriate amounts from variation orders, claims and incentive payments in respect of telecommunications systems contracts. Contract costs incurred comprise direct materials, the costs of subcontracting, direct labour and an appropriate proportion of variable and fixed construction overheads.

Revenue from fixed price telecommunications systems contracts is recognised using the percentage of completion method when the contract activities have progressed to a stage where economic benefit can be reasonably foreseen and is measured by reference to the proportion of costs incurred to date to the estimated total cost of the relevant contract.

Provision is made for foreseeable losses as soon as they are anticipated by management.

Where contract costs incurred to date plus recognised profits less recognised losses exceed progress billings, the surplus is treated as an amount due from customers for contract work.

Where progress billings exceed contract costs incurred to date plus recognised profits less recognised losses, the surplus is treated as an amount due to customers for contract work.

Government grants

Government grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, the fair value is credited to other payable or other long-term payable accounts and is released to the income statement over the expected useful life of the relevant asset by equal annual instalments.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the income statement.

Provisions for warranties granted by the Group on construction contracts are recognised based on cost of sales and past experience of the level of repairs and returns.

Provisions for warranties granted by the Group on handsets are recognised based on sales volume and past experience of the level of repairs and returns.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement, or in equity if it relates to items that are recognised in the same or a different period directly in equity.

Current tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred tax liability arises from goodwill or the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carryforward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carryforward of unused tax credits and unused tax losses can be utilised except:

- where the deferred tax asset relating to the deductible temporary differences arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Conversely, previously unrecognised deferred tax assets are reassessed at each balance sheet date and are recognised to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee benefits

Defined contribution pension schemes

The Company and certain of its subsidiaries established in the PRC have joined a number of defined contribution pension schemes organised by the relevant provincial and municipal social insurance management bodies of the PRC government for certain of its employees. The Company, these subsidiaries and the employees are required to make monthly contributions to these plans calculated as a percentage of the employees' salaries during the year. The contributions payable are charged as an expense to the income statement as incurred. The assets of the schemes are held separately from those of the Group in independently administered funds.

Defined benefits pension scheme

In addition, the Group provides certain employees, who joined the Group before 1 January 2002, with post-retirement monthly pension payments. The cost of providing these benefits under the Group's defined benefits pension scheme is actuarially determined and recognised over the employees' service period by using the projected unit credit method. The Group makes monthly pension payments to eligible retirees and no contribution has been made to fund future obligations since the commencement of the defined benefits scheme. Therefore, there are no assets in respect of this scheme held separately from those of the Group in independently administered funds and no actuarial valuation for the plan assets has been conducted.

Share-based payment transactions

The Company operates a share incentive scheme for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the operations of the Group. Employees (including directors) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments (''equity-settled transactions'').

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date at which they are granted. The fair value is determined by an external valuer using an appropriate pricing model, further details of which are given in note 38. In valuing equity-settled transactions, no account is taken of any performance conditions, other than conditions linked to the price of the shares of the Company (''market conditions''), if applicable.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the ''vesting date''). The cumulative expense recognised for equity-settled transactions at each balance sheet date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The charge or credit to the income statement for a period represents the movement in cumulative expense recognised as at the beginning and end of that period.

No expense is recognised for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Employee benefits (continued)

Share-based payment transactions (continued)

Where the terms of an equity-settled award are modified, as a minimum an expense is recognised as if the terms had not been modified. In addition, an expense is recognised for any modification which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

Borrowing costs

Borrowing costs are recognised as expenses in the income statement in the period in which they are incurred.

Foreign currencies

These financial statements are presented in Renminbi, which is the Company's functional and presentation currency. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Foreign currency transactions are initially recorded using the functional currency rates ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rates of exchange ruling at the balance sheet date. All differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

The functional currencies of certain overseas subsidiaries, a jointly-controlled entity and an associate are currencies other than the Renminbi. As at the balance sheet date, the assets and liabilities of these entities are translated into the presentation currency of the Company at the exchange rates ruling at the balance sheet date and, their income statements are translated into Renminbi at the weighted average exchange rates for the year. The resulting exchange differences are included in the exchange fluctuation reserve. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statement.

For the purpose of the consolidated cash flow statement, the cash flows of overseas subsidiaries are translated into Renminbi at the exchange rates ruling at the dates of the cash flows. Frequently recurring cash flows of overseas subsidiaries which arise throughout the year are translated into Renminbi at the weighted average exchange rates for the year.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short-term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired.

For the purpose of the balance sheets, cash and cash equivalents comprise cash on hand and at banks, including term deposits, which are not restricted as to use.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

2.4 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(a) from the sale of goods, when the significant risks and rewards of ownership have been transferred to the buyer, provided that the Group maintains neither managerial involvement to the degree usually associated with ownership, nor effective control over the goods sold;

(b) from the construction contracts, on the percentage of completion basis, as further explained in the accounting policy for ''Construction contracts'' above;

(c) from the rendering of services, when services are rendered;

(d) interest income, on an accrual basis using the effective interest method by applying the rate that discounts the estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset;

(e) dividend income, when the shareholders' right to receive payment has been established; and

(f) for contracts involving multiple deliverables, where the deliverables are governed by more than one authoritative accounting standard, the Group generally will evaluate each deliverable to determine whether it represents a separate unit of accounting based on the following criteria: (a) whether the delivered item has value to the customer on a standalone basis, (b) whether there is objective and reliable evidence of the fair value of the undelivered item(s), and (c) if the contract includes a general right of return relative to the delivered item, delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Group. If objective and reliable evidence of fair value exists for all units of accounting in the arrangement, revenue is allocated to each unit of accounting or element based on relative fair values. In situations where there is objective and reliable evidence of fair value for all undelivered elements, but not for delivered elements, the residual method is used to allocate the contract consideration. Under the residual method, the amount of revenue allocated to delivered elements equals the total arrangement consideration less the aggregate fair value of any undelivered elements. Each unit of accounting is then accounted for under the applicable revenue recognition guidance. So long as elements otherwise governed by separate authoritative accounting standards cannot be treated as separate units of accounting, the elements are combined into a single unit of accounting for revenue recognition purposes. In this case, revenue allocated to the unit of accounting is deferred until all combined elements have been delivered or, once there is only one remaining element to be delivered, based on the revenue recognition guidance applicable to the last delivered element within the unit of accounting.

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained profits within the equity section of the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

Judgements

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the financial statements:

Revenue recognition

The Group's material revenue streams are the result of a wide range of activities, from custom design and installation over a period of time to a single delivery of equipment to a customer. The Group's networking solutions also cover a broad range of technologies and are offered on a global basis. As a result, our revenue recognition policies can differ depending on the level of customization within the solution and the contractual terms with the customer. Newer technologies within one of the Group's reporting segments may also have different revenue recognition policies, depending on, among other factors, the specific performance and acceptance criteria within the applicable contract. Therefore, management must use significant judgement in determining how to apply the current accounting standards and interpretations, not only based on the networking solution, but also within networking solutions based on reviewing the level of customization and contractual terms with the customer. As a result, our revenues may fluctuate from period to period based on the mix of solutions sold and the geographic region in which they are sold.

When a customer arrangement involves multiple deliverables where the deliverables are governed by more than one authoritative standard, the Group evaluates all deliverables to determine whether they represent separate units of accounting based on the following criteria:

- whether the delivered item has value to the customer on a stand alone basis;
- whether there is objective and reliable evidence of the fair value of the undelivered item(s); and
- if the contract includes a general right of return relative to the delivered item, delivery or performance of the undelivered item(s) is considered probable and is substantially in the Group's control.

The Group's determination of whether deliverables within a multiple element arrangement can be treated separately for revenue recognition purposes involves significant estimates and judgement, such as whether fair value can be established on undelivered obligations and/or whether delivered elements have standalone value to the customer. Changes to our assessment of the accounting units in an arrangement and/or our ability to establish fair values could significantly change the timing of revenue recognition.

If objective and reliable evidence of fair value exists for all units of accounting in the contract, revenue is allocated to each unit of accounting or element based on relative fair values. In situations where there is objective and reliable evidence of fair value for all undelivered elements, but not for delivered elements, the residual method is used to allocate the contract consideration. Under the residual method, the amount of revenue allocated to delivered elements equals the total arrangement consideration less the aggregate fair value of any undelivered elements. Each unit of accounting is then accounted for under the applicable revenue recognition guidance. If sufficient evidence of fair value cannot be established for an undelivered element, revenue related to delivered elements is deferred until the earlier of when sufficient fair value is established and when all remaining elements have been delivered. Once there is only one remaining element to be delivered within the unit of accounting, the deferred revenue is recognised based on the revenue recognition guidance applicable to the last delivered element. For instance, where post-contract support is the last delivered element within the unit of accounting, the deferred revenue is recognised ratably over the remaining post-contract support term once post-contract support is the only undelivered element.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Judgements (continued)

Revenue recognition (continued)

The Group's assessment of which revenue recognition guidance is appropriate for accounting for a deliverable also can involve significant judgement. For instance, the determination of whether software is more than incidental to hardware can impact on whether the hardware is accounted for under software revenue recognition guidance or based on general revenue recognition guidance. This assessment could significantly impact the amount and timing of revenue recognition.

For elements related to customised network solutions and certain network build-outs, revenues are recognised under the HKAS 11 *Construction Contract*, generally using the percentage-of-completion method. In using the percentage-of-completion method, revenues are generally recorded based on a measure of the percentage of costs incurred to date on a contract relative to the estimated total expected contract costs. Profit estimates on long-term contracts are revised periodically based on changes in circumstances and any losses on contracts are recognised in the period that such losses become known. Generally, the terms of long-term contracts provide for progress billing based on completion of certain phases of work. Contract revenues recognised, based on costs incurred towards the completion of the project, that are unbilled are accumulated in the contracts in progress account included in accounts receivable, net. Billings in excess of revenues recognised to date on long-term contracts are recorded as advance billings in excess of revenues recognised to date on contracts within other accrued liabilities. Significant judgement is often required when estimating total contract costs and progress to completion on these arrangements, as well as whether a loss is expected to be incurred on the contract. Management uses historical experience, project plans and an assessment of the risks and uncertainties inherent in the arrangement to establish these estimates. Uncertainties include implementation delays or performance issues that may or may not be within the control of the Group. Changes in these estimates could result in a material impact on revenues and net earnings.

Revenue for hardware that does not require significant customisation, and where any software is considered incidental, is recognised under HKAS 18 *Revenue*, revenue is recognised provided that persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the fee is fixed or determinable and collectibility is reasonably assured.

For hardware, delivery is considered to have occurred upon shipment provided that the risk of loss, and title in certain jurisdictions, have been transferred to the customer. For arrangements where the criteria for revenue recognition have not been met because legal title or the risk of loss on products was not transfer to the buyer until final payment had been received or where delivery had not occurred, revenue is deferred to a later period when title or the risk of loss passes either on delivery or on receipt of payment from the customer.

For further information on the Group's revenue recognition policies relating to our material revenue streams, please refer to note 2.4 to these consolidated financial statements.

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Estimation uncertainty

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

Impairment of intangible assets and property, plant and equipment

The Group determines whether intangible assets and property, plant and equipment are impaired when there is an indication of impairment. This requires an estimation of the value in use of the cash-generating units to which the intangible assets and property, plant and equipment were allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of intangible assets at 31 December 2006 was RMB274,905,000 (2005: RMB335,835,000). The carrying amount of property, plant and equipment was approximately RMB3,053,019,000 (2005: RMB2,470,965,000). More details are set out in notes 15 and 17.

Management carries out impairment review on intangible assets and property, plant and equipment by comparing the lower of their carrying amount and recoverable amount of them respectively.

An impairment loss is recognised when the carrying amount of intangible assets and property, plant and equipment exceeds the recoverable amount. An impairment loss is charged to the income statement in the period in which it arises. Management assesses the recoverable amount by the higher of the fair value less costs to sell and the expected value in use which is determined by the expected useful life and the expected discounted net cash flows of intangible assets and property, plant and equipment.

Impairment of trade receivables

In determining whether there is objective evidence of an impairment loss, the Group takes into consideration the estimation of future cash flows. The amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e., the effective interest rate computed at initial recognition). Where the actual future cash flows are less than expected, a material impairment loss may arise.

Equity settled share expense

The estimated cost of the share incentive scheme is recognised in income statements based on estimation of various assumptions.

One of the major factors that could impact the cost is the turnover rate of respective participants under the scheme. In situation that the actual turnover rate is less than the management estimation, such cost would be higher.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

3. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

Estimation uncertainty (continued)

Warranty claims

The Group generally offers warranties for its products for 12 months. Management estimates the related provision for future warranty claims based on historical warranty claim information, as well as recent trends that might suggest that past cost information may differ from future claims.

Factors that could impact the estimated claim information include the success of the Group's productivity and quality initiatives, as well as parts and labour costs.

Were claims costs to differ by 10% from management's estimates, the warranty provisions would be an estimated amount of approximately RMB25 million higher or lower in the year of 2006.

Depreciation and amortisation

The Group's net book value of property, plant and equipment as at 31 December 2006 was approximately RMB3,053,019,000 (2005: RMB2,470,965,000). The Group depreciates items of property, plant and equipment on the straight-line basis over their estimated useful lives, and after taking into account their estimated residual value, commencing from the date the items of property, plant and equipment are placed into productive use. The estimated useful lives and dates that the Group places the items of property, plant and equipment into productive use reflect the directors' estimate of the periods that the Group intends to derive future economic benefits from the use of the Group's property, plant and equipment.

Deferred tax assets

As at 31 December 2006, deferred tax assets of approximately RMB210,923,000 have been recognised in the Group's balance sheet. The realisability of the deferred tax assets mainly depend on whether sufficient future profits or taxable temporary differences will be realised in the future. Since the Group is expecting a growth in profits to be generated in the future based on management estimation, the directors of the Company consider that the deferred tax assets could be fully utilized in the future, and would be recognised in the income statement for the period in which such a reversal takes place.

4. SEGMENT INFORMATION

Segment information is presented by way of two segments: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

The Group's operating business are structured and managed separately, according to the nature of their operations and the products and services they provide. Each of the Group's business segments represents a strategic business unit that offers products and services which are subject to risks and returns that are different from those of the other business segments. Summary details of the business segments are as follows:

(a) The wireless communications segment engages in the provision of systems integration and the sale of equipment for mobile phone network systems, primarily in respect of CDMA, GSM and wireless local access (PHS) systems.

(b) The wireline switch and access segment engages in the manufacture and sale of wireline, circuit-switches and narrow-band access systems for fixed line phone systems.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

4. SEGMENT INFORMATION (continued)

(c) The optical and data communications segment engages in the provision of DSL systems, SDH, WDM systems and softswitch systems, broadband routing switches, wireless access data products and other data communications products.

(d) The handsets segment engages in the manufacture and sale of CDMA and GSM mobile phone handsets and wireless local access (PHS) handsets.

(e) The telecommunications software systems and services and other products segment represented the provision of telecommunications software systems such as operation support systems and the provision of fee-based services.

In determining the Group's geographical segments, revenues are attributed to the segments based on the location of the customers, and assets are attributed to the segments based on the location of the assets.

(a) Business segments

The following tables present revenue, profit and certain asset, liability and expenditure information for the Group's business segments for the years ended 31 December 2006 and 2005.

Group

	Wireless communications		Wireline switch and access		Optical and data communications		Handsets		Telecommunications software systems, services and other products		Consolidated	
	2006 RMB'000	2005 RMB'000	**2006 RMB'000**	2005 RMB'000	**2006 RMB'000**	2005 RMB'000	**2006 RMB'000**	2005 RMB'000	**2006 RMB'000**	2005 RMB'000	**2006 RMB'000**	2005 RMB'000
Segment revenue:												
Telecommunications system contracts	**9,186,920**	8,930,836	**2,279,424**	2,752,570	**3,874,634**	3,352,980	**—**	—	**1,912,160**	1,943,428	**17,253,138**	16,979,814
Sale of goods and services	**—**	—	**—**	—	**—**	—	**4,519,492**	4,333,082	**1,259,054**	263,024	**5,778,546**	4,596,106
Total	**9,186,920**	8,930,836	**2,279,424**	2,752,570	**3,874,634**	3,352,980	**4,519,492**	4,333,082	**3,171,214**	2,206,452	**23,031,684**	21,575,920
Segment results	**2,604,063**	2,590,240	**593,821**	1,085,112	**364,028**	160,110	**512,429**	118,165	**432,191**	334,131	**4,506,532**	4,287,758
Interest and unallocated gains											**792,124**	681,646
Unallocated expenses											**(4,121,795)**	(3,183,548)
Finance costs											**(153,694)**	(175,884)
Share of profits and losses of:												
Jointly-controlled entities											**(652)**	(1,198)
Associates											**8,175**	(2,969)
Profit before tax											**1,030,690**	1,605,805
Tax											**(127,078)**	(179,851)
Profit for the year											**903,612**	1,425,954

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

4. SEGMENT INFORMATION (continued)

(a) Business segments (continued)

Group

	Wireless communications		Wireline switch and access		Optical and data communications		Handsets		Telecommunications software systems, services and other products		Consolidated	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005
Assets and liabilities	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Segment assets	**7,928,525**	5,292,995	**1,979,726**	2,196,473	**3,352,383**	2,778,123	**2,368,637**	2,162,194	**1,124,605**	810,136	**16,753,876**	13,239,921
Investments in jointly-controlled entities											**5,936**	6,588
Investments in associates											**51,257**	35,583
Unallocated assets											**9,976,177**	9,181,950
Total assets											**26,787,246**	22,464,042
Segment liabilities	**491,760**	860,005	**56,382**	91,578	**560,098**	204,755	**254,266**	344,933	**269,644**	93,207	**1,632,150**	1,594,478
Unallocated liabilities											**13,829,259**	10,148,323
Total liabilities											**15,461,409**	11,742,801
Other segment information:												
Depreciation and amortisation	**218,625**	123,367	**61,374**	37,519	**140,369**	82,886	**137,870**	105,251	**53,653**	45,421	**611,891**	478,496
Capital expenditure	**422,669**	371,525	**118,655**	112,990	**271,375**	249,611	**266,542**	316,966	**103,729**	136,787	**1,182,970**	1,187,879

(b) Geographical segments

The following table presents revenue information for the Group's geographical segments. Over 90% of the Group's assets are located in the PRC. Accordingly, no analysis of the assets and capital expenditure by geographical segment is presented.

Group

	The PRC		Asia (excluding the PRC)		Africa		Others		Consolidated	
	2006	2005	**2006**	2005	**2006**	2005	**2006**	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Segment revenue:										
Telecommunications system contracts	**9,879,161**	10,838,079	**3,918,344**	3,428,396	**2,392,356**	2,576,744	**1,063,277**	136,595	**17,253,138**	16,979,814
Sale of goods and services	**2,922,604**	3,036,230	**1,835,323**	1,140,259	**170,874**	258,667	**849,745**	160,950	**5,778,546**	4,596,106
	12,801,765	13,874,309	**5,753,667**	4,568,655	**2,563,230**	2,835,411	**1,913,022**	297,545	**23,031,684**	21,575,920

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

5. REVENUE, OTHER INCOME AND GAINS

Revenue, which is also the Group's turnover, represents the aggregate of an appropriate proportion of contract revenue from telecommunications systems contracts and the invoiced value of goods and services sold net of value-added tax ("VAT") and after allowances for goods returns and trade discounts. All significant intra-group transactions have been eliminated on consolidation.

An analysis of the Group's revenue and other income and gains is as follows:

	Note	2006 RMB'000	2005 RMB'000
Revenue			
Telecommunications systems contracts		**17,253,138**	16,979,814
Sale of goods and services		**5,778,546**	4,596,106
		23,031,684	21,575,920
Other income			
Government grants		**22,544**	139,491
Contingent rent receivable in respect of an operating lease		**27,813**	—
Service fees		**39,633**	15,379
VAT subsidies, exemptions and refunds#		**612,163**	456,015
Bank and other interest income		**49,050**	54,870
		751,203	665,755
Gains			
Excess over the cost of business combinations		**—**	12,236
Fair value gain on an equity investment at fair value through profit or loss		**16,595**	—
Gain on disposal of an equity investment at fair value through profit or loss		**24,326**	—
Gain on deemed disposal of interests in a subsidiary	40	**—**	3,655
		40,921	15,891
		792,124	681,646

During the years ended 31 December 2005 and 2006, the Company received VAT subsidies on the amount of VAT paid for high-technology products as approved by the Shenzhen Economic and Trade Bureau (深圳市經濟貿易局), Shenzhen Science and Technology Bureau (深圳市科技局), Shenzhen Finance Bureau (深圳市財政局), Shenzhen State Tax Bureau (深圳市國家稅務局), Shenzhen Local Tax Bureau (深圳市地方稅務局) and Nanjing State Tax Bureau (南京市國家稅務局). In addition, for the years ended 31 December 2005 and 2006, Shenzhen Zhongxing Software Company, Limited ("Zhongxing Software") and Nanjing Zhonging Software Company, Limited, being a designated software enterprises, were entitled to VAT refunds on the effective VAT rate in excess of 3% after the payment of statutory net output VAT of 17%. Such VAT refunds were approved the Shenzhen State Tax Bureau (深圳市國家稅務局) and Nanjing State Tax Bureau (南京市國家稅務局) and had been received by Zhongxing Software and Nanjing Zhonging Software Company, Limited.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

6. PROFIT BEFORE TAX

The Group's profit before tax is arrived at after charging:

	Notes	**2006 RMB'000**	2005 RMB'000
Cost of inventories sold		**14,295,410**	13,373,519
Depreciation	15	**510,333**	394,444
Less: Amount capitalised as deferred development costs		**—**	(7,585)
		510,333	386,859
Amortisation of intangible assets other than deferred development costs	17	**49,201**	50,355
Amortisation of deferred development costs**	17	**52,357**	32,380
		101,558	82,735
Impairment of goodwill*		**—**	56,267
Impairment of trade receivables*		**111,611**	15,642
Provision for warranties**	35	**114,724**	225,790
Write-down of inventories to net realisable value**		**52,781**	96,185
Minimum lease payments under operating leases on land and buildings		**206,054**	188,905
Auditors' remuneration		**6,080**	4,870
Staff costs (including directors' and supervisors' remuneration — note 8):			
Wages, salaries, bonuses, allowances and welfares		**3,103,539**	2,601,779
Equity settled share expense		**2,480**	—
Pension scheme contributions:			
Defined benefits pension scheme — note 33		**2,787**	2,224
Defined contribution pension scheme		**208,596**	187,081
		3,317,402	2,791,084
Foreign exchange differences, net*		**29,422**	48,390
Loss on disposal of items of property, plant and equipment*		**13,933**	6,163
Loss on disposal of intangible assets*	17	**952**	70
Recognition of financial guarantee contract*		**3,689**	—
Loss on disposal of interests in subsidiaries*		**—**	2,057

* The impairment of goodwill, impairment of trade receivables, foreign exchange differences, recognition of financial guarantee contract, loss on disposal of items of property, plant and equipment, loss on disposal of intangible assets and loss on disposal of interests in subsidiaries are included in "Other expenses" on the face of the consolidated income statement.

** The provision for warranties, amortisation of deferred development costs and write-down of inventories to net realisable value are included in "Cost of sales" on the face of the consolidated income statement.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

7. FINANCE COSTS

	Group	
	2006 **RMB'000**	2005 RMB'000
Interest on bank loans wholly repayable within five years	**58,817**	36,042
Finance costs on trade receivables factored and bills discounted	**94,877**	139,842
	153,694	175,884

8. DIRECTORS' AND SUPERVISORS' REMUNERATION

Directors' and supervisors' remuneration for the year, disclosed pursuant to the Listing Rules and Section 161 of the Hong Kong Companies Ordinance, are as follows:

	Group	
	2006 **RMB'000**	2005 RMB'000
Fees	**—**	—
Other emoluments of executive directors and supervisors:		
Salaries, bonuses, allowances and welfare	**2,795**	3,037
Performance related bonuses	**3,171**	2,524
Share incentive scheme	**15**	—
Retirement benefits scheme contribution	**51**	32
	6,032	5,593

During the year, certain directors were granted shares under a share incentive scheme in respect of their services to the Group, further details of which are set out in note 38 to the financial statements. The fair value of such shares which has been recognised in the income statement, was determined as at the date of grant and the amount included in the financial statements for the year is included in the above directors' remuneration disclosures.

(a) Independent non-executive directors

The salaries, bonuses, allowances and welfare paid to independent non-executive directors during the year were as follows:

	2006 **RMB'000**	2005 RMB'000
Zhu Wuxiang	**60**	60
Chen Shaohua	**60**	60
Tan Zhenhui	**—**	25
Mi Zhengkun	**60**	60
Li Jin	**60**	60
Qiao Wenjun	**60**	60
	300	325

There were no other emoluments payable to the independent non-executive directors during the year (2005: Nil).

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(b) Executive directors, non-executive directors and supervisors

	Fees RMB'000	Salaries, bonuses, allowances and welfare RMB'000	Performance related bonuses RMB'000	Share incentive scheme RMB'000	Retirement benefits scheme contributions RMB'000	Total remuneration RMB'000
2006						
Executive directors:						
Yin Yimin	—	422	1,141	—	9	1,572
Shi Lirong	—	354	420	—	9	783
He Shiyou	—	359	450	—	17	826
	—	1,135	2,011	—	35	3,181
Non-executive directors:						
Hou Weigui	—	332	405	—	—	737
Wang Zongyin	—	60	—	3	—	63
Xie Weiliang	—	60	—	3	—	63
Zhang Junchao	—	60	—	3	—	63
Li Juping	—	60	—	3	—	63
Dong Lianbo	—	60	—	3	—	63
	—	1,767	2,416	15	35	4,233
Supervisors:						
Zhang Taifeng	—	329	405	—	—	734
Wang Wangxi	—	249	248	—	9	506
He Xuemei	—	150	102	—	7	259
Qu Deqian	—	—	—	—	—	—
Wang Yan	—	—	—	—	—	—
	—	728	755	—	16	1,499

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

8. DIRECTORS' AND SUPERVISORS' REMUNERATION (continued)

(b) Executive directors, non-executive directors and supervisors (continued)

	Fees RMB'000	Salaries, bonuses, allowances and welfare RMB'000	Performance related bonuses RMB'000	Retirement benefits scheme contributions RMB'000	Total remuneration RMB'000
2005					
Executive directors:					
Yin Yimin	—	423	700	8	1,131
Shi Lirong	—	353	420	8	781
He Shiyou	—	387	250	2	639
	—	1,163	1,370	18	2,551
Non-executive directors:					
Hou Weigui	—	332	363	—	695
Wang Zongyin	—	60	—	—	60
Xie Weiliang	—	60	—	—	60
Zhang Junchao	—	60	—	—	60
Li Juping	—	60	—	—	60
Dong Lianbo	—	60	—	—	60
Tang Shanyi	—	25	—	—	25
	—	1,820	1,733	18	3,571
Supervisors:					
Zhang Taifeng	—	332	363	—	695
Wang Wangxi	—	321	294	8	623
He Xuemei	—	159	134	6	299
Qu Deqian	—	—	—	—	—
Wang Yan	—	—	—	—	—
Li Jinhu	—	20	—	—	20
Cao Quansheng	—	20	—	—	20
Li Huanru	—	20	—	—	20
Cui Hongwei	—	20	—	—	20
	—	892	791	14	1,697

There was no arrangement under which directors and supervisors waived or agreed to waive any remuneration during the year.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

9. FIVE HIGHEST PAID EMPLOYEES

The five highest paid employees during the year included no (2005: one) director, details of whose remuneration are set out in note 8 above. Details of the remuneration of the five (2005: four) non-director and non-supervisor, highest paid employees for the year are as follows:

	2006 RMB'000	2005 RMB'000
Salaries, bonuses, allowances and welfare	**6,394**	4,145
Performance related bonuses	**1,041**	863
Retirement benefits scheme contributions	**1,030**	18
	8,465	5,026

The number of non-director and non-supervisor, highest paid employees whose remuneration fell within the following bands is as follows:

	Number of employees	
	2006	2005
Nil to RMB1,000,000	**—**	—
RMB1,000,001 to RMB1,500,000	**—**	4
RMB1,500,001 to RMB2,000,000	**5**	—
	5	4

During the year, no director or supervisor waived or agreed to waive any emolument, and no emoluments were paid by the Group to the directors, supervisors or any of the five highest paid employees as an inducement to join or upon joining the Group or as compensation for loss of office.

10. TAX

	2006 RMB'000	2005 RMB'000
Group:		
Current — Hong Kong	**6,951**	5,726
Current — Mainland China	**106,449**	34,700
Current — Overseas	**165,014**	94,331
Deferred tax charged/(credit) (note 36)	**(151,336)**	45,094
Total tax charge for the year	**127,078**	179,851

Hong Kong profits tax has been provided at the rate of 17.5% (2005: 17.5%) on the estimated assessable profits arising in Hong Kong during the year. Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the countries in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

10. TAX (continued)

Under the relevant PRC income tax law, except for certain preferential treatments available to the Company and its subsidiaries, the Group's entities established in the PRC are subject to corporate income tax at a rate of 33% on their taxable income.

The Company and its subsidiaries that are registered and operating in the Shenzhen Special Economic Zone of the PRC are entitled to a preferential income tax rate of 15%.

As a designated software enterprise, Zhongxing Software, a major subsidiary of the Company has been approved as a new software enterprise and entitled to full exemption from corporate income tax for two years and a 50% relief in corporate income tax in the three years thereafter starting from the first profitable year from 1 January 2003 until 31 December 2007. The corporate income tax rate applicable to Zhongxing Software was 7.5% during the current year.

ZTE Mobile Tech Co., Ltd (''ZTE Mobile'') is entitled to full exemption from corporate income tax for two years and a 50% relief in corporate income tax in the three years thereafter starting from the first profitable year from 1 January 2003 until 31 December 2007. ZTE Mobile is entitled to a corporate income tax rate of 7.5%.

A reconciliation of the tax expense applicable to profit before tax using the statutory rate for the countries in which the Company and its subsidiaries are domiciled to the tax expense at the effective tax rate, and a reconciliation of the applicable rate (i.e., the statutory tax rate) to the effective tax rate, are as follows:

	2006		2005	
	RMB'000	%	RMB'000	%
Profit before tax	**1,030,690**		1,605,805	
Tax at statutory tax rate	**340,128**	33.0	529,916	33.0
Lower tax rate for specific provinces or local authority	**(185,539)**	(18.0)	(289,045)	(18.0)
Expenses not deductible for tax	**97,993**	9.5	103,669	6.5
Income not subject to tax	**(36,595)**	(3.6)	(51,602)	(3.2)
Tax holiday	**(96,883)**	(9.4)	(89,482)	(5.5)
Profits and losses attributable to jointly-controlled entities and associates	**(1,129)**	(0.1)	625	—
Tax losses utilised from previous years	**(11,146)**	(1.1)	(5,702)	(0.4)
Other tax allowances	**(72,480)**	(7.0)	(41,558)	(2.6)
Tax losses of subsidiaries	**92,729**	9.0	23,030	1.4
Tax charge at the Group's effective rate	**127,078**	12.3	179,851	11.2

No share of tax attributable to jointly-controlled entities is included in ''Share of profits and losses of jointly-controlled entities'' on the face of the consolidated income statement (2005: Nil).

No share of tax attributable to associates is included in ''Share of profits and losses of associates'' on the face of the consolidated income statement (2005: Nil).

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

11. PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT

The consolidated profit attributable to equity holders of the parent for the year ended 31 December 2006 includes a profit of approximately RMB831,130,000 (2005: RMB1,084,317,000) which has been dealt with in the financial statements of the Company (note 39(b)).

12. DIVIDEND

	2006	2005
	RMB'000	RMB'000
Proposed final — RMB0.15 (2005: RMB0.25) per ordinary share	**143,928**	239,880

The proposed final dividend for the year is subject to the approval of the Company's shareholders at the forthcoming annual general meeting.

13. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The calculation of basic earnings per share is based on the profit for the year attributable to ordinary equity holders of the parent of RMB766,972,000 (2005: RMB1,287,701,000) and the weighted average number of 959,521,650 (2005: 959,521,650) ordinary shares in issue during the year.

The calculation of diluted earnings per share amounts is based on the profit for the year attributable to ordinary equity holders of the parent of RMB766,972,000 (2005: RMB1,287,701,000) and the weighted average number of 959,521,650 (2005: 959,521,650) shares in issue during the year, as used in the basic earnings per share calculation, and the weighted average number of 525,808 shares assumed to have been issued at no consideration on the deemed exercise of all dilutive potential shares into shares.

Diluted earnings per share amounts for the years ended 31 December 2005 have not been presented as the Company did not have any potentially dilutive ordinary shares during that year.

14. DISTRIBUTION OF PROFIT

In accordance with the Company Law of the PRC and the articles of associations, the Company and certain of its subsidiaries are required to allocate 10% of their profit after tax, as determined in accordance with PRC accounting standards and regulations applicable to these companies, to the statutory surplus reserve (the "SSR") until such reserves reach 50% of the registered capitals of these companies. Part of the SSR may be capitalised as these companies' share capitals, provided that the remaining balances after the capitalisation are not less than 25% of the registered capitals of these companies.

In previous years, the Company and certain of its subsidiaries are required to transfer 5% to 10% of their profit after tax, as determined in accordance with PRC accounting standards and regulations applicable to these companies, to statutory public welfare fund (the "PWF"). According to the "Company Law of the People's Republic of China (2005 revised)" that took effect as of 1 January 2006, and the modified articles of associations, the Company and its subsidiaries will not allocate the PWF starting from 2006. The balance of PWF as at 31 December 2005 was transferred to the SSR.

Certain of the Company's subsidiaries are Chinese-foreign equity joint ventures. In accordance with the "Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures" and their respective articles of associations, these subsidiaries are required to allocate certain of their profit after tax as determined in accordance with PRC accounting standards and related regulations to enterprise expansion fund, reserve fund and employee bonus and welfare fund. The allocation rates are determined by their respective board of directors.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

15. PROPERTY, PLANT AND EQUIPMENT

Group

	Buildings RMB'000	Leasehold improvements RMB'000	Machinery, computer and office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2006						
At 31 December 2005 and at 1 January 2006:						
Cost	865,216	51,631	2,414,643	210,369	140,737	3,682,596
Accumulated depreciation and impairment	(115,695)	(28,046)	(1,003,661)	(64,229)	—	(1,211,631)
Net carrying amount	749,521	23,585	1,410,982	146,140	140,737	2,470,965
At 1 January 2006, net of accumulated depreciation and impairment	749,521	23,585	1,410,982	146,140	140,737	2,470,965
Additions	584	10,482	694,826	40,399	389,451	1,135,742
Disposals	—	—	(29,911)	(4,873)	—	(34,784)
Depreciation provided during the year	(32,891)	(19,327)	(434,526)	(23,589)	—	(510,333)
Transfers	17,587	9,591	33,374	—	(60,552)	—
Exchange realignments	(434)	—	(7,893)	(244)	—	(8,571)
At 31 December 2006, net of accumulated depreciation and impairment	734,367	24,331	1,666,852	157,833	469,636	3,053,019
At 31 December 2006:						
Cost	882,918	71,704	3,016,304	238,044	469,636	4,678,606
Accumulated depreciation and impairment	(148,551)	(47,373)	(1,349,452)	(80,211)	—	(1,625,587)
Net carrying amount	734,367	24,331	1,666,852	157,833	469,636	3,053,019

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Group

	Buildings RMB'000	Leasehold improvements RMB'000	Machinery, computer and office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2005						
At 31 December 2004 and at 1 January 2005:						
Cost	650,152	60,020	1,845,110	158,541	115,574	2,829,397
Accumulated depreciation and impairment	(86,298)	(37,513)	(712,621)	(57,834)	—	(894,266)
Net carrying amount	563,854	22,507	1,132,489	100,707	115,574	1,935,131
At 1 January 2005, net of accumulated depreciation and impairment	563,854	22,507	1,132,489	100,707	115,574	1,935,131
Additions	4,642	12,948	614,462	66,183	271,950	970,185
Disposals	(9,279)	—	(17,672)	(5,170)	(15,434)	(47,555)
Acquisition of subsidiaries	—	—	12,345	475	—	12,820
Disposal of subsidiaries (note 40)	—	—	(5,589)	(539)	—	(6,128)
Depreciation provided during the year	(29,399)	(11,870)	(337,518)	(15,657)	—	(394,444)
Transfers	219,759	—	11,594	—	(231,353)	—
Exchange realignments	(56)	—	871	141	—	956
At 31 December 2005, net of accumulated depreciation and impairment	749,521	23,585	1,410,982	146,140	140,737	2,470,965
At 31 December 2005:						
Cost	865,216	51,631	2,414,643	210,369	140,737	3,682,596
Accumulated depreciation and impairment	(115,695)	(28,046)	(1,003,661)	(64,229)	—	(1,211,631)
Net carrying amount	749,521	23,585	1,410,982	146,140	140,737	2,470,965

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Company

	Buildings RMB'000	Leasehold improvements RMB'000	Machinery, computer and office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2006						
At 31 December 2005 and at 1 January 2006:						
Cost	833,910	34,724	1,385,321	154,964	77,261	2,486,180
Accumulated depreciation and impairment	(102,885)	(23,112)	(596,068)	(45,568)	—	(767,633)
Net carrying amount	731,025	11,612	789,253	109,396	77,261	1,718,547
At 1 January 2006, net of accumulated depreciation and impairment	731,025	11,612	789,253	109,396	77,261	1,718,547
Additions	—	—	407,546	32,558	368,134	808,238
Disposals	—	—	(11,000)	(3,785)	—	(14,785)
Transfers from subsidiaries	—	—	22,141	1,090	—	23,231
Transfers to subsidiaries	—	—	(295,655)	(6,938)	—	(302,593)
Depreciation provided during the year	(31,836)	(5,473)	(213,725)	(16,092)	—	(267,126)
Transfers	—	9,591	33,374	—	(42,965)	—
Exchange realignments	(50)	—	(28)	73	—	(5)
At 31 December 2006, net of accumulated depreciation and impairment	699,139	15,730	731,906	116,302	402,430	1,965,507
At 31 December 2006:						
Cost	833,861	44,315	1,378,237	172,135	402,430	2,830,978
Accumulated depreciation and impairment	(134,722)	(28,585)	(646,331)	(55,833)	—	(865,471)
Net carrying amount	699,139	15,730	731,906	116,302	402,430	1,965,507

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Company

	Buildings RMB'000	Leasehold improvements RMB'000	Machinery, computer and office equipment RMB'000	Motor vehicles RMB'000	Construction in progress RMB'000	Total RMB'000
31 December 2005						
At 31 December 2004 and at 1 January 2005:						
Cost	624,882	47,519	1,063,557	118,952	98,101	1,953,011
Accumulated depreciation and impairment	(73,842)	(34,143)	(410,418)	(41,604)	—	(560,007)
Net carrying amount	551,040	13,376	653,139	77,348	98,101	1,393,004
At 1 January 2005, net of accumulated depreciation and impairment	551,040	13,376	653,139	77,348	98,101	1,393,004
Additions	—	8,543	474,924	52,349	208,919	744,735
Disposals	(10,731)	—	(6,515)	(4,217)	(10,000)	(31,463)
Transfers from subsidiaries	—	—	20,931	618	—	21,549
Transfers to subsidiaries	—	—	(161,085)	(3,941)	—	(165,026)
Depreciation provided during the year	(29,043)	(10,307)	(191,498)	(13,346)	—	(244,194)
Transfers	219,759	—	—	—	(219,759)	—
Reclassifications	—	—	(544)	544	—	—
Exchange realignments	—	—	(99)	41	—	(58)
At 31 December 2005, net of accumulated depreciation and impairment	731,025	11,612	789,253	109,396	77,261	1,718,547
At 31 December 2005:						
Cost	833,910	34,724	1,385,321	154,964	77,261	2,486,180
Accumulated depreciationand impairment	(102,885)	(23,112)	(596,068)	(45,568)	—	(767,633)
Net carrying amount	731,025	11,612	789,253	109,396	77,261	1,718,547

As at 31 December 2006, the Group was in the process of obtaining the real estate title certificate for a building located in Shenzhen, the PRC, with a net book value of approximately RMB238,060,000 (2005: RMB220,000,000), included in the Group's buildings.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

15. PROPERTY, PLANT AND EQUIPMENT (continued)

Company (continued)

Approximately RMB40,416,000 (2005: RMB14,000,000) of the Group's machinery, computer and office equipment represented telecommunications equipment that has been leased to a third party for the operation of a wireless network. According to the respective contract, the lease payment will be made to the Group's subsidiary by way of sharing a certain portion of the profit generated from such telecommunications network for a period of five years where the ownership of these telecommunications equipment will be retained by the subsidiary during the five-year period. During the five-year period, the Group will be solely responsible for the safeguard and the maintenance of the network. Considering that the risk in relation to the assets has not been substantially transferred to the third party, the directors are of the view that such arrangement should be accounted for as operating lease. The equipment was accounted for as construction in progress as at 31 December 2005.

At 31 December 2006, the real estate title certificate for certain of the Group's buildings with net book values of approximately RMB117.2 million (2005: Nil) were held by the court as security in relation to a litigation proceeding (note 42(b)).

16. PREPAID LAND PREMIUMS/LAND LEASE PAYMENTS

Group

	2006 **RMB'000**	2005 RMB'000
Carrying amount at 1 January	**56,480**	54,456
Additions during the year	**1,533**	3,341
Recognised during the year	**(1,418)**	(1,317)
Carrying amount at 31 December	**56,595**	56,480
Current portion	**(1,449)**	(1,418)
Non-current portion	**55,146**	55,062

Various pieces of leasehold land are held under medium term leases and are situated in Mainland China.

Company

	2006 **RMB'000**	2005 RMB'000
Carrying amount at 1 January	**50,706**	50,714
Additions during the year	**—**	1,241
Recognised during the year	**(1,300)**	(1,249)
Carrying amount at 31 December	**49,406**	50,706
Current portion	**(1,300)**	(1,300)
Non-current portion	**48,106**	49,406

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

16. PREPAID LAND PREMIUMS/LAND LEASE PAYMENTS (continued)

Various pieces of leasehold land are held under medium term leases and are situated in Mainland China.

As at 31 December 2006, the Group was in the process of obtaining the land use right certificates of certain pieces of land located in Shenzhen, Wuxi, and Anhui, the PRC, with net book values of approximately RMB2,500,000, RMB3,400,000 and RMB2,600,000, respectively.

17. INTANGIBLE ASSETS

Group

	Technology know-how RMB'000	Computer software RMB'000	Operating concession RMB'000	Deferred development costs RMB'000	Total RMB'000
31 December 2006:					
Cost at 1 January 2006, net of accumulated amortisation and impairment	**1,356**	**96,108**	**56,264**	**182,107**	**335,835**
Additions	**—**	**42,715**	**1,172**	**—**	**43,887**
Retirements and disposals	**—**	**(480)**	**(472)**	**—**	**(952)**
Exchange realignments			**(2,307)**	**—**	**(2,307)**
Amortisation provided during the year	**(318)**	**(45,700)**	**(3,183)**	**(52,357)**	**(101,558)**
At 31 December 2006	**1,038**	**92,643**	**51,474**	**129,750**	**274,905**
At 31 December 2006:					
Cost	**1,356**	**268,722**	**68,007**	**239,619**	**577,704**
Accumulated amortisation and impairment	**(318)**	**(176,079)**	**(16,533)**	**(109,869)**	**(302,799)**
Net carrying amount	**1,038**	**92,643**	**51,474**	**129,750**	**274,905**
31 December 2005:					
Cost at 1 January 2005, net of accumulated amortisation and impairment	683	108,902	31,877	66,487	207,949
Additions	1,067	35,512	29,774	148,000	214,353
Retirements and disposals	—	(70)	—	—	(70)
Acquisition of subsidiaries	47	—	—	—	47
Disposals of subsidiaries (note 40)	—	(3,709)	—	—	(3,709)
Amortisation provided during the year	(441)	(44,527)	(5,387)	(32,380)	(82,735)
At 31 December 2005	1,356	96,108	56,264	182,107	335,835
At 31 December 2005:					
Cost	2,397	237,012	69,614	288,039	597,062
Accumulated amortisation and impairment	(1,041)	(140,904)	(13,350)	(105,932)	(261,227)
Net carrying amount	1,356	96,108	56,264	182,107	335,835

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

17. INTANGIBLE ASSETS (continued)

Company

	Computer software RMB'000	Deferred development costs RMB'000	Total RMB'000
31 December 2006:			
Cost at 1 January 2006, net of accumulated amortisation and impairment	**86,320**	**182,107**	**268,427**
Additions	**33,843**	**—**	**33,843**
Retirements and disposals	**(334)**	**—**	**(334)**
Amortisation provided during the year	**(41,887)**	**(52,357)**	**(94,244)**
At 31 December 2006	**77,942**	**129,750**	**207,692**
At 31 December 2006:			
Cost	**250,127**	**239,620**	**489,747**
Accumulated amortisation and impairment	**(172,185)**	**(109,870)**	**(282,055)**
Net carrying amount	**77,942**	**129,750**	**207,692**
31 December 2005:			
Cost at 1 January 2005, net of accumulated amortisation and impairment	93,348	66,487	159,835
Additions	33,342	148,000	181,342
Retirements and disposals	(190)	—	(190)
Amortisation provided during the year	(40,180)	(32,380)	(72,560)
At 31 December 2005	86,320	182,107	268,427
At 31 December 2005:			
Cost	219,783	288,038	507,821
Accumulated amortisation and impairment	(133,463)	(105,931)	(239,394)
Net carrying amount	86,320	182,107	268,427

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

18. INVESTMENTS IN SUBSIDIARIES

	Company	
	2006	2005
Unlisted shares, at cost	**555,379**	517,218
Less: Provision for impairment	**(113,065)**	(108,350)
	442,314	408,868

The Company's trade and bills receivable, other receivable, trade and bills payable and other payable balances with the subsidiaries are disclosed in notes 24, 26, 30 and 31, to the financial statements respectively. The amounts due from/to subsidiaries are unsecured, interest-free and are repayable on demand.

Particulars of the principal subsidiaries are as follows:

Name	Place and date of incorporation/ registration and operations	Nominal value of issued ordinary/ registered share capital	Percentage of equity attributable to the Company Direct	Indirect	Principal activities
ZTE Kangxun Telecom Company, Limited ("Kangxun")#(i) (深圳市中興康訊電子有限公司)	The PRC/ Mainland China 1 November 1996	RMB50,000,000	90	—	Manufacture and sale of electronic components
ZTE Soft Technology Co., Limited ("ZTE Soft")(ii) (南京中興軟創科技有限責任公司)	The PRC/ Mainland China 21 February 2003	US$7,231,029	76	—	Development, manufacture and marketing of computer software and digital equipment
Xian ZTE Jingcheng Communication Company, Limited ("Xian Jingcheng")#(i) (西安中興精誠通訊有限公司)	The PRC/ Mainland China 21 May 2004	RMB15,000,000	70	—	Development, manufacture and marketing of information technology products and provision of related technical services
Shenzhen Zhongxing Software Company, Limited ("Zhongxing Software")#(ii) (深圳市中興軟件有限責任公司)	The PRC/ Mainland China 9 July 2003	RMB50,000,000	73	25	Development of telecommunications systems software and provision of related consultancy services
Wuxi Zhongxing Optoelectronics Technologies Company, Limited ("Wuxi Zhongxing")#(i) (無錫市中興光電子技術有限公司)	The PRC/ Mainland China 31 January 2000	RMB10,000,000	65	—	Development of technology for optical electronic products and provision of related technical services
ZTE Integration Telecom Ltd.#(i) (深圳中興集訊通信有限公司)	The PRC/ Mainland China 27 June 2003	RMB55,000,000	75	5	Development, manufacture and sale of information technology products

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

18. INVESTMENTS IN SUBSIDIARIES (continued)

Name	Place and date of incorporation/ registration and operations	Nominal value of issued ordinary/ registered share capital	Percentage of equity attributable to the Company Direct	Indirect	Principal activities
ZTE Mobile Tech Co., Limited ("ZTE Mobile")#(i) (深圳市中興移動技術有限公司)	The PRC/ Mainland China 12 September 2001	RMB33,333,000	95	—	Development, manufacture and sale of telecommunications related products
ZTE do Brasil Ltda##* (中興通訊(巴西)有限責任公司)	Brazil 7 August 2002	US$200,000 Ordinary	100	—	Development, manufacture and sale of telecommunications related products and provision of related technical services
Congo-Chine Telecom S.A.R.L. ("Congo-Chine")## (剛中電信有限責任公司)	The Democratic Republic of Congo 14 November 2000	US$17,450,0000 Ordinary	51	—	Construction and operation of telecommunications networks
Zhongxing Telecom Pakistan (Pvt.) Limited##* (中興通訊巴基斯坦(私人)有限公司)	Islamic Republic of Pakistan 21 September 1998	Rupees37,919,043 Ordinary	93	—	Manufacture and sale of telecommunications systems equipment
ZTE (H.K.) Limited (中興通訊(香港)有限公司)	Hong Kong 27 October 2000	HK$50,000,000 Ordinary	100	—	Marketing and sale of telecommunications systems equipment and provision of management services
Anhui Wantong Posts and Telecommunications Company, Limited ("Anhui Wantong")#(i) (安徽皖通郵電股份有限公司)	The PRC/ Mainland China 16 April 1997	RMB22,214,400	51	—	Development, manufacture and sale of computer software and integrated information systems
Shenzhen Changfei Investment Company, Limited ("Changfei")#(i) (深圳市長飛投資有限公司)	The PRC/ Mainland China 6 February 2004	RMB30,000,000	51	—	Investment holding
Shanghai Zhongxing Telecom Equipment Technology & Service Company, Limited#(i) (上海中興通訊技術有限責任公司)	The PRC/ Mainland China 10 May 2004	RMB10,000,000	51	—	Development, manufacture and sale of computer software and telecommunications systems equipment
Yangzhou Zhongxing Mobile Telecom Equipment Co., Limited#(i) (揚州中興移動通訊設備有限公司)	The PRC/ Mainland China 30 July 2002	RMB6,000,000	65	—	Development, manufacture and sale of computer software and integrated information systems

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

18. INVESTMENTS IN SUBSIDIARIES (continued)

Name	Place and date of incorporation/ registration and operations	Nominal value of issued ordinary/ registered share capital	Percentage of equity attributable to the Company Direct	Indirect	Principal activities
ZTE Microelectronics Technology Co., Ltd[#(i)] (深圳市中興微電子技術有限公司)	The PRC/ Mainland China 28 November 2003	RMB15,000,000	—	81	Design, manufacture and sale of integrated circuit products
Shenzhen Kangquan Electromechanical Company, Limited ("Kangquan")[#] (深圳市康銓機電有限公司)	The PRC/ Mainland China 2 June 2003	RMB16,000,000	—	29.33[###]	Sale of telecommunications systems equipment and provision of related technical services
Shenzhen Lead Communications Company, Limited ("Lead")[#] (深圳市立德通訊器材有限公司)	The PRC/ Mainland China 17 June 2003	RMB10,000,000	—	31.88[###]	Sale of telecommunications systems equipment and provision of related technical services
Shenzhen Ruide Electronic Industrial Company, Limited[#] (深圳市睿德電子實業有限公司)	The PRC/ Mainland China 27 April 2004	RMB8,700,000	—	29.31[###]	Sale of telecommunications systems equipment and provision of related technical services
Guangzhou Nanfang Telecommunications System Software Company Limited ("Guangzhou Nanfang Telecom")[#(i)] (廣州南方電信系統軟件有限公司)	The PRC/ Mainland China 21 September 1999	RMB12,430,000	—	63.84	Development, manufacture and marketing of telecommunication systems software
ZiMax (Cayman) Holding Ltd. ("ZiMax")	Cayman Islands 13 August 2004	US$5,500,000 Ordinary	100	—	Investment holding
ZiMax Technologies, Inc. ("ZiMax Tech")	United States of America 2 June 2005	US$5,379,945 Ordinary	—	100	Research and development of telecommunications related products

(i) These subsidiaries are registered as limited companies under the PRC law.

(ii) These subsidiaries are registered as sino-foreign joint ventures under the PRC law.

The English names of these subsidiaries are directly translated from their Chinese names.

The Chinese names of these subsidiaries are directly translated from their registered names.

These subsidiaries are the subsidiaries of a non wholly-owned subsidiary of the Company, and accordingly, are accounted for as subsidiaries by virtue of the Company's control over them.

* Not audited by Ernst & Young Hong Kong or other Ernst & Young International member firms

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

19. INVESTMENTS IN JOINTLY-CONTROLLED ENTITIES

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Unlisted shares, at cost	**—**	—	**2,500**	2,500
Share of net assets	**5,936**	6,588	**—**	—
	5,936	6,588	**2,500**	2,500

The Group's trade and bills receivable, trade and bills payable and other payable balances with a jointly-controlled entity are disclosed in notes 24, 30 and 31 to the financial statements respectively. The amounts due from/to the jointly-controlled entities are unsecured, interest-free and are repayable on demand.

Particulars of the principal jointly-controlled entities are as follows:

Name	Business structure	Place and date of incorporation/ registration and operations	Nominal Value of issued and paid-up capital/ registered capital	Percentage of Ownership interest	Percentage of Voting power	Percentage of Profit sharing	Principal activities
Beijing Zhongxing Telecom Ltd. ("Beijing Zhongxing")# (北京中興新通訊設備有限公司)	Corporate	The PRC/ Mainland China 17 March 1998	RMB5,000,000	50	50	50	Sale of telecommunications systems equipment, computer network and peripheral devices and provision of consultancy and equipment leasing services
Bestel Communications Limited ("Bestel")	Corporate	Republic of Cyprus 28 May 2001	CYP600,000 Ordinary	50	50	50	Provision of telecommunications solutions and related consultancy services

The English name of this jointly-controlled entity is directly translated from its Chinese name.

The investment in Beijing Zhongxing is directly held by the Company while that of Bestel is held by a wholly-owned subsidiary of the Company.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

19. INVESTMENTS IN JOINTLY-CONTROLLED ENTITIES (continued)

The following table illustrates the summarised financial information of the Group's jointly-controlled entities:

	2006 **RMB'000**	2005 RMB'000
Share of the jointly-controlled entities' assets and liabilities		
Current assets	**7,272**	6,163
Non-current assets	**—**	2,530
Current liabilities	**(1,336)**	(2,105)
Net assets	**5,936**	6,588
Share of the jointly-controlled entities' results		
Turnover	**633**	4,315
Other revenue	**260**	1,427
Total revenue	**893**	5,742
Total expenses	**(1,538)**	(6,940)
Tax	**(7)**	—
Loss after tax	**(652)**	(1,198)

20. INVESTMENTS IN ASSOCIATES

	Group		**Company**	
	2006 **RMB'000**	2005 RMB'000	**2006** **RMB'000**	2005 RMB'000
Unlisted shares, at cost	**—**	—	**37,088**	37,088
Share of net assets	**51,257**	35,583	**—**	—
	51,257	35,583	**37,088**	37,088
Provision for impairment	**—**	—	**(9,774)**	(12,381)
	51,257	35,583	**27,314**	24,707

The Group's trade receivable, trade payable and other payable balances with associates are disclosed in notes 24, 30, 31 to the financial statements, respectively. The amounts due from/to associates are unsecured, interest-free and are repayable on demand.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

20. INVESTMENTS IN ASSOCIATES (continued)

Particulars of the principal associates are as follows:

Name	Business structure	Place and date of incorporation/ registration and operations	Nominal Value of issued and paid-up capital/ registered capital	Percentage of ownership interest attributable to the Group	Principal activities
Beijing Zhongxing Yuanjing Technology Co., Ltd. ("Beijing Yuanjing")#* (北京中興遠景科技有限公司)	Corporate	The PRC 18 October 2000	RMB10,000,000	30	Research and development of telecommunications related products
ZTE IC Design Co. Ltd ("ZTEIC Design")#* (深圳市中興集成電路設計有限責任公司)	Corporate	The PRC 20 March 2000	RMB64,000,000	40	Design, research, development and sale of integrated circuits and related electronical products
Shenzhen Weigao Semi-conductor Technology Co., Ltd.#* (深圳市微高半導體科技有限公司)	Corporate	The PRC 15 June 2004	RMB10,000,000	20.4	Design, research, development and sale of semi-conductor products
Wuxi Kaier Technology Co., Ltd.#* (無錫凱爾科技有限公司)	Corporate	The PRC 26 November 2004	RMB10,000,000	20.07	Development, manufacture and sale of camera lenses for mobile phone
Shenzhen Zhongxing Xinyu FPC Company Limited#* (深圳市中興新宇軟電路有限公司)	Corporate	The PRC 30 July 2003	RMB11,000,000	11.58**	Development, manufacture and sale of circuits; import and exportof related products and technologies
Shenzhen Smart Electronics Ltd. ("Smart")#* (深圳思碼特電子有限公司)	Corporate	The PRC 4 July 2005	HK$30,000,000	15.3**	Development, manufacture and sale of telecommunications related components

The English names of these associates are directly translated from their Chinese names.

* Not audited by Ernst & Young Hong Kong or other Ernst & Young International member firms.

** These associates are held through a non wholly-owned subsidiary of the Company which has significant influence over the boards of directors of these associates.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

20. INVESTMENTS IN ASSOCIATES (continued)

The above table lists the associates of the Group which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other associates would, in the opinion of the directors, result in particulars of excessive length.

The year end date for the financial statements of the above associates is coterminous with those of the Group.

The following table illustrates the summarised financial information of the Group's associates extracted from their management accounts:

	2006	2005
	RMB'000	RMB'000
Assets	**395,992**	205,325
Liabilities	**244,427**	108,392
Revenues	**550,031**	169,154
Profit	**26,864**	7,543

21. AVAILABLE-FOR-SALE INVESTMENTS

	Group		**Company**	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Unlisted equity investments, at fair value	**43,488**	43,288	**41,488**	41,288

The above investments consist of investments in equity securities which were designated as available-for-sale financial assets and have no fixed maturity date or coupon rate.

The fair values of unlisted available-for-sale equity investments have been estimated using a valuation technique based on assumptions that are not supported by observable market prices or rates. The directors believe that the estimated fair values resulting from the valuation technique, which are recorded in the consolidated balance sheet, and the related changes in fair values, which are recorded in the consolidated equity, are reasonable, and that they are the most appropriate values at the balance sheet date.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

22. INVENTORIES

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Raw materials	**1,240,514**	1,248,645	**568,775**	782,628
Work in progress	**704,550**	532,923	**295,830**	287,420
Finished goods	**536,091**	458,759	**314,500**	208,044
	2,481,155	2,240,327	**1,179,105**	1,278,092

23. TELECOMMUNICATIONS SYSTEMS CONTRACTS

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Amount due from customers for contract work	**5,833,480**	4,689,157	**5,809,647**	4,440,842
Amount due to customers for contract work	**(996,275)**	(733,455)	**(991,612)**	(688,876)
	4,837,205	3,955,702	**4,818,035**	3,751,966
Contract costs incurred plus recognised profits less recognised losses to date	**21,619,372**	19,420,235	**19,673,274**	16,346,089
Less: Progress billings	**(16,782,167)**	(15,464,533)	**(14,855,239)**	(12,594,123)
	4,837,205	3,955,702	**4,818,035**	3,751,966

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

24. TRADE AND BILLS RECEIVABLES/LONG-TERM TRADE RECEIVABLES

Progress payment for telecommunications systems contracts is normally made in accordance with the agreed payment schedule. The Group's trading terms with its major customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally 90 days and is extendable up to two years depending on customers' credit worthiness. The credit terms for major customers are reviewed regularly by senior management. The Group seeks to maintain strict control over its outstanding receivables and has a credit control department to minimise credit risk. Overdue balances are reviewed regularly by senior management. In view of the aforementioned, there is no significant concentration of credit risk. Trade receivables are non-interest-bearing.

An aged analysis of the trade and bills receivables as at the balance sheet date, based on the invoice date and net of provision, is as follows:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 6 months	**6,242,121**	3,968,731	**6,381,674**	4,697,530
7 to 12 months	**650,526**	701,656	**763,464**	840,424
1 to 2 years	**448,583**	313,288	**375,495**	428,519
2 to 3 years	**13,124**	10,551	**135,215**	11,872
Over 3 years	**6,383**	215	**42,659**	39,724
	7,360,737	4,994,441	**7,698,507**	6,018,069
Current portion of trade and bills receivables	**(6,988,034)**	(4,686,775)	**(7,370,341)**	(5,690,947)
Long-term portion	**372,703**	307,666	**328,166**	327,122

The balances due from subsidiaries, the ultimate holding company, jointly-controlled entities, associates and related companies included in the above are as follows:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Subsidiaries	**—**	—	**1,813,557**	1,661,034
The ultimate holding company	**2,074**	177	**142**	8
Jointly-controlled entities	**8,874**	2,070	**8,874**	2,070
Associates	**2,869**	2,150	**—**	—
Related companies	**678**	13,314	**49**	3,071
	14,495	17,711	**1,822,622**	1,666,183

The balances are unsecured, interest-free and are repayable on demand, and on credit terms similar to those offered to the major customers of the Group.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

25. FACTORED TRADE RECEIVABLES/FACTORED LONG-TERM TRADE RECEIVABLES

At 31 December 2006, the Company and a subsidiary of the Group factored trade receivables of RMB1,552,054,000 (2005: RMB724,181,000) to banks on a without-recourse basis for cash. As the Company and the subsidiary of the Group still retained the risks and rewards associated with the delay in payment by the customers, the financial asset derecognition conditions as stipulated in HKAS 39 have not been fulfilled. Accordingly, bank advances from the factoring of the Group's trade receivables have been accounted for as liabilities in the consolidated balance sheet.

26. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Prepayments	**115,429**	154,597	**16,281**	70,729
Deposits and other receivables	**1,378,029**	1,029,214	**954,967**	1,025,357
Due from subsidiaries	**—**	—	**1,069,871**	1,122,894
Due from related companies	**3,865**	4,502	**—**	4,502
Dividend receivables	**—**	—	**817,631**	16,465
	1,497,323	1,188,313	**2,858,750**	2,239,947

The amounts due from subsidiaries and related companies are unsecured, interest-free and are repayable on demand.

27. LOAN RECEIVABLES

As at 31 December 2006, the Group had two loan receivables from customers.

A loan receivable of US$1,777,000 (equivalent to approximately RMB13,941,000) was granted during the year. The balance is unsecured, interest-free and is repayable in September 2007.

Another loan receivable of EUR787,500 (equivalent to approximately RMB8,085,000) (2005: RMB30,176,000) bore interest at the three-month EURIBOR + 1% to 3%, was repayable in four installments which had been fully repaid by February 2007.

A loan of SEK43,000,000 (equivalent to approximately RMB44,015,000) bore interest at the STIBOR + 3% to 8%, was granted in 2005 and secured by certain properties and shares of the customer and guaranteed by the customer's immediate holding company. The balance was repaid during the year.

The balance is measured at amortised cost in accordance with the valuation technique using the effective interest method. The directors believe that the carrying amount resulting from the valuation technique approximates to its fair value, which is reasonable and is the most appropriate value at the balance sheet date.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

28. EQUITY INVESTMENT AT FAIR VALUE THROUGH PROFIT OR LOSS

The equity investment for the Group and the Company at 31 December 2006 was listed in Hong Kong and was classified as held for trading.

29. CASH AND CASH EQUIVALENTS AND PLEDGED BANK DEPOSITS

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash and bank balances	**3,168,658**	4,178,498	**2,018,061**	3,007,727
Time deposits	**1,142,402**	1,394,634	**939,859**	1,251,209
	4,311,060	5,573,132	**2,957,920**	4,258,936
Less: Pledged bank deposits	**(168,997)**	(175,899)	**(35,201)**	(46,126)
Cash and cash equivalents	**4,142,063**	5,397,233	**2,922,719**	4,212,810

At the balance sheet date, the cash and bank balances of the Group denominated in Renminbi amounted to approximately RMB2,072,490,000 (2005: RMB3,689,593,000). The Renminbi is not freely convertible into other currencies, however, under Mainland China's Foreign Exchange Control Regulations and Administration of Settlement, Sale and Payment of Foreign Exchange Regulations, the Group is permitted to exchange Renminbi for other currencies through banks authorised to conduct foreign exchange business.

At 31 December 2006, except for the pledged bank deposits of RMB31 million (2005: Nil) were frozen for a litigation proceeding (note 42(b)), all other pledged bank deposits were for banking facilities.

Cash at banks earns interest at floating rates based on daily bank deposit rates. Short-term time deposits are made for varying periods of between one day and three months depending on the immediate cash requirements of the Group, and earn interest at the respective short-term time deposit rates. The carrying amounts of the cash and cash equivalents and pledged deposits approximate to their fair values.

30. TRADE AND BILLS PAYABLES

An aged analysis of the trade and bills payables as at the balance sheet date, based on the invoice date, is as follows:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Within 6 months	**6,816,521**	6,049,126	**8,858,602**	8,418,896
7 to 12 months	**81,489**	142,100	**704**	3,698
1 to 2 years	**47,855**	45,968	**8,256**	11,343
2 to 3 years	**14,612**	5,506	**1,272**	3,778
Over 3 years	**31,188**	27,092	**23,087**	19,738
	6,991,665	6,269,792	**8,891,921**	8,457,453

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

30. TRADE AND BILLS PAYABLES (continued)

The balances due to subsidiaries, the ultimate holding company, related companies, associates and a jointly-controlled entity included in the above are as follows:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Subsidiaries	**—**	—	**8,778,447**	8,248,272
The ultimate holding company	**147,860**	104,563	**—**	—
Related companies	**71,367**	125,867	**3,724**	2,975
Associates	**22,108**	15,557	**—**	—
A jointly-controlled entity	**301**	182	**—**	—
	241,636	246,169	**8,782,171**	8,251,247

The balances are unsecured, interest-free and are repayable on demand.

The trade payables are non-interest-bearing and are normally settled on 90-day terms.

31. OTHER PAYABLES AND ACCRUALS

		Group		Company	
		2006	2005	**2006**	2005
	Note	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Receipts in advance		**631,231**	860,106	**513,954**	492,673
Other payables		**890,569**	940,784	**476,793**	637,286
Accruals		**974,730**	847,861	**613,222**	562,147
Provision for warranties	35	**230,417**	248,998	**230,417**	248,998
Due to the ultimate holding company		**361**	313	**361**	313
Due to subsidiaries		**—**	—	**367,862**	647,775
Due to a jointly-controlled entity		**—**	1,024	**—**	1,024
Due to associates		**300**	765	**—**	765
Due to related companies		**4,964**	286	**272**	—
		2,732,572	2,900,137	**2,202,881**	2,590,981

The other payables are non-interest-bearing and have an average term of three months. The balances due to ultimate holding company, subsidiaries, a jointly-controlled entity, associates and related companies are unsecured, interest-free and are repayable on demand.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

32. INTEREST-BEARING BANK BORROWINGS

Group	2006 Effective interest rate (%)	2006 Maturity	2006 RMB000	2005 Effective interest rate (%)	2005 Maturity	2005 RMB000
Current						
Bank loans — unsecured	4.43–6.14	2007	274,116	5.58–6.14	2006	552,000
Bank loans — unsecured	LIBOR+0.5	2007	546,610	—	—	—
Bank loans — secured	5.02	2007	125,000	4.96	2006	47,695
			945,726			599,695
Non-current						
Bank loans — secured	LIBOR+1.5	2015	269,737	—	—	—
Bank loans — unsecured	4–4.32	2008–2010	980,000	4	2007	80,000
Bank loans — unsecured	LIBOR+0.4	2008–2009	429,505	—	—	—
			1,679,242			80,000
			2,624,968			679,695

Company	2006 Effective interest rate (%)	2006 Maturity	2006 RMB000	2005 Effective interest rate (%)	2005 Maturity	2005 RMB000
Current						
Bank loans — unsecured	4.43–6.14	2007	195,217	5.58-6.14	2006	500,000
Bank loans — unsecured	LIBOR+0.5	2007	546,610	—	—	—
			741,827			500,000
Non-current						
Bank loans — unsecured	4.05–4.32	2008–2010	900,000	—	—	—
Bank loans — unsecured	LIBOR+0.4	2008–2009	429,478	—	—	—
			1,329,478			—
			2,071,305			500,000

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

32. INTEREST-BEARING BANK BORROWINGS (continued)

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Analysed into:				
Bank loans repayable:				
Within one year or on demand	**945,726**	599,695	**741,827**	500,000
In the second year	**1,033,157**	80,000	**1,017,130**	—
In the third to fifth years, inclusive	**376,348**	—	**312,348**	—
Beyond five years	**269,737**	—	**—**	—
	2,624,968	679,695	**2,071,305**	500,000

Notes:

(a) Except for bank loans of approximately RMB1,521,042,000 (2005: RMB127,696,000) which are denominated in United Sates dollars, all borrowings are in Renminbi.

(b) Except for the unsecured bank loans with a carrying amount of RMB1,254,116,000 (2005: RMB632,000,000) and a secured bank loan with a carrying amount of RMB125,000,000 (2005: RMB47,695,000), all borrowings of the Group bear interest at floating interest rates.

The Group's and the Company's secured bank loans or banking facilities are secured by:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Pledged bank deposits	**137,997**	175,899	**4,201**	46,126
Trade receivables	**1,552,054**	771,876	**1,545,800**	688,605
	1,690,051	947,775	**1,550,001**	734,731

Certain of the Group's and Company's unsecured bank loans are guaranteed by:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Other banks or government	**120,900**	580,000	**—**	500,000

The carrying amounts of the Group's and the Company's borrowings approximate to their fair values.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

33. PROVISION FOR RETIREMENT BENEFITS

The Group and the Company provide certain of the eligible staff with post-retirement benefits pursuant to a retirement benefits plan. The plan is funded solely by the Group on an actual payment basis.

The latest actuarial valuation of the plan was conducted at 31 December 2006 in accordance with HKAS 19 *Employee Benefits* by qualified actuaries of Watson Wyatt Hong Kong Limited. The present value of defined benefits obligations and current service costs are determined actuarially based on the projected unit credit method, which involves a number of assumptions and estimates including the rate of inflation, discount rate, employees' turnover ratio as well as mortality rate. Actuarial gains/(losses) are recognised by amortising the amount by which cumulative unrecognised gains/(losses) exceed 10% of the greater of the assets of the plan and the defined benefits obligations over the average expected future working lifetime of the active members of the plan.

The benefits obligations recognised in the balance sheet are as follows:

Group and Company

	2006 RMB'000	2005 RMB'000
Present value of the obligations	**58,234**	54,577
Unrecognised actuarial losses	**(26,176)**	(24,118)
Net liability in the balance sheet	**32,058**	30,459

Movements in the net liability recognised in the balance sheet during the year are as follows:

	2006 RMB'000	2005 RMB'000
Net liability at beginning of year	**30,459**	28,923
Benefits expenses recognised in the consolidated income statement	**2,787**	2,224
Pension payments made	**(1,188)**	(688)
Net liability at end of year	**32,058**	30,459

The principal assumptions used in determining the pension benefits obligations are shown below:

	2006	2005
(a) Discount rate	**3.75%**	3.5%

(b) The expected rate of increase in salaries ranged from 1% to 7.5% per annum, which was based on the number of years of employment.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

33. PROVISION FOR RETIREMENT BENEFITS (continued)

The benefits expense recognised in the consolidated income statement for the year is as follows:

	2006	2005
	RMB'000	RMB'000
Current service cost	**—**	—
Interest cost on benefits obligations	**1,890**	1,935
Net actuarial losses recognised in the year	**897**	289
Benefits expense included in staff costs — note 6	**2,787**	2,224

34. OTHER LONG-TERM PAYABLES

Other long-term payables represent government grants which are unsecured, interest-free and have no fixed terms of repayment.

35. PROVISION FOR WARRANTIES

	Group		**Company**	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
At beginning of year	**248,998**	186,227	**248,998**	186,227
Additional provisions	**114,724**	225,790	**114,724**	225,790
Amounts utilised during the year	**(133,305)**	(163,019)	**(133,305)**	(163,019)
At 31 December 2006	**230,417**	248,998	**230,417**	248,998

In respect of telecommunications systems contracts, the Group and the Company provide warranties to their customers for twelve months after contract completion dates, during which free repair and maintenance services are provided. A provision for warranties is made at 2% to 2.5% of the cost of equipment sold during the year, and is estimated based on the equipment return rate and past experience of the level of repairs and maintenance. The estimation is reviewed on an ongoing basis and revised where appropriate.

In respect of handsets, the Group and the Company generally provide a one-year warranty to their customers under which faulty products will be repaired or replaced. The amount of provision for warranties is estimated based on sales volume and past experience of the level of repairs and return.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

36. DEFERRED TAX

The movements in deferred tax assets and liabilities during the year are as follows:

	Group		Company	
	2006	2005	**2006**	2005
	RMB'000	RMB'000	**RMB'000**	RMB'000
Deferred tax assets:				
At beginning of year	**59,587**	104,681	**55,113**	76,475
Deferred tax credit/(charged) to the income statement during the year (note 10)	**151,336**	(45,094)	**139,434**	(21,362)
At end of year	**210,923**	59,587	**194,547**	55,113
Deferred tax assets:				
Provision against inventories	**53,166**	39,069	**44,088**	39,069
Provision for warranties	**34,562**	37,350	**34,562**	37,350
Provision for retirement benefits	**4,809**	4,569	**4,809**	4,569
Tax losses	**51,141**	—	**51,141**	—
Overseas tax	**87,516**	—	**87,516**	—
Government grants	**399**	739	**399**	739
Unrealised profit arising on consolidation	**7,298**	4,474	**—**	—
Deferred tax liabilities:				
Intangible assets	**(27,968)**	(26,614)	**(27,968)**	(26,614)
Deferred tax assets, net	**210,923**	59,587	**194,547**	55,113

At 31 December 2005 and 2006, there was no significant unrecognised deferred tax liability for taxes that would be payable on the unremitted earnings of certain of the Group's subsidiaries, jointly-controlled entities and associates as the Group has no liability to additional tax should such amounts be remitted.

37. SHARE CAPITAL

	2006	2005
	RMB'000	RMB'000
Registered, issued, and fully paid		
State-owned A shares of RMB1.00 each	**392,080**	392,080
Legal person A shares of RMB1.00 each	**29,724**	29,724
Individual A shares of RMB1.00 each	**377,567**	377,567
H shares of RMB1.00 each	**160,151**	160,151
	959,522	959,522

Zhongxingxin, the ultimate holding company of the Group, has further undertaken not to sell its original non-tradable shares amounting to more than five percent and ten percent of the total share capital of the Company during the period from the 13th month to 24th month and the period from the 25th month to 36th month subsequent to their listing on the Shenzhen Stock Exchange on 29 December 2005, respectively.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

37. SHARE CAPITAL (continued)

Zhongxingxin has further provided a specific undertaking that where it sells its shares during the period from the 13th month to the 24th month after such shares have been granted the right of listing and circulation on the Shenzhen Stock Exchange, the price at which the shares are sold shall not be lower than the mathematical average of the closing prices of its A Shares for the 60 trading days prior to the first announcement of the Share Reform Plan by the Board, that is, RMB26.75 per share. The proceeds from any sale in breach of such undertaking shall be reverted to the Company's account for the benefit of all shareholders of the Company.

38. SHARE INCENTIVE SCHEME

During the year, the Company launched a share incentive scheme for providing incentive and reward to 3,435 employees of the Company and its subsidiaries (the "Participants"), including 21 directors and senior management pursuant to which the Company has agreed to grant a total number of 43,182,000 A shares (the "Awarded Shares") for the benefit of the Participants. The Participants have to pay the subscription amounts for the Awarded Shares on the basis of the purchase of 5.2 Awarded Shares at the subscription price for every 10 Awarded Shares granted, out of which the subscription amounts for 3.8 Awarded Shares are funded by the Participants at their own cost and the subscription amounts for the 1.4 Awarded Shares are funded by the conversion of the deferred bonus that the Participants would otherwise have received prior to their agreement not to participate in the distribution of 2006 deferred bonus. The subscription price is RMB30.05 per share, being the closing price of the Company's A shares as quoted on the Shenzhen Stock Exchange on the trading day immediately preceding the date on which the board meeting for reviewing the share incentive scheme was convened for the first time.

According to the share incentive scheme, the Company has set aside a total number of 4,798,000 shares (the "Potential Awarded Shares") for granting to employees (the "Potential Participants") who make significant contributions to the Company and important personnel required by the Company who are identified after the share incentive scheme has been reviewed and passed at the general meeting. The Supervisor Committee will verify the qualifications of the aforesaid employees. The admission of Directors, Supervisors and Senior Management as the Potential Participants shall be submitted to the general meetings of the Company for its approval. The subscription price for the Potential Awarded Shares will be calculated on the same basis of the Awarded Shares as described above.

The Awarded Shares and the Potential Awarded Shares will be vested to the Participants subject to the terms and conditions attached to the share incentive scheme for a period no shorter than two years from the date of approval, during which the participants shall be restricted from disposing of any of the Awarded Shares. The shares awarded by the Company under the share incentive scheme are considered to be share-based payments under HKFRS 2.

The fair value of the shares awarded during the year was estimated at approximately RMB2,480,000.

The fair value of shares awarded during the year was estimated as at the date of grant, valued by an independent professional valuer, Towers Perrin, taking into account the expected future dividend yield prior to the vesting of the Awarded Shares of which the participants will not be entitled, and other terms and conditions upon which the shares were awarded.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

39. RESERVES

(a) Group

The amounts of the Group's reserves and the movements therein for the current and prior years are presented in the consolidated statement of changes in equity on pages 177 and 178 of the financial statements.

The capital reserves of the Group include the non-distributable reserves of the Company and its subsidiaries created in accordance with accounting and financial regulations in the PRC.

In accordance with the PRC Company Law and the Company's articles of association, the Company and its subsidiaries registered in the PRC are required to appropriate certain percentage of the statutory net profit after tax to the statutory reserve fund. Subject to certain restrictions set out in the relevant PRC regulations and in the subsidiaries' articles of association, the statutory reserve fund may be used either to offset losses, or for capitalisation issues by way of paid-up capital. The reserves cannot be used for purposes other than those for which they are created and are not distributable as cash dividends.

The share incentive scheme reserve was created for the share incentive scheme launched by the Company to provide incentive and reward to certain employees of the Company and its subsidiaries.

(b) Company

	Notes	Issued share capital RMB'000	Capital reserve RMB'000	Share incentive scheme reserves RMB'000	Statutory reserves RMB'000	Exchange fluctuation reserve RMB'000	Retained profits RMB'000	Proposed final dividend RMB'000	Total RMB'000
At 1 January 2005		959,522	5,462,515	—	650,718	3,561	229,830	239,880	7,546,026
Final 2004 dividend declared		—	—	—	—	—	—	(239,880)	(239,880)
Transfer from/(to) retained profits		—	—	—	118,885	—	(118,885)	—	—
Profit for the year		—	—	—	—	—	1,084,317	—	1,084,317
Proposed final 2005 dividend	12	—	—	—	—	—	(239,880)	239,880	—
Exchange realignments and other income recognised directly in equity		—	5,306	—	—	(3,509)	—	—	1,797
At 31 December 2005 and 1 January 2006		959,522	5,467,821	—	769,603	52	955,382	239,880	8,392,260
Final 2005 dividend declared		—	—	—	—	—	—	(239,880)	(239,880)
Transfer from/(to) retained profits		—	—	—	—	—	—	—	—
Loss for the year		—	—	—	—	—	831,130	—	831,130
Proposed final 2006 dividend	12	—	—	—	—	—	(143,928)	143,928	—
Exchange realignments and other income recognised directly in equity		—	—	—	—	(1,545)	—	—	(1,545)
Equity settled share expense	38	—	—	2,480	—	—	—	—	2,480
At 31 December 2006		959,522	5,467,821	2,480	769,603	(1,493)	1,642,584	143,928	8,984,445

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

40. DISPOSAL OF INTERESTS IN SUBSIDIARIES

	2006 RMB'000	2005 RMB'000
Net assets disposed of:		
Property, plant and equipment	—	6,128
Intangible assets	—	3,709
Available-for-sale investment	—	1,582
Inventories	—	11,013
Cash and bank balances	10,518	31,552
Trade receivables	—	26,399
Prepayments and other receivables	254	5,880
Trade payables	—	(14,833)
Short-term loan	—	(9,990)
Accruals and other payables	(78)	(35,517)
Minority interests	(100)	(11,555)
	10,594	14,368
Loss on disposal of interests in subsidiaries	—	(1,198)
Gain on deemed disposal of interest in a subsidiary	—	3,655
	10,594	16,825

	2006 RMB'000	2005 RMB'000
Satisfied by:		
Cash	10,229	328
Reclassification from interests in subsidiaries to interests in associates	365	10,900
Reclassification from interests in subsidiaries to interests in jointly-controlled entities	—	5,597
	10,594	16,825

An analysis of the net inflow of cash and cash equivalents in respect of the disposal of interests in subsidiaries is as follows:

	2006 RMB'000	2005 RMB'000
Cash consideration	10,229	328
Cash and bank balances disposed of	(10,518)	(31,552)
Net outflow of cash and cash equivalents in respect of the disposal of interests in subsidiaries	(289)	(31,224)

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

41. NOTE TO THE CONSOLIDATED CASH FLOW STATEMENT

Major non-cash transaction

During the year, the Company acquired a 3% interest in ZTE Software from another shareholder with effect from July 2006 at a consideration of approximately RMB29 million. The consideration was included in the other payables at 31 December 2006.

42. CONTINGENT LIABILITIES

(a) At the balance sheet date, contingent liabilities not provided for in the financial statements were as follows:

Group and Company

	2006	2005
	RMB'000	RMB'000
Factored trade receivables	**107,181**	438,490
Guarantees given to banks in respect of performance bonds	**5,200,588**	2,823,760
	5,307,769	3,262,250

(b) On 3 November 2005, a Jiangsu Provincial Higher People's Court (the ''Court'') action was commenced by a customer against a subsidiary of the Group and the Company in respect of a claim for return of advance payment, accrued interest and compensating losses of approximately RMB71 million in aggregate. As at the date of approval of these financial statements, no decision had been made in the court proceedings.

Meanwhile, RMB31 million of the Group's cash had been temporary frozen and the real estate title certificate for certain of the Group's buildings with net book value of approximately RMB117.2 million were held by the court as security for such litigation. In the opinion of the directors, based on legal advice from the Company's lawyer engaged for this action, the subsidiary of the Group and the Company have valid defences against such claims and any resulting liabilities would not have any material adverse impact on the Group's financial position. Therefore, no provision in respect of such claims was made in the financial statements.

(c) On 16 December 2005, an arbitration was commenced by a foreign supplier against the Company in respect of claims for breach of contract and infringement of intellectual property rights in the amount of approximately US$36,450,000 (equivalent to approximately RMB294.2 million) in aggregate.

As at the approval date of these financial statements, no arbitral award or other decision by the tribunal had been made on the claims. In the opinion of the directors, based on legal advice from the Company's lawyer engaged for the action, the Company had valid defences against the claims brought in the arbitration, the directors currently believed that the outcome of the arbitration would not have a material adverse impact on the Group's financial position. Therefore, no provision in respect of such claims had been made in the financial statements.

(d) On 18 August 2005, the Company received a notice of arbitration from a foreign consultant in respect of a claim for consultancy fee, agency fee and compensation for undue delay in honouring payment with a total amount approximately US$1,714,000 (equivalent to approximately RMB13,384,000). During the year of 2006, the plaintiff raised the claim to approximately US$2,143,000 (equivalent to approximately RMB16,734,000).

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

42. CONTINGENT LIABILITIES (continued)

(d) (continued)

As at the approval date of these financial statements, no decision has been made in the arbitration. In the opinion of the directors, based on legal advice from the Company's lawyer engaged for this action, the Company has valid defences, against such claims and any resulting liabilities would not have any material adverse impact on the Group's financial position. Therefore, no provision in respect of such claims has been made in the financial statements.

(e) In 2005, ZTE Pakistan Private Limited, the subsidiary of the Group in Pakistan had commenced a defence action against the Collectorate of Customs, Sales Tax and Central Excise (Adjudication/Appeals), Rawalpindi in respect of a claim by the latter for additional customs duties of approximately Rs.177 million (equivalent to approximately RMB23.9 million), which was subsequently raised to approximately Rs.240 million (equivalent to approximately RMB31.2 million) and a penalty of approximately Rs.2.4 billion (equivalent to approximately RMB324 million) for an alleged misdeclaration of imported goods in the Customs, Central Excise and Sales Tax Appellate Tribunal, Islamabad, Pakistan.

The Central Board of Revenue referred all disputes between the parties to the Alternate Dispute Resolution Committee (the "Committee") for resolution and on 5 September 2005, the Committee has recommended in favour of the subsidiary of the Group.

As at the approval date of these financial statements, no decision has been made in the Tribunal. The directors estimated that the maximum financial impact to the Group relating to additional customs duties would be in the order of approximately Rs.36 million (equivalent to approximately RMB4.8 million) and has made an accrual of RMB4 million accordingly in the Group's financial statements for the year ended 31 December 2006. In the opinion of the directors, based on legal advice from the Company's lawyer engaged for this action, the subsidiary of the Group has valid defences, against the aforesaid claims and any resulting liabilities would not have any material adverse impact on the Group's financial position. Therefore, no further provision in respect of customs duties penalty was considered necessary to be made in the financial statements.

(f) In August 2006, a foreign customer commenced an arbitration for a claim against the Company, for Rs.762,982,000 (equivalent to approximately RMB97,980,000), in respect of the Company's failure to honour a contract. As at the approval date of these financial statements, the arbitration body has not made any decision regarding the case; while in return, the Company has launched a counter claim against the foreign customer for failure in honouring the contract. As at the approval date of these financial statements, no decision has been made in the arbitration and neither did the Company pay any compensation regarding the arbitration. In the opinion of the directors, based on legal advice from the Company's lawyer engaged for this action, the Company had valid defence against such claims and any resulting liabilities would not have material adverse impact on the Group's financial position. Accordingly, no provision in respect of such claims was made in the financial statements.

(g) The Group has provided a financial guarantee for an independent customer with a maximum amount of RMB50 million included corresponding interest, which will expire in September 2018.

In accordance with HKAS 39 and HKFRS 4, such financial guarantee contract is accounted for as a financial liability and recognised initially at its fair value of RMB3,689,000.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

43. PLEDGE OF ASSETS

Details of the Group's bank loans, which are secured by the assets of the Group, are included in note 32 to the financial statements.

44. OPERATING LEASE ARRANGEMENTS

(a) As lessor

The Group is entitled to share a portion of the profit generated from the telecommunication network as disclosed in note 15 to the financial statements. During the year, approximately RMB 29 million (2005: Nil) of operating lease rental income had been recognised under this arrangement.

(b) As lessee

The Group leases certain of its offices under operating lease arrangements, with leases negotiated for terms ranging from 1 to 12 years.

At 31 December 2006, the Group had total future minimum lease payments under non-cancellable operating leases falling due as follows:

	2006	2005
	RMB'000	RMB'000
Within one year	**118,347**	97,047
In the second to fifth years, inclusive	**81,470**	79,109
After five years	**1,554**	7,269
	201,371	183,425

45. COMMITMENTS

In addition to the operating lease commitments detailed in note 44 above, the Group had the following commitments at the balance sheet date:

Capital commitments

	2006	2005
	RMB'000	RMB'000
Land and buildings:		
Contracted, but not provided for	**795,991**	231,561
Investment in associates:		
Contracted, but not provided for	**80,331**	21,065

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

46. DIFFERENCES IN FINANCIAL STATEMENTS PREPARED UNDER PRC GAAP AND HKFRSs

Ernst & Young is responsible for the audit of the Group's and the Company's financial statements prepared under HKFRSs.

The effects on the net profit and shareholders' equity arising from material differences between the consolidated financial statements prepared under PRC GAAP and those under HKFRSs are summarised as follows:

	Notes	**2006 RMB'000**	2005 RMB'000
Profit			
Profit from ordinary activities attributable to shareholders under PRC GAAP		**807,353**	1,194,343
Add back/(deduct):			
Accounting standards differences			
Recognition of government grants	(i)	**2,123**	(8,881)
Provision for retirement benefits	(ii)	**(1,599)**	(1,536)
Deferred development costs	(iii)	**(52,357)**	115,621
Recognition of an excess over the cost of business combinations	(iv)	**—**	9,460
Deferred tax	(v)	**(1,454)**	(21,306)
Fair value gains on an equity investment at fair value through profit or loss	(vi)	**16,595**	—
Recognition of a financial guarantee contract	(vii)	**(3,689)**	—
Profit attributable to equity holders of the parent under HKFRSs		**766,972**	1,287,701
Shareholders' equity			
Shareholders' equity under PRC GAAP		**10,678,911**	10,125,095
Add back/(deduct):			
Accounting standards differences			
Recognition of government grants	(i)	**(2,805)**	(4,926)
Provision for retirement benefits	(ii)	**(32,058)**	(30,459)
Deferred development costs	(iii)	**129,751**	182,108
Deferred tax	(v)	**(22,760)**	(21,306)
Fair value gains on an equity investment at fair value through profit or loss	(vi)	**16,595**	—
Recognition of a financial guarantee contract	(vii)	**(3,689)**	—
Equity attributable to equity holders of the parent under HKFRSs		**10,763,945**	10,250,512

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

46. DIFFERENCES IN FINANCIAL STATEMENTS PREPARED UNDER PRC GAAP AND HKFRSs (continued)

(i) Government grants

Government grants for specific research and development projects are accounted for as specific payables under PRC GAAP. Whereas under HKFRSs, such grants are accounted for as deferred income in the other payable or other long-term payable accounts.

Under PRC GAAP, research and development costs are recognised as technology development costs in inventories to the extent of the granted amounts, and the specific payables thereof will be transferred to the inventory account to offset the technology development costs upon completion of the projects.

Under HKFRSs, deferred income is recognised as income over the periods necessary to match the grants on a systematic basis to the costs that they are intended to compensate.

(ii) Provision for retirement benefits

Under PRC GAAP, there is no specific standard, regulation or rule for the recognition of post-retirement benefits under defined retirement benefits plan. The costs of post-retirement benefits are expensed as incurred.

Under HKFRSs, the costs of providing these benefits under the defined retirement benefits plan are actuarially determined and recognised over the employees' service period.

(iii) Deferred development costs

Under PRC GAAP, all research and development costs are charged to the income statement as incurred.

Under HKFRSs, expenditure incurred on projects to develop new products is capitalised and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably; there is reasonable certainty that the projects are technically feasible; and the products have commercial value. Product development expenditure which does not meet these criteria is expensed when incurred.

(iv) Excess over the cost of business combinations

Under PRC GAAP, an excess over the cost of business combination is credited to the capital reserve.

Under HKFRSs, any excess of the Group's interest in the net fair value of the acquirees' identifiable assets and liabilities over the cost of acquisition of such acquirees (previously referred to as negative goodwill), after reassessment, is recognised immediately in the income statement.

(v) Deferred tax

Deferred tax is recognised to account for the effect of any temporary differences arising from the accounting differences between PRC GAAP and HKFRSs in the preparation of the Group's financial statements under PRC GAAP and HKFRSs.

(vi) Fair value gains on an equity investment at fair value through profit or loss

Under PRC GAAP, equity investments held for trading are measured at cost.

Under HKFRSs, equity investments held for trading are classified as financial assets at fair value through profit or loss. Any gains or losses result from change in fair value are recognised in the income statement.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

46. DIFFERENCES IN FINANCIAL STATEMENTS PREPARED UNDER PRC GAAP AND HKFRSs (continued)

(vii) Financial guarantee contract

Under PRC GAAP, there is no specific standard, regulation or rule for the recognition of financial guarantee contracts. Such financial guarantee contracts are disclosed as a contingent liability.

Under HKFRSs, financial guarantee contracts are accounted for as financial liabilities which are recognised initially at its fair value. Subsequent to initial recognition, the Group measures its financial guarantee contract at the higher of: (i) the amount determined in accordance with HKAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and (ii) the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with HKAS 18 *Revenue*.

47. RELATED PARTY TRANSACTIONS

(I) Transactions with related parties

In addition to the transactions and balances detailed elsewhere in these financial statements, the Group had the following material related party transactions during the year:

	Notes	**2006 RMB'000**	2005 RMB'000
The ultimate holding company:			
Purchase of raw materials	(a)	**359,439**	311,970
Sale of finished goods	(b)	**3,682**	545
Shareholders of the ultimate holding company:			
Purchase of raw materials	(a)	**145,991**	208,207
Sale of finished goods	(e)	**7,830**	19,621
Jointly-controlled entities:			
Purchase of raw materials	(a)	**—**	89
Sale of finished goods	(b)	**31,947**	7,513
Acquisition of a 19% equity interest in ZTE ITS Limited	(c)	**—**	1,024
Associates:			
Purchase of raw materials	(a)	**105,858**	48,787
Sale of finished goods	(b)	**18,101**	2,815
Sale of finished goods	(e)	**—**	9,025
Purchase of raw materials	(e)	**—**	5,874
Entity controlled by key management personnel of the Group:			
Purchase of raw materials	(a)	**217**	8,166
Shareholder of a subsidiary:			
Corporate guarantee	(d)	**80,000**	80,000
Fellow subsidiaries:			
Purchase of raw materials	(a)	**107,379**	125,950
Sale of finished goods	(b)	**1,218**	13

In the opinion of the directors, the above transactions were conducted in the ordinary course of business.

NOTES TO FINANCIAL STATEMENTS
(Prepared under Hong Kong financial reporting standards)
31 December 2006

47. RELATED PARTY TRANSACTIONS (continued)

(I) Transactions with related parties (continued)

Notes:

(a) The purchases of raw materials were made in accordance with published prices and conditions similar to those offered by the suppliers to their major customers.

(b) The sales of finished goods were made in accordance with published prices and conditions offered to major customers of the Group.

(c) In 2005, Beijing Zhongxing Telecom Ltd, the Group's 50% owned jointly-controlled entity, disposed of its 70% equity interest in ZTE ITS Limited, of which 19% of the disposed interests was acquired by the Company for a cash consideration of RMB1,024,000. Subsequent to the disposal of the 70% equity interests in ZTE ITS Limited by Beijing Zhongxing Telecom Ltd, ZTE ITS Limited, which was formerly a 35% owned jointly-controlled entity of the Group, became a 19% owned available-for-sale investment of the Group.

(d) The guarantee in respect of bank borrowings was provided by related parties at nil consideration.

(e) The purchase and sale prices of the goods were determined at rates mutually agreed between the Group and the related parties.

(II) Outstanding balances with related parties:

(i) Details of the Group's trade balances with the ultimate holding company, jointly-controlled entities, associates and other related parties as at balance sheet date are disclosed in notes 24 and 30 to the financial statements.

(ii) Details of the Group's balances of receivables and payables which are not trading in nature with the ultimate holding company, jointly-controlled entities, associates and other related parties as at balance sheet date are disclosed in notes 26 and 31 to the financial statements.

(III) Compensation of key management personnel of the Group

	2006	2005
	RMB'000	RMB'000
Short-term employee benefits	**4,992**	4,875
Post-employment benefits	**74**	53
Total compensation paid to key management personnel	**5,066**	4,928

Included in the transactions with the Group's ultimate holding company and the fellow subsidiaries, certain transactions amounting to approximately RMB451 million constitute continuing connected transactions as defined in Chapter 14A of the Listing Rules.

NOTES TO FINANCIAL STATEMENTS

(Prepared under Hong Kong financial reporting standards)
31 December 2006

48. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The main risks arising from the Group's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. Generally, the Group introduces conservative strategies on its risk management. As the Group's exposure to these risks is kept to a minimum, the Group has not used any derivatives and other instruments for hedging purposes. The Group does not hold or issue derivative financial instruments for trading purposes. The board of directors reviews and agrees policies for managing each of these risks and they are summarised as follows:

Interest rate risk

At 31 December 2006, the bank loans of the Group and the Company including fixed rate debts and floating debts based on LIBOR. The Group and the Company have no significant concentration of interest rate risk.

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from sales or purchases by operating units in currencies other than the units' functional currency, where the revenue is predominately in US$ and RMB and certain portion of the bank loans is denominated in US$. The Group tends to accept foreign currency exchange risk avoidance or allocation terms when arriving at purchase and sales contracts. The Group takes rolling forecast on foreign currency revenue and expenses, matches the currency and amount incurred, so as to alleviate the impact to business due to exchange rate fluctuation.

Credit risk

With respect to credit risk arising from the other financial assets of the Group, which comprise cash and cash equivalents, and trade receivables, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

In order to minimise the credit risk, the management of the Group has delegated a team responsible for determination of credit limits, credit approvals and other monitoring procedures to ensure that follow-up action is taken to recover overdue debts. In addition, the Group reviews regularly the recoverable amount of each individual trade receivables to ensure that adequate impairment losses are made for irrecoverable amounts. In this regard, the directors of the Company consider that the Group's credit risk is minimal.

Liquidity risk

The Group's objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and other interest-bearing loans. In addition, banking facilities have been put in place for contingency purposes.

49. POST BALANCE SHEET EVENT

During the 5th Session of the 10th National People's Congress, which was concluded on 16 March 2007, the PRC Corporate Income Tax Law (''the New Corporate Income Tax Law'') was approved and will become effective on 1 January 2008. The New Corporate Income Tax Law introduces a wide range of changes which include, but are not limited to, the unification of the income tax rate for domestic-invested and foreign-invested enterprises at 25%. Since the detailed implementation and administrative rules and regulations have not yet been announced, the financial impact of the New Corporate Income Tax Law to the Group cannot be reasonably estimated at this stage.

50. APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved and authorised for issue by the board of directors on 18 April 2007.