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

China Netcom Group Corporation (Hong Kong) Limited

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

HKSE : 906 NYSE : CN

China Netcom **Brings the Olympics** to You

2007
Annual Report

Contents

Company Profile and Corpoate Information

China Netcom Group Corporation (Hong Kong) Limited (the "Company"; together with its subsidiaries, the "Group") was incorporated in Hong Kong with limited liability under the Companies Ordinance (Chapter 32 of the Laws of Hong Kong) on October 22, 1999. The shares of the Company were listed on The New York Stock Exchange on November 16, 2004 and the Main Board of The Stock Exchange of Hong Kong Limited (the "Hong Kong Stock Exchange") on November 17, 2004.

The Company is a leading broadband and fixed-line communications operator in China. After we sold the telecommunications assets, liabilities and business operations in Guangdong Province and Shanghai Municipality on February 28, 2007, our service regions consist of Beijing Municipality, Tianjin Municipality, Hebei Province, Henan Province, Shandong Province, Liaoning Province, Heilongjiang Province, Jilin Province, Neimenggu Autonomous Region and Shanxi Province.

In our service regions, the Company provides fixed-line voice and value-added services, broadband and other Internet-related services, information and communications technology (ICT) services, business and data communications services and advertising and media services.

The Company's principal services consist of:

- Fixed-line voice and value-added services, including local, domestic long distance, international long distance and fixed-line value-added services;
- Broadband and other Internet-related services, including broadband and narrow-band Internet access services like XDSL, LAN, dial-up, wireless as well as broadband content and applications services;
- ICT services, including IT and CT based integrated solutions such as system integration, software, outsourcing, special advisory, and professional services like Internet information and disaster recovery services;
- Business and data communications services, including managed data and leased-line services; and
- Advertising and media business.

As of December 31, 2007, the total number of the Company's ordinary shares in issue was 6,674,328,400. China Network Communications Group Corporation ("China Netcom Group", our ultimate controlling shareholder), beneficially owned approximately 69.63% of shares in the Company through China Netcom Group Corporation (BVI) Limited ("CNC BVI"); Shandong Provincial State-owned Assets Supervision and Administration Commission beneficially owned 2.24% of shares in the Company; each of Chinese Academy of Sciences Holdings Co., Ltd., Information and Network Center of the State Administration of Radio, Film and Television, China Railways Telecommunications Center and Shanghai Alliance Investment Limited beneficially owned 0.55% of shares in the Company; Telefónica Internacional, S.A.U. beneficially owned 5.00% of shares in the Company, and public investors owned 20.93% of shares in the Company. Chinese Academy of Sciences Holdings Co., Ltd., Information and Network Center of the State Administration of Radio, Film and Television, China Railways Telecommunications Center and Shanghai Alliance Investment Limited respectively signed a Share Purchase Agreement with Telefónica Internacional S.A. on January 18, 2008. Pursuant to the Share Purchase Agreements, the four shareholders will transfer the shares of the Company they beneficially own to Telefónica Internacional, S.A. or its related entities. Upon completion of the Share Purchase Agreements, Telefónica Internacional S.A. and its associates will be interested in approximately 7.22% of the issued share capital of the Company.

Company Profile and Corpoate Information

Registered office
Room 6701, The Center
99 Queen's Road Central
Hong Kong

Board of Directors

Mr. ZHANG Chunjiang	Chairman and Executive Director
Mr. ZUO Xunsheng	Executive Director and Chief Executive Officer
Ms. LI Jianguo	Executive Director
Mr. ZHANG Xiaotie	Executive Director
Mr. LI Fushen	Executive Director and Chief Financial Officer
Mr. YAN Yixun	Non-executive Director
Mr. Cesareo ALIERTA IZUEL	Non-executive Director
Mr. José María ÁLVAREZ-PALLETE	Non-executive Director
Mr. John Lawson THORNTON	Independent Non-executive Director
Mr. Victor CHA Mou Zing	Independent Non-executive Director
Dr. QIAN Yingyi	Independent Non-executive Director
Mr. HOU Ziqiang	Independent Non-executive Director
Mr. Timpson CHUNG Shui Ming	Independent Non-executive Director
Ms. Hong CHEN JIN	(alternate Director to Mr. Cesareo ALIERTA IZUEL and Mr. José María ÁLVAREZ-PALLETE)

Joint company secretaries
Mr. HUO Haifeng
Ms. MOK Kam Wan

Qualified accountant
Mr. LEUNG June Man HKICPA, AICPA

Auditors
PricewaterhouseCoopers

Legal advisers
As to Hong Kong Laws: Linklaters
As to U.S. Laws: Skadden, Arps, Slate, Meagher & Flom LLP

Investor Relations
Beijing Office
No. 21 Financial Street, Xicheng District
Beijing 100032, People's Republic of China
Telephone: 8610-66259550
Facsimile: 8610-66259544
E-mail: ir@cnc.cn
Website: www.china-netcom.com

Committees of the Board

Audit committee
Mr. Timpson CHUNG Shui Ming *Chairman*
Mr. Victor CHA Mou Zing
Dr. QIAN Yingyi
Mr. HOU Ziqiang

Compensation committee
Dr. QIAN Yingyi *Chairman*
Mr. ZHANG Xiaotie
Mr. LI Fushen
Mr. John Lawson THORNTON
Mr. Timpson CHUNG Shui Ming

Nominating and corporate governance committee
Mr. John Lawson THORNTON *Chairman*
Mr. ZHANG Chunjiang
Mr. ZUO Xunsheng
Mr. Victor CHA Mou Zing
Dr. QIAN Yingyi

Strategy committee
Mr. ZHANG Chunjiang *Chairman*
Mr. ZUO Xunsheng
Ms. LI Jianguo
Mr. LI Fushen
Mr. José María ÁLVAREZ-PALLETE
Dr. QIAN Yingyi
Mr. HOU Ziqiang

Supervision committee
Ms. LI Jianguo *Chairman*
Mr. ZHANG Xiaotie
Mr. Victor CHA Mou Zing
Mr. HOU Ziqiang
Mr. Timpson CHUNG Shui Ming

Stock code
Hong Kong Stock Exchange: 906
New York Stock Exchange: CN

Company Profile and Corpoate Information

Share registrar and transfer office

Computershare Hong Kong Investor Services Limited
Rooms 1712-1716,
17th Floor, Hopewell Centre
183 Queen's Road East
Wan Chai
Hong Kong

American depositary receipts depositary

Citibank, N.A.
388 Greenwich St., 14th Floor New York, NY10013, U.S.A.
Tel: 1-212-816-6671
Fax: 1-212-816-6865

Form 20-F

As required by the United States securities laws and regulations, the Company will file an annual report on Form 20-F with the United States Securities and Exchange Commission before June 30, 2008. The soft copy of Form 20-F will be available for viewing and download at: www.china-netcom.com once filed.

2007 Major Milestones

January

January 24, the Company and Xinhua News Agency entered into a full-scale cooperation framework agreement to cooperate in the development and applications of on-line video, value-added telecom services and other new media services.

January 25, China Netcom (Japan) Operations Corporation was incorporated in Japan.

February

February 4, the core network of China Next Generation Internet (CNGI), jointly built by China Netcom Group and other partners, was certified to have met the national standards.

February 26, China Netcom Group System Integration Limited Corporation was appointed by Beijing Organization Committee for the Games of the XXIX Olympiad (BOCOG) as the provider of data network facilities and services for the Olympic Games. The Company will offer the fullest range of fixed-line telecommunications services ever in the history of Olympic Games.

February 28, the Company disposed of its telecommunications assets, liabilities and business operations in Guangdong Province and Shanghai Municipality and would cease to provide services in these two regions.

March

March 1, the Company launched the website, www.shinecard.cn, where subscribers can store value to the shinecards and use other related services.

March, the Company started providing video search services for enterprises, CVNet, in some service regions of the Company.

April

April 6, the bundled service, "Family 1+", was promoted across all the service regions of the Company.

April 8, Mr. Li Fushen, Executive Director and Chief Financial Officer of the Company, was selected as "CFO of the Year in China 2006", on the 3rd CFO Summit Forum of China.

April 16, China Netcom Group entered into service procurement contracts with China State Council Informatization Office on network integration and vertical network service of the central-government-level information transmission backbone network.

April 19, the key project, "Research and Development and Industrialization of Crucial Technologies in IPv6-based next generation Internet (NGI)" of Beijing Municipal Science and Technology Commission (BMSTC), which was initiated by China Netcom (Group) Company Limited ("CNC China") was certified by BMSTC to have met required standards.

April 19, the website, www.cncmax.com, was awarded as one of the Top 10 Broadband Websites for 2007 during Broadband Video Service and Development Summit 2007 and the first Mobile Video Annual Assembly.

April 20, China Netcom Beijing Branch and Deutsche Presse Agentur (DPA) entered into the Agreement of International Circuit Transmission for 2008 Olympic Games, which was the first step for the Company to provide full-scale Olympic communications services to the overseas media operators.

2007 Major Milestones

May

May 8, the Company launched a proprietary instant messaging service "Lingxin", which was developed on PHS and Broadband.

May 30, the Company entered into the Letter of Intent for TV Broadcasting Communication Service with European Broadcasting Union (EBU) for the 29th Olympic Games. According to the letter of intent, the Company will provide international circuits in six directions connecting International broadcasting Centre (IBC) and the Europe during the Games. The TV signals will cover the entire European continent and its peripheral areas.

June

June 11, Qingdao Submarine Cable Landing Port of China Netcom Group was officially put into use. As the northernmost landing port in China, it cuts by half the transmission distance between Shanghai, Beijing and north Asia, including Japan and Korea. The landing port reduces substantially the possibility of network latency.

July

July 16, China Netcom Group entered into a Cooperation Agreement on ID Information Service with the Ministry of Public Security, marking a new form of cooperation between telecom carriers and the government in e-governance and e-commerce.

July 19, upon the approval of Ministry of Commerce, the Company was granted the right to operate advertisement business, according to which the Company was entitled to design, produce and release advertisements and act as an advertising agent for both domestic and foreign advertisers in the service areas of the Company.

July 25, China Netcom Group held a Broadband Olympic Product Release on the theme of "Olympics on Broadband, Beyond Your Dreams". The Company released 26 products in three series, respectively based on the themes of "Perfect Service", "Portable Information" and "Value Enhancement".

August

August 6, the Company entered into a Cooperation Agreement on Olympic TV Broadcasting with AT&T. The partners will jointly provide the international transmission of the Olympic TV signals to National Broadcasting Company (NBC) during the 2008 Olympic Games.

August 7, the Company established its Beijing Olympic Communication Office, which is to directly provide fixed-line communication services to 19 venues in the core area of the Olympic Games including the Technical Operation Center (TOC), the Main Press Centre and the stadiums.

August 8, the Olympic Call Center of the Company officially launched the call center for Good Luck Beijing test events, when Internet card "PBB", a broadband Olympic product targeting at media was released. It will provide flexible, convenient and high-speed Internet access to print media.

August 8, "CNC MAX" was promoted in full scale across the service regions of the Company.

August 15, China SecTrust Corporation Limited, a wholly-owned subsidiary of China Netcom Group, was incorporated, which will be engaged in certificate authority (CA) service and on-line information security service.

August 31, "Message Search", an SMS search service independently developed by the Company was launched, intended to provide integrated information search service.

September

September 24, the Company officially launched the website, http://house.cncmax.cn/ through "CNC MAX" to enable internet surfers to search for flats or apartments, which are showcased on video. It is the first of its kind in China to provide video clips about flats and apartments for rent or sale.

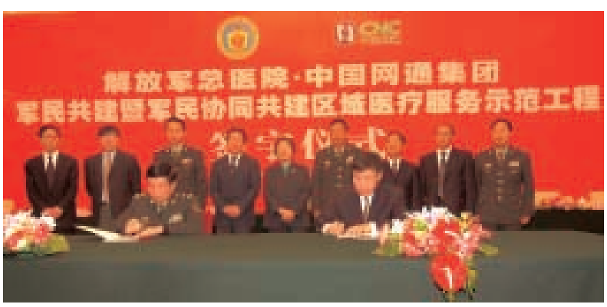
September 26, China Netcom Beijing Branch entered into a Cooperation Agreement on Olympic TV Broadcasting with Telstra to jointly provide the international transmission of the Olympic TV signals to Channel 7 in Australia in the 2008 Olympic Games.

October

October 10, China Netcom Group convened a Demo Conference of AVS-IPTV Commercial Trial Results and Possible Business in Dalian, demonstrating that the proprietary AVS technology of the national standard could achieve satisfactory results when applied in IPTV.

October 15, the Company launched a training product called "Interactive Oral-English", intended for the real-time English-speaking training on line.

October 30, China Netcom Group entered into a Cooperation Agreement on Jointly Building Medical Service Pilot Project with 301 Hospital in the Great Hall of the People.



November

November 1, the opening ceremony of China Netcom (Europe) Operations Limited was held in London.

November 15, China Netcom Group Broadband Online Limited Corporation, a subsidiary of the Company, was awarded the "Best Practice in Multimedia Education 2007" by China Computer Education Annual Meeting.

November 27, the Board of Directors of the Company was granted the "Directors of the Year Award 2007 of Hang Seng Index Constituents" by the Hong Kong Institute of Directors.

December

December 5, China Netcom Group System Integration Limited Corporation entered into the Equity Interest Transfer Agreement with China Netcom Group Beijing Communications Corporation to procure the entire equity interest of Beijing Telecommunications Planning and Designing Institute Corporation Limited. The Acquisition was completed on December 31, 2007.

December 14, China Netcom Group and China Academy of Telecommunication Research (CATR) of the Ministry of Information Industry (MII) jointly proposed establishing the Industrial Alliance of Interactive Media in Beijing, which consists of 18 domestic network operators, content providers, system and terminal manufacturers, chip providers and software and meter providers.

December, China Netcom Group was granted by the Ministry of Information Industry as an "Honored Enterprise in promoting the pilot scheme of promoting integrated information technology service in rural areas".

Financial Highlights

Hong Kong GAAP (RMB millions, except earnings per share)	2007	2006
Excluding amortisation of upfront connection fees		
Continuing operations:		
Revenues	**82,488**	81,788
Operating expenses	**66,739**	64,643
Deficit on revaluation of fixed assets	**—**	1,335
Profit for the year from continuing operations	**9,954**	9,072
CAPEX	**20,684**	24,560
Free cash flow (1)	**11,775**	7,490
Profi for the year from discontinued operations (2)	**624**	1,487
Profit for the year	**10,578**	10,559
Earnings per share from operations attributable to shareholders of the Company for the year	**RMB1.59**	RMB1.60
Earnings per ADS from operations attributable to shareholders of the Company for the year	**RMB31.8**	RMB32.0

(1) Free cash flow refers to net cash inflow from operating activities of continuing operations net of our capital expenditure.

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

Dear Shareholders,

Over the past three years, the Company has focused its efforts on strategic transformation and reform of operating principles. In 2007, I am delighted to report that we have made significant progress in this regard. We were able to strengthen and reinforce our new corporate identity as a broadband and multimedia service provider, paving the way for the Company's rapid growth in the future. We believe that the Company can sustain growth and create value for shareholders as long as it follows this long-term vision.

Strategic Transformation

In 2007, the revenue generated from innovative businesses maintained its growth momentum and grew by 38.9%, and accounted for 34.7% of the total revenue, up 9.5 percentage points compared with the same period last year.

China's Internet market continued to maintain a fast growth in 2007. According to China Internet Network Information Center, China added 73 million Internet users in 2007, reaching a total of 210 million by December 2007, up 53.3% from December 2006. The increasing use of Internet by all sectors of the public is accelerating and the number of younger, low-income and rural users also started to increase. People have become more reliant on Internet in their daily lives. Access to the Internet is increasingly regarded not as a luxury but a household necessity.

Capitalizing on the rapid growth of the Internet market, the Company launched its "Super Broadband Plan" to drive the growth of broadband services in two areas — broadband access, and broadband content and applications. In terms of broadband access, the number of broadband subscribers has been growing rapidly in the past three years. In 2007, the growth rate of broadband subscribers was 37%, which was 6.3 percentage points higher than that of the previous year.

In terms of broadband content and applications, the Company is delivering integrated content and applications directly onto the desktops of our broadband subscribers through its "CNC MAX". It is also running a pilot scheme of delivering broadband content and applications to other terminals such as TVs through technological innovation. In 2007, the Company began delivering smart terminals and HomeBox for home multimedia information to the users in some cities. The Company plans to deliver content and applications to user terminals of various types and offer quadruple-play multimedia and information services as it continues the execution of its strategic transformation into a broadband communications and multimedia services provider.

With the increase in our broadband subscribers and "CNC MAX" Client, and the growth in content and applications, the Company has begun to develop its advertising and media business. In 2007, through its services of "Phone Navigation", "CNC MAX" and "CNC Yellow Pages", the Company was exploring its competitive advantages in the area of advertising and media business.

During 2007, the Chinese government conducted a sweeping informatization drive. The aim is to raise efficiency in government, improve the competitiveness of enterprises, and upgrade living standards for the general public. The Company clearly recognizes the opportunities presented by government policy on informatization. To capture these, the Company has improved its ability to provide ICT solutions to government and corporate users, particularly at the high end of the ICT value chain. In 2007, the Company had built competitive advantage in providing integrated solutions for e-government, pollution monitoring, and "Safe City" etc.

Chairman's Statement

Olympic Opportunities

In 2007, the Company intensified marketing around its "Broadband Olympics" strategy, which is expected to drive substantial growth in both broadband and ICT services. The "Broadband Olympics" strategy is expected to deliver significant improvements to brand image, services, management, and overall competitiveness.

- High-speed networks: The Company launched a series of projects for the construction of high-speed optical networks. These include an optical network connecting all Olympic venues, the world's first ASON + MSTP network designed for the Olympics, and the first wide-area Centrex across the country.

- Easy network access: The Olympics will highlight the wide range of access modes offered by the Company, including LAN, EPON, McWill wireless access, and IC card certification access.

- Broadband products for the Olympic Games: These include the Olympic Yellow Pages, Broadband Olympic Content-Push, Portable USB key, and Multi-media broadband card. The Company will soon launch new products such as the "CNC MAX" Olympic Channel and Easy Broadband Cards in 2008.

- Comprehensive ICT solutions for the Olympics: Construction of an Olympic network monitoring system has been completed, and the Company has started offering Olympic call center services. The Company will complete a fixed-line communications command and control system, event management network system, and organization management system for the Olympic Games in 2008. Capitalizing on its Olympic partnership status, the Company has signed ICT contracts for security, transport and fire-fighting agencies associated with the Olympic Games.

- Higher service standards: CNC Olympic Services standards have been established and will be implemented in the Olympic cities.

Corporate Governance

In 2007, the Company continued to improve its corporate governance focused on its existing board governance structure.

After reviewing the performance of the board and the directors in the year 2006, the Company devised a plan to further enhance directors' understanding of the Company's operations through professional training. This includes a system to enable directors to exchange information and knowledge on a regular basis as well as receive timely information on operations, in order to help them make informed and scientific decisions on matters of significance to the Company. This system includes regular meetings between directors and the management, and monthly reports to directors.

In 2007, the Company launched new procedures for the selection and succession of senior executives, which will lead to a more open, transparent and systematic approach to appointment and succession of directors and senior executives.

Since 2004, the Company has won recognition from public and professional bodies for its persistent efforts in "establishing world-class corporate governance". In 2007, the Company received the prestigious "Directors of the Year Award 2007" from the Hong Kong Institute of Directors in the Hang Seng Index Constituents category. The award has strengthened the Company's confidence and commitment to achieving the highest standards of corporate governance.

Dividend

Based on the financial performance of the Company in 2007 and its development strategy, the Board of Directors has proposed the payment of a final dividend of HK$0.592 per share for the financial year ended December 31, 2007, up 7.1% compared with HK$0.553 per share in 2006.

Resignation and Appointment of Directors and the Management

On January 15, 2007, Ms. Li Liming resigned as Non-Executive Director of the Company and Mr. Li Fushen was appointed as Executive Director. On the same day, Mr. Zhang Changsheng resigned as Senior Vice President and Mr. Zhang Xiaotie was appointed as Senior Vice President. On July 12, 2007, Mr. Miao Jianhua resigned as Executive Director and Mr. Tian Suning resigned as Vice-Chairman and Non-Executive Director. On the same day, Ms. Li Jianguo was appointed as Executive Director. On December 5, 2007, Mr. Mauricio Sartorius resigned as Non-Executive Director and Mr. Cesareo Alierta Izuel was appointed as Non-Executive Director. On the same day, Ms. Hong Chen Jin (Margaret Chen), was appointed as Alternate Director to Mr. Cesareo Alierta Izuel and ceased serving as Alternate Director to Mr. Mauricio Sartorius. On the same day, Mr. Jiang Zhengxin was appointed as Vice President of the Company.

On behalf of the Board, I would like to extend my sincere thanks to Mr. Miao Jianhua, Mr. Tian Suning and Mr. Mauricio Sartorius for their outstanding contributions to the Company during their tenures as directors. I would also like to extend a warm welcome to Ms. Li Jianguo and Mr. Cesareo Alierta Izuel in joining the board of directors.

Looking into the Future

The telecommunications industry is undergoing rapid and profound changes. It is hard for the traditional operational model to keep up with the fast growth in demand and the quick pace of technological innovation. We firmly believe that the only way to sustain growth and enhance value for our shareholders is to deliver breakthrough innovation, embrace challenge proactively, and drive trends rather than following them.

In 2008, the Company will continue its strategic transformation into a broadband communications and multimedia service provider. For our public subscribers, we will leverage opportunities presented by the exponential growth of the Internet to attract more broadband access subscribers, strengthen the integration of content and applications, and deliver content and applications to user terminals via "CNC MAX" Client and HomeBox. The Company will expand its advertising and media business by optimizing its internal resources, which will generate new factors to drive sustainable growth.

The Company will promote ICT services for government and corporate customers and move to a higher position on the ICT value chain. The Company will leverage its advantages in terms of corporate resources and brand name to enter the outsourcing industry, which will help improve its competitive edge in ICT services and in becoming one of China's leading providers of ICT services.

The Company will persevere in the pursuit of licenses for mobile services and IPTV services which will pave the way for the Company to become a comprehensive "broadband communications and multimedia service provider".

Let me extend my sincere thanks to the shareholders, customers, employees and partners of the Company for their consistent support.

Zhang Chunjiang
Chairman

Hong Kong, March 25, 2008

Chief Executive Officer's Statement

Dear Shareholders,

In 2007, the Company focused on innovation and its strategic transformation into a broadband communications and multimedia services provider in respect of technologies, businesses and systems. Innovative businesses made up 34.7% of its revenue, up 9.5 percentage points compared to 2006. In a competitive environment where fixed-line voice services were increasingly substituted by mobile voice services, the successful development of innovative businesses has been crucial in offsetting the decline of traditional fixed-line voice services and has contributed to an increase in revenue. Through three years of hard work, the Company is gradually moving from a telecommunications services provider of traditional fixed-line voice services to a broadband communications and multimedia service provider.

1. Financial Results

As of the end of 2007, the Company generated RMB84,005 million in revenues from continuing operations, including amortization of upfront connection fees of RMB1,517 million. Excluding amortization of upfront connection fees, our revenue from continuing operations was RMB82,488 million, representing a year-on-year growth of 0.9% (unless otherwise specified, all reported data excludes the effect of amortization of upfront connection fees and discontinued operations). Consolidated net profit of the Company was RMB10,578 million, including net profit of RMB624 million generated from discontinued operations.

In 2007, capital expenditure was RMB20,684 million, representing a decline of 15.8% from last year and a reduction of RMB316 million compared to the guidance provided by the senior management at the beginning of the year. Benefiting from the effective management of cash flow and capital expenditure, our free cash flow in 2007 was RMB11,775 million, representing a growth of 57.2%.

2. Business Review

In 2007, the substitution of fixed-line voice services by mobile voice services accelerated. Mobile telecommunications operators accounted for 90.3% of the net increase in the revenue of the telecommunications industry. In a fiercely competitive market, the Company continued to implement its strategy of becoming a broadband communications and multimedia service provider. Operationally, it has adopted strategies to expand innovative businesses, stabilize fixed-line voice businesses, push ahead management reforms and improve free cash flow. Our strategy has proved to be effective.

Innovative Businesses

In 2007, innovative businesses contributed RMB28,656 million to revenue, representing a growth of 38.9%.

During the year, the Company launched a "Super Broadband Plan" to take advantage of growth opportunities presented by the rapid expansion of the Internet market in China. Within our service regions, we increased broadband access speed, put new operational and business models into practice, and promoted our Olympic ties and strategy. By the end of 2007, the total number of broadband subscribers of the Company increased 5,339 thousand to 19,768 thousand, representing a growth of 37.0% compared with the same period of last year and a market share of 88.9%.

Along with the expansion of its broadband subscriber base, the Company focused on integrating broadband content and applications and innovating development model. "CNC MAX" Client was launched to deliver enriched content and applications directly to the desktops of our subscribers. New user terminals, ranging from PCs to TV sets enriched the means of access for customers. Broadband services generated a total revenue of RMB13,835 million in 2007, and ARPU was RMB67.4. In particular, revenue from broadband content and applications business was RMB1,749 million, up 107.7% from the previous year, and contributed RMB8.5 to the average revenue per broadband subscriber.

In 2007, with the expanding "CNC MAX" Client user base and enrichment of content and applications, the Company began to develop its advertising and media business. In 2007, based on "Phone Navigation", "CNC MAX" and "CNC Yellow Pages", the Company explored its competitive advantage in the area of advertising and media. By the end of the year advertising and media business had generated revenue of RMB380 million.

With the increasing penetration of IT across all sectors of society, the fast pace of technological change and increasing network integration, the traditional boundaries among communications networks, the Internet, and corporate intranets have been diminishing and this has led to the development of an integrated ICT industry. The Company has established a long-term goal of becoming one of China's leading ICT service providers, as well as a network information specialist for government and corporate customers by leveraging its brand and resources. In 2007, the Company made great efforts to develop ICT services in order to enhance its position in providing integrated solutions for key customers and markets, as well as enhance its ability to provide higher-value added services.

In 2007, the Company seized the opportunities presented by the Chinese government's initiative to promote information technology in administrative affairs, and secured a number of significant integrated IT projects. It has built up its key competitive advantages in providing integrated solutions for government, Olympics, health, education, finance and other industries. For instance, the Company developed business relationships with important customers such as the State Council Informatization Office, the National People's Congress, the Ministry of Commerce, China International E-commerce Center and the Chinese Academy of Medical Sciences. It has also improved its capabilities on research and development and project management. At the end of 2007, the Company acquired Beijing Telecommunications Planning and Designing Institute Corporation Limited. The acquisition has brought stronger technical qualifications, broader customer relationships and a greater number of professionals to the Company. These will strengthen the Company's capabilities to deliver ICT services and accelerate the Company's shift towards the high end of the ICT value chain. In 2007, the Company generated RMB3,990 million in its ICT business, representing a growth of 366.7%.

In 2007, the Company focused on expanding the scope of value-added services and increasing the penetration rate of value-added services for its fixed-line subscribers. By the end of 2007, revenue from value-added services had increased by 14.5% to RMB6,114 million, accounting for 7.4% of total revenue, an increase of 0.9 percentage points from 2006. The number of Personalized Ring subscribers was 28,137 thousand, representing a growth of 78.6%. Of this number, 19,970 thousand used fixed-line Personalized Ring, representing a growth of 124.1% and a penetration rate of 23.6%. The penetration rate of Caller Identification Service was 72.2%, an increase of 3.4 percentage points.

Traditional Fixed-line Voice Services

In 2007, in the field of traditional fixed line services, the Company continued to promote bundled services and integrated services under the brand names "Family 1+" and, "Same Number", driving the growth of innovative businesses by bundling various services in one package. By the end of 2007, the number of "Family 1+" subscribers reached 8,378 thousand, representing a growth of 650.7% over the previous year. The "Same Number" subscriber base had grown to 1,663 thousand, an increase of 75.7%. Fast growth of the "Family 1+" service supported development of broadband access, broadband content and applications as well as value-added services. In 2007, more than 80% of the net growth in the broadband subscribers of the Company also subscribed to "Family 1+".

Due to the increasingly rapid mobile substitution, the number of our local telephone subscribers declined. By the end of 2007, the number had decreased by 3,152 thousand to 110,820 thousand, of which PHS subscribers numbered 26,189 thousand, a drop of 4.1% compared with the previous year. The ARPU and traffic for local telephone services continued to fall.

We believe that with the growing penetration of the "Family 1+" service plan, the steady improvement of its pricing system and shift of the service plan positioning to home multimedia information service, the value of the fixed-line telephone services customer will be maximized.

3. Management Reforms

Strategic transformation is leading the Company into new businesses such as multimedia and IT services, where we are facing new operational models and new competitors different from those in the traditional fixed-line voice services. The only way to develop core competitiveness in new business areas and meet customers' constantly changing needs is to introduce ground-breaking changes to our management model.

Changes in Organizational Structure

In 2007, the Company conducted a customer-oriented marketing system reform as a starting point for changes to its organizational structure. Specialized marketing teams were organized under three customer categories - Large Corporates and Government, Small and Medium Enterprises, and Residentials. The changes were made in order to improve customer satisfaction, allocate resources more efficiently, and shift focus from marketing product to customizing product.

Changes in Financial Management

Strategic transformation is also leading changes in financial management, which has shifted focus from volume processing of transactions to decision-making support and value creation. With a shared financial system, standard legal and management reports as well as transaction processing are outsourced to a financial sharing center. Standardized and process-based outsourced management can greatly improve financial efficiency and drive down costs. The quality of accounting and risk control management can also be improved. More importantly, financial managers can be freed from basic transaction activities and can devote more time to providing support for strategic decision-making and value creation.

In 2007, the Company established the "CNC Financial Service Sharing Center", to share accounting, payment and revenue management processes among headquarters and subsidiaries.

4. Development Strategies for 2008

In 2008, the Company will focus on the following aspects of its development strategies:

- Implementing the "Super Broadband Plan" to increase broadband access speed and diversify broadband access modes and terminals;
- Developing broadband content and applications in order to increase the market penetration rate of "CNC MAX" Client, and to deliver broadband content and applications to as many user terminals as possible through technological innovation with an aim of increasing revenue contribution from the business of broadband content and applications, as well as advertising and media services;
- Integrating available resources to develop advertising and media businesses based on phone search engine, Internet advertising and Yellow Pages;
- Optimizing "Family 1+" bundled services and gradually shift its positioning to satisfy residential customers' needs for broadband and multimedia information services;
- Promoting ICT services in order to enhance our capabilities to deliver high-value added ICT services as well as strengthen our competitive edge in core industries and areas.
- Developing ICT services to outsourcing business with a focus on call center and IDC areas, where the Company has competitive advantages in terms of resources.
- Expanding the customer-oriented marketing system reform, with pilot projects in a number of provinces. The ultimate goal is to promote the system throughout our service regions by the end of 2008. We will also further develop the financial sharing system, and conduct trials in provincial branches.

In 2008, with a focus on innovation, we will seize the historic opportunity of the Beijing 2008 Olympic Games to speed up the Company's strategic transformation into a broadband communications and multimedia service provider.

I would like to take this opportunity to express my gratitude to our customers, shareholders, the board of directors and the staff for their support and trust.

ZUO Xunsheng
Chief Executive Officer

Hong Kong, March 25, 2008


国家体育场座位9.1万个
中国网通让40亿人与现场0距离
第一届真正的宽带奥运会

Profile of Directors and Senior Management

Directors

Zhang Chunjiang, 49, Chairman and Executive Director, has served as a Director since June 2004. He has been the Chairman of China Netcom (Group) Company Limited since September 2004 and President of China Netcom Group since May 2003. He has served as a Non-executive Director of PCCW Limited (listed on the Hong Kong Stock Exchange with an American Depositary Receipt trading on the Pink Sheets' OTC Market in U.S.) since April 2005. Prior to joining China Netcom Group, Mr. Zhang served as Deputy Minister of the Ministry of Information Industry (MII) and was one of the most senior regulatory officials in the PRC telecommunications industry from December 1999 to May 2003. From August 1993 to December 1999, Mr. Zhang held a series of senior-level positions at the former Liaoning Provincial Posts and Telecommunications Bureau, the former Ministry of Posts and Telecommunications (MPT), and the MII, including serving as the Deputy Director of the former Liaoning Provincial Posts and Telecommunications Bureau, Director of Mobile Telecommunications Administration of the MPT and Director of Telecommunications Administration of the MII. Mr. Zhang is a senior engineer of professor level and has extensive experience in telecommunications management, operations and technology. Mr. Zhang graduated from the Beijing University of Posts and Telecommunications in 1982 with a bachelor's degree in telecommunications.

Zuo Xunsheng, 57, Executive Director and Chief Executive Officer, has served as Executive Director and Chief Executive Officer since May 2006, and served as Chief Operating Officer of the Company from December 2005 to May 2006 overseeing general operations of the Company. Mr. Zuo has served as Senior Vice President since July 2004. He has also served as Vice President of China Netcom Group since April 2002. He has served as a Non-executive Director and Deputy Chairman of PCCW Limited (listed on the Hong Kong Stock Exchange with an American Depositary Receipt trading on the Pink Sheets' OTC Market in U.S.) since July 2007. Before joining China Netcom Group, Mr. Zuo was President of the former Shandong Telecommunications Company from May 2000 to April 2002. From October 1997 to May 2000, Mr. Zuo has served as Director of the former Posts and Telecommunications Bureau of Shandong Province. From 1993 to 1997, Mr. Zuo has served as Director of the former Bureau of Telecommunications of Jinan City. Mr. Zuo graduated from Guanghua School of Management of Peking University with an EMBA degree.

Li Jianguo, 54, Executive Director, has served as Executive Director since July 2007 and served as senior management officer of China Netcom Group since July 2007. Before joining China Netcom Group, Ms. Li held a series of senior-level positions at China United Telecommunications Corporation, including serving as a director and chairperson of the trade union, and served as the Chairperson of the board of supervisors of China United Telecommunications Corporation Limited (listed on the Shanghai Stock Exchange) and Executive Director of China Unicom Limited (listed on the New York Stock Exchange and the Hong Kong Stock Exchange). Ms. Li held leading positions in various enterprises, local governments and state ministries and committees for a significant period of time, and she has extensive experience in working for the government and enterprises and in management. Ms. Li graduated from the Xiangtan University with a bachelor's degree in Chemical Engineering in 1982 and received a master's degree in business administration from the Hong Kong Polytechnic University.

Zhang Xiaotie, 55, Executive Director and Senior Vice President, has served as a Director since

October 2004 and Senior Vice President since January 2007 overseeing procurement and logistics management. He served as the Joint Company Secretary from October 2004 to December 2005. He also has served as Vice President of China Netcom Group since July 2003. From June 2002 to July 2003, Mr. Zhang also served as Assistant to President and General Manager of Planning and Finance Department of China Netcom Group. Before joining China Netcom Group, Mr. Zhang served as Deputy Director and Director of Economic Planning and Communication Settlement Department of MII. He also held a series of senior-level positions at the former MPT and former Beijing Administration of Telecommunications. Mr. Zhang graduated from the School of Economics and Management of Tsinghua University with an M.S. degree.

Li Fushen, 45, Executive Director and Chief Financial Officer, has served as executive director since January 2007, and has served as Chief Financial Officer since September 2005. He served as Joint Company Secretary from December 2006 to March 2008. He served as Financial Controller from July 2004 to August 2005. Since October 2005, he has served as the Chief Accountant of China Netcom Group. He has served as a Non-executive Director of PCCW Limited (listed on the Hong Kong Stock Exchange with an American Depositary Receipt trading on the Pink Sheets' OTC Market in the U.S.) since July 2007. From October 2003 to August 2005, he served as General Manager of the Finance Department of China Netcom Group. From November 2001 to October 2003, he served as Deputy General Manager of Jilin Communications Company and Deputy General Manager of the former Jilin Provincial Telecommunications Company. He graduated from the Australian National University with a master's degree in management, and from the Jilin Engineering Institute with a degree in engineering management in 1988.

Yan Yixun, 69, Non-executive Director, has served as a Director since 2001. He was a member of the Standing Committee of the Eighth, Ninth and Tenth National People's Congress. He was the Vice Chairman of the Financial and Economic Committee of the Tenth National People's Congress and a member of the Education, Science, Culture and Health Committee of the Ninth National People's Congress. From December 1992 to November 2000, he served as Vice Chairman of the Chinese Academy of Sciences, and prior to that he served as Director of Shanghai Technical Physics Research Institute. He was a first-term Board Director of Legend Holdings Limited and now serves as Chairman of the Board of New Margin Venture Capital Co., Ltd. and Director of Chinese Academy Sciences Holdings Co., Ltd.. Mr. Yan received a master's degree from the Institute of Electronics of the Chinese Academy of Sciences in 1966 and graduated from the Department of Radio Electronics at Tsinghua University in 1962.

Cesareo Alierta Izuel, 62, Non-executive Director, has served as a Director since December 2007.

Profile of Directors and Senior Management

He has been director of Telefónica S.A. (listed on various stock exchanges including Madrid, New York and London) as from January 1997, member of its Executive Committee since January 1999, and has become the Executive Chairman of Telefónica S.A. since July 2000. Mr. Cesareo Alierta Izuel is a member of the Colombia Business School Board of Overseers. He is also a director of Telecom Italia (listed on the stock exchange of Milan). He was a member of the Board of Directors of Telefónica O2 Europe, Plc from January 2006 to January 2008. Between 1970 and 1985, he has been the General Manager of the Capital Markets division at Banco Urquijo in Madrid. He has been the Chairman and founder of Beta Capital. As from 1991, he has also acted as the Chairman of the Spanish Financial Analysts' Association. He has also been a member of the Board of Directors and the Standing Committee of the Madrid Stock Exchange. Between June 1996 and November 1999, he was Director and Chairman of Tabacalera, S.A.. At that time Tabacalera, S.A. changed its name into Altadis, S.A. (following the merger of Tabacalera, S.A. with the French Group, Seita) and he became Director and Chairman of Altadis, S.A.. He was the Chairman of Altadis, S.A. until July 2000, but he continued as a member of the Board of Directors and Executive Committee of Altadis S.A. until February 2008. Mr. Cesareo Alierta Izuel holds a degree in law from the University of Zaragoza and a master's degree of business administration from the University of Columbia.

José María Álvarez-Pallete, 44, Non-executive Director, has served as a Director since September 2005. He joined Telefónica Internacional S.A. in February 1999 as General Manager for Finance. In September of the same year, he became Chief Financial Officer of Telefónica, S.A.. In July 2002, he was appointed as Executive Chairman of Telefónica Internacional, S.A.. In July 2006, he was appointed as General Manager of Telefónica Latinoamérica and a member of the Board of Telefónica, S.A. (listed on various Stock Exchanges including Madrid, New York and London). In addition, Mr. Álvarez-Pallete is a Director on the boards of Telecomunicaciones de Sao Paulo, S.A. (listed on the Stock Exchanges of Sao Paulo and New York), Compañía de Telecomunicaciones de Chile, S.A. (listed on the Stock Exchanges of Santiago de Chile and New York), Telefónica de España S.A., Telefónica Móviles España S.A., Telefónica Datacorp, S.A., Telefónica de Argentina, S.A. (listed on the Stock Exchanges of Buenos Aires and New York), Telefónica de Perú S.A.A. (listed on the Stock Exchange of Lima), Colombia Telecomunicaciones, S.A. ESP, Telefónica Móviles Colombia, S.A., Telefónica Móviles México, S.A., Brasilcel, N.V., Allianca Atlantica Holding B.V. and Telefónica O2 Europe, plc. Mr. Álvarez-Pallete received a bachelor's degree in economics from the Universidad Complutense of Madrid.

John Lawson Thornton, 54, Independent Non-executive Director, has served as a Director since

October 2004. Mr. Thornton is Professor and Director of Global Leadership Project at Tsinghua University in Beijing. He was President and a Director of The Goldman Sachs Group, Inc. until July 2003. Mr. Thornton is a Director of Ford Motor Company (listed on the New York Stock Exchange), Industrial and Commercial Bank of China Ltd. (listed on the Shanghai Stock Exchange and the Hong Kong Stock Exchange), Intel Corporation (listed on NASDAQ Stock Exchange) and News Corporation, Inc. (listed on the New York Stock Exchange and the Australian Stock Exchange). He is also Chairman of the Brookings Institution Board of Trustees. Mr. Thornton received an A.B. in history from Harvard College in 1976, a B.A. and M.A. in jurisprudence from Oxford University in 1978 and a M.P.P.M. from the Yale School of Management in 1980.

Victor Cha Mou Zing, 58, Independent Non-executive Director, has served as a Director since October 2004. Mr. Cha is the Deputy Chairman and the Managing Director of HKR International Limited, Alternate Independent Non-executive Director of New World Development Company Limited and Independent Non-executive Director of SOHO China Limited (all above companies being listed on the Hong Kong Stock Exchange). He is also a member of the Chinese People's Political Consultative Committee of Zhejiang Province and a council member of the Hong Kong Polytechnic University. Mr. Cha graduated from Stanford University with a MBA degree and University of Wisconsin with a B.S. degree.

Dr. Qian Yingyi, 51, Independent Non-executive Director, has served as a Director since October 2004. He is a Professor of Economics at the University of California, Berkeley. Since 2006, Dr. Qian has been the Dean of the School of Economics and Management at Tsinghua University. Dr. Qian has served as Independent Director of the Industrial and Commercial Bank of China Ltd. (listed on the Shanghai Stock Exchange and the Hong Kong Stock Exchange) as from 2005, Independent Director of Vimicro International Corporation (listed on New York NASDAQ) as from 2006, and the Chairman of the Supervisory Board of Vtion Wireless Technology AG as from 2007. Before joining the Berkeley faculty in 2001, Dr. Qian has taught in the Department of Economics at Stanford University and the University of Maryland. In 1990, Dr. Qian received his Ph.D. in Economics from Harvard University, after receiving an M.Phil. in management science/operations research from Yale University and an M.A. in statistics from Columbia University. In 1981, Dr. Qian graduated from Tsinghua University with a B.S. degree in mathematics.

Hou Ziqiang, 70, Independent Non-executive Director, has served as a Director since October

Profile of Directors and Senior Management

2004. Since March 2005, Mr. Hou has served as Independent Non-Executive Director of the Varitronix International Limited (listed on the Hong Kong Stock Exchange). Mr. Hou founded China Kejian Company Limited in 1984 and has also been its Chairman. From 1993 to 1997, Mr. Hou was Director of the Institute of Acoustics of the Chinese Academy of Sciences. From 1988 to 1993, Mr. Hou was Secretary General of the Chinese Academy of Sciences. Mr. Hou graduated from Peking University in 1958 with a bachelor's degree in physics.

Timpson Chung Shui Ming, 56, G.B.S., J.P., Independent Non-executive Director, has served as a Director since October 2004. He is a fellow member of the Hong Kong Institute of Certified Public Accountants and the Association of Chartered Certified Accountants. He is a Independent Non-executive Director of Tai Shing International (Holdings) Limited, Glorious Sun Enterprises Limited, The Miramar Hotel & Investment Co. Limited and Nine Dragons Paper (Holdings) Limited (four companies being listed on the Hong Kong Stock Exchange). In addition, Mr. Chung is a member of the National Committee of the 11th Chinese People's Political Consultative Conference and the Chairman of the Council of the City University of Hong Kong. Formerly, he was a member of the National Committee of the 10th Chinese People's Political Consultative Conference, an Executive Director of Hantec Investment Holdings Limited and an Executive Director of Shimao China Holdings Limited. He was also Chairman of the Hong Kong Housing Society, a member of the Executive Council of the Hong Kong Special Administrative Region, the Vice Chairman of the Hong Kong Special Administrative Region Government Land Fund Advisory Committee, a member of the Hong Kong Housing Authority, a member of the Managing Board of the Kowloon-Canton Railway Corporation and a member of the Disaster Relief Fund Advisory Committee. Mr. Chung holds a bachelor of science degree from the University of Hong Kong and a master's degree of business administration from the Chinese University of Hong Kong.

Ms. Hong Chen Jin (Margaret Chen), 45, Alternate Director to Mr. Cesareo Alierta Izuel and Mr. José María Álvarez-Pallete, served as an Alternate Director of Mr. Cesareo Alierta Izuel since December 2007 and an Alternate Director of Mr. José María Álvarez-Pallete since December 2006. She served as an Alternate Director of Mr. Mauricio Sartorius who was previously a non-executive director of the Company, from December 2006 to December 2007. Ms. Hong Chen Jin began her career in China as faculty member of the Management School of Shanghai Jiaotong University. She has worked in the United States of America for seven years. Among others, she worked as a Vice President of research and development in ACS, a software development company. Prior to joining Telefónica as a telecom senior consultant in 1995, she was a partner of INDETEL, a telecom consulting company in Spain. During the ten years in Telefónica Group prior to her Asia assignment, she has profound operational experience in fixed-line and mobile business including IT strategy, marketing and sales. In 2005, she was assigned as Director, Asia, Telefónica Internacional S.A. At the beginning of 2007, Ms. Hong Chen Jin was awarded as one of the most influential women in telecommunications industry in China for the year of 2006 by the Ministry of Information Industry of China. Ms. Hong Chen Jin has been a director of China Netcom Group Broadband Service Applications Limited Corporation For National Engineering Laboratory as from August 2007. Ms. Hong Chen Jin holds a bachelor's degree in computer science of Shanghai Jiaotong University and a master's degree of business administration, and a master's degree in Industrial Engineering in the United States of America.

Joint Company Secretaries and Qualified Accountant

Huo Haifeng, 43, Joint Company Secretary and Vice President, has served as the Vice President of the Company from December 2006 and is currently in charge of risk management and legal affairs of the Company. Mr. Huo was the General Manager of Tianjin Communications Company from August 2004 to November 2006 and served as the General Manager of Dalian Branch of Liaoning Communications Company from December 2002 to August 2004. Mr. Huo was the General Manager of Dalian Branch of Liaoning Telecommunications Company of former China Telecom Group from April 2001 to December 2002. He worked as the General Manager of Anshan Branch of Liaoning Telecommunications Company from August 2000 to April 2001. Mr. Huo served as Director of Bureau of Telecommunications Administration in Anshan city of Liaoning Province from October 1998 to August 2000. Mr. Huo graduated from Changchun University of Posts and Telecommunications on the major of computer application in July 1987, and from Beijing University of Posts and Telecommunications Graduate School in August 1998, and obtained a master's degree of business management from Australian National University in October 2002.

Mok Kam Wan, 45, Joint Company Secretary. Ms. Mok joined the Company in October 2005. She holds a bachelor's degree of laws from the University of London and a master's degree in business administration from The Hong Kong Polytechnic University. Ms. Mok is an associate member of The Institute of Chartered Secretaries and Administrators in the United Kingdom and The Hong Kong Institute of Chartered Secretaries.

Leung June Man, 38, Assistant to the Chief Financial Officer and Qualified Accountant. Mr. Leung has joined the Company since June 2005. He graduated from Washington State University in 1992 with a bachelor's degree in business administration, major in accounting. Mr. Leung is a member of both of Hong Kong Institute of Certified Public Accountants and American Institute of Certified Public Accountants.

Senior Management Officers

Profile of Directors and Senior Management

Zuo Xunsheng, Executive Director and Chief Executive Officer.

Pei Aihua, 57, Senior Vice President, has served as Senior Vice President since July 2004 overseeing corporate development, mobile communications and administration. He has also served as Vice President of China Netcom Group since April 2002. Before joining China Netcom Group, he was Deputy General Manager of the former Beijing Telecommunications Company from July 2001 to April 2002, General Manager of Sichuan Provincial Telecommunications Company from July 2000 to July 2001, and Deputy Director of the former China General Bureau of Posts and Telecommunications from June 1997 to May 2000. Mr. Pei is a senior engineer of professor level. He graduated with a master's degree in information and communication management jointly sponsored by the Management School of Fudan University and the Norway Management School in 2001. He graduated from Changchun Optical Precision Machinery College with a master's degree in electrical engineering in 1993 and Beijing School of Telecommunications in microwave technology in 1976.

Zhao Jidong, 57, Senior Vice President, has served as Senior Vice President since July 2004, and is responsible for Olympics communications, international affairs and Beijing Municipal Branch Company. He has also served as Vice President of China Netcom Group since July 2003. Before joining China Netcom Group, Mr. Zhao served as General Manager of Beijing Communications Company from July 2002 to July 2003, and General Manager of the former Beijing Telecommunications Company from May 2000 to July 2002. From November 1994 to May 2000, Mr. Zhao served as the Deputy Director and Director of the former Beijing Telecommunications Bureau. Mr. Zhao graduated with a master's degree in information and communication management jointly sponsored by the Management School of Fudan University and the Norway Management School, and from Fudan University with a B.A. degree in English in 1975.

Zhang Xiaotie, Executive Director and Senior Vice President

Li Fushen, Executive Director and Chief Financial Officer

Jiang Zhengxin, 51, Vice President, has served as the Vice President since December 2007, in

charge of marketing and major account management, and served as Vice President of China Netcom Group since September 2007. He was the General Manager of Zhejiang Branch of China Netcom Group from June 2004 to September 2007 and served as the deputy general manager of South Communications Co. Ltd of China Netcom Group from March 2004 to June 2004. Before joining China Netcom Group, Mr. Jiang was the deputy general manager of Jilin Mobile Communications Company from July 1999 to March 2004. Mr. Jiang served as deputy director of Bureau of Telecommunications Administration in Changchun of Jilin Province from February 1998 to July 1999. Mr. Jiang is a senior engineer of professor level with the degree of PHD of political economy from Jilin University, and he obtained a master's degree of Radio engineering from Beijing University of Posts and Telecommunications in 1982.

Teng Yong, 53, Chief Technical Officer, has served as Chief Technical Officer since August 2006, responsible for technical issues and ICT applications. He served as the General Manager of Hebei Communications Company from July 2004 to April 2006 and the General Manager of Tianjin Communications Company from July 2002 to July 2004. Mr. Teng held the position of General Manager of Tianjin Telecommunications Company from May 2000 to July 2002 and the Deputy Director and later Director of the Posts and Telecommunications Administration of Tianjin from May 1995 to May 2000. Mr. Teng graduated from Nanjing University of Posts and Telecommunications with a major in automatic telephone switching in February 1980, and later obtained a doctor degree of management and engineering from Tianjin University.

Zhu Lijun, 54, Vice President, has served as Vice President since December 2006, responsible for network operation and consumer rights protection. Since March 2005 , he has served as Assistant to the President of China Netcom Group, and served as General Manager of Department of Planning and Construction starting from July 2004. He was the General Manager of Shanxi Communications Company from August 2002 to July 2004. He was the General Manager of Shanxi Telecommunications Company from December 2001 to August 2002. He worked as the General Manager of Telecommunications Company of Guangxi Zhuang Autonomous Region from July 2000 to December 2001, and served as the Deputy Director of the Posts and Telecommunications Administration of Neimenggu Autonomous Region from August 1996 to July 2000. Mr. Zhu graduated from the Department of Chinese Language and Literature of Inner Mongolia Normal University in 1986, and later obtained a master's degree of international business management from Australian National University.

Huo Haifeng, Joint Company Secretary and Vice President.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The Company is deeply aware of the significance of corporate governance in achieving effective checks and balance and protecting the interests of all shareholders, and is dedicated to pursuing sustained optimisation of corporate governance. The Company regards the building of sound corporate governance as an important means to maintain shareholder relationship and enhance corporate value. The Company is convinced that sound corporate governance is of great importance to the sustainable long-term growth of the Company and that the efforts to improve and optimise our corporate governance and the progress that have been made to this end will help in enhancing our core competitiveness and increasing corporate value.

In 2007, the Company maintained the current sound structure of the Board with five committees under the Board, namely, the Audit Committee, the Compensation Committee, the Nominating and Corporate Governance Committee, the Strategy Committee and the Supervision Committee. The composition and assignment of duties of the Board committees have strictly complied with the provisions in the Code on Corporate Governance Practices. Such arrangement will enable the Directors to make full use of their expertise and experience, enhance their ability to fulfil their duties and improve their performance. In 2007, the Company also implemented the assessment on the annual performance of the Board and the Directors. On the basis of in-depth discussions and analysis of the assessment results and for the purpose of protecting the interests of all shareholders, improving efficiency in decision-making, and rationalizing the exercise of the functions of the Directors, the Company made constant efforts to improve and optimise the mechanisms, systems and processes relating to corporate governance including the "Articles of Association", "Guidelines for Directors", "Guidelines for the Board of Directors", "Procedural Rules for the Board of Directors and Board Committees". The related optimisation work clearly identified the division of responsibilities between the Board and the management of the Company, improved the work efficiency of the Board, and strengthened the ethical requirements on the Directors. In 2007, the Company strengthened training for the Directors to improve their expertise, deepen their understanding of the technologies and businesses of the Company, and make the decision-making of the Board more scientific. Our efforts laid a solid foundation for the improvement of corporate governance. In 2007, the Company conducted five training sessions for the directors covering telecommunications technologies, international accounting standards, corporate governance theories, information and communications services and the disclosure requirements of the Listing Rules.

Throughout 2007, the Company has fully complied with the relevant code provisions set out in the "Code on Corporate Governance Practices", Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("the Listing Rules").

In 2007, the Board of the Company received the "Directors of the Year Award 2007" from the Hong Kong Institute of Directors in the category "Hang Seng Index Constituent Stocks". The winning of this award proves that the Company was widely recognized by the market and professional agencies for its learning and drawing on the advanced corporate governance experience of international companies and building up a world-class corporate governance structure. The winning of this award also strengthened the determination and confidence of the Company in achieving outstanding corporate governance.

In 2008, the optimisation work will focus on senior-level human resource management, risk management and strategy management. The Board will take effective measures to tap the potentials of the Company, strengthen the supervision on the implementation of corporate strategies, and achieve the sustained and healthy growth of the Company.

Corporate Governance

The Board

Adhering to the international corporate governance best practices, the Company pays high regard to the independence of the Board and has been adhering to the principles that non-executive directors shall be the majority in the Board so as to ensure the decisions of the Board are in line with the best interests of shareholders. The Board comprises of thirteen Directors, including five independent non-executive Directors, three non-executive Directors and five executive Directors. Members of the Board are professionals from the telecommunications, finance, property development and consultancy industries and economists. The diversified expertise and rich industry experiences of the Directors are the valuable assets of the Company. By virtue of their in-depth understanding of our technologies and businesses, in 2007, the Directors contributed significantly to the implementation of our strategies and the management and control of operational risks.

The responsibility of the Board is to lead and supervise the Company in the conduct of its affairs and to protect interests of shareholders and the Company as a whole. It exercises its powers pursuant to our Articles of Association, the relevant laws, regulations and regulatory requirements; it is responsible for convening shareholders' general meetings and executing the resolutions of the general meetings; it is responsible for supervising and controlling the governance structure and rules, defining our medium and long-term development strategies and approving our annual strategic development plans, budgets and targets, capital expenditure and investment plans, supervising the effectiveness of our internal control system and regulatory compliance of our operations, formulating a management succession system, managing the performance of the management of the Company, and exercising the functions required by other applicable laws, regulations and regulatory provisions. The Board delegates day-to-day management of the Company's business and administration to the management and may make rational adjustment to the scope of authorization on a regular basis according to the actual operations of the Company.

The Board routinely meets four times each year and special Board meeting may be convened as and when required. All members of the Board have full and timely access to relevant information for meetings in advance. The proposed Board and Board committee meeting schedules for a fiscal year are agreed and determined at the preceding fiscal year's Board meetings. During this reporting period, the Board held seven meetings.

During this reporting period, the Board at all time complied with the requirements of the Listing Rules relating to the appointment of at least three independent non-executive Directors, and complied with the requirements that at least one of the independent non-executive Directors must have appropriate accounting or related financial management professional qualifications.

Biographies of the Chairman, Executive Directors, Non-Executive Directors and Independent Non-Executive Directors are set out on pages 16 to 23 of this annual report.

Chairman and Chief Executive Officer

The positions of Chairman and Chief Executive Officer are held by Mr. Zhang Chunjiang and Mr. Zuo Xunsheng respectively. The Company believes that such arrangement is in line with the best corporate governance practice and will help maintaining the independence of the Board and increasing the supervision on the management. The Chairman is mainly responsible for convening and chairing meetings of the Board, as well as leading the Board in performing its functions in corporate governance, strategy management, human resources management, risk management and other related areas. The Chief Executive Officer is responsible for the operations of the Company and accountable to the Board. Both the Chairman and Chief Executive Officer of the Company have extensive experience in the telecommunications sector. The Company is confident that their expertise and experience will be beneficial for the enhancement of the Company's performance.

Independent Non-Executive Directors

In 2007, the Independent Non-Executive Directors participated in the decision-making of the Board in an earnest manner, abided by professional ethics, and demonstrated their due independence. They arrived at a better understanding of the industry environment, technologies, services and operations of the Company through active participation in training, seminars and studies. They made valuable contributions to the Company in many aspects such as corporate governance, senior-level human resources management and strategy development and planning. In 2006, our management proposed the disposal of the Company's telecommunications assets, liabilities and operations in Guangdong Province and Shanghai Municipality. In accordance with the requirements of the Listing Rules, the Board established an independent board committee, which comprised all Independent Non-Executive Directors and chaired by Mr. Timpson Chung Shui Ming to provide independent advice on the fairness and reasonableness of the disposal transaction. On the basis of the three meetings in 2006, the independent board committee convened another three meetings in 2007 to study the disposal transaction. In addition, the continuing connected transactions between China Netcom Group and CNC China, a wholly owned subsidiary of the Company, expired in 2007 and were renewed. In accordance with the requirements of the Listing Rules, the Board established an independent board committee, which comprised all independent non-executive Directors and chaired by Mr. Timpson Chung Shui Ming. The independent board committee held four meetings in 2007 to review the fairness and reasonableness of these continuing connected transactions. The committee acted in the interests of the minority shareholders, reviewed the qualifications and capability of the independent financial advisor and discussed in detail the fairness and reasonableness of the terms of the disposal and continuing connected transactions, in order to protect the legitimate rights and interests of the minority shareholders.

To fully demonstrate the function of independent non-executive Directors and protect the interests of the minority shareholders, the Board, in accordance with legal requirements and international best practices, arranged for the independent non-executive Directors to play a key role in reviewing all the connected transactions.

The Company has obtained the confirmation from all the independent non-executive Directors relating to their independence under the Listing Rules. The Company considered all the independent non-executive Directors to be independent. There were no relationship among the Directors (including the Chairman and the Chief Executive Officer).

Non-Executive Directors

All non-executive directors are appointed for a term of three years, and are subject to retirement by rotation and re-election by shareholders. Pursuant to the Articles of Association of the Company, one-third of the Directors, including both executive and non-executive Directors, are required to retire from office by rotation at the annual general meeting each year. A retiring Director is eligible for re-election. Any Director who is appointed by the Board will hold office until the next following general meeting and will be eligible for re-election.

Board Committees

In 2007, the structure of the Board committees remained unchanged. There were five committees under the Board, namely, the Audit Committee, the Compensation Committee, the Nominating and Corporate Governance Committee, the Strategy Committee and the Supervision Committee. The Board clearly defined the responsibilities of each committee as well as their terms of reference.

Audit Committee

To guarantee the objectiveness, fairness and independence of the Audit Committee, the Audit Committee comprises four Independent Non-Executive Directors and is chaired by Mr. Timpson Chung Shui Ming. Other members of the committee include Mr. Victor Cha Mou Zing, Dr. Qian Yingyi and Mr. Hou Ziqiang. The primary responsibilities of the Audit Committee include supervising and managing our financial reporting system, reviewing the appointment of auditors, and supervising the work of the internal audit department as well as guiding and supervising our internal control system.

As a fellow member of the HKICPA and of the ACCA, Mr. Chung has extensive professional experience. His active participation has helped improve the internal control system and the financial reporting system of the Company. Led by Mr. Chung, not only has the Audit Committee performed its responsibilities in supervising corporate auditing, it also played an important role in optimizing the Company's internal control system. The Audit Committee reviews the implementation on the internal control system regularly, and supervises the rectification of internal control problems identified and has established an effective channel of complaints and reports.

In 2007, the Audit Committee held four meetings and discharged its responsibilities under the relevant regulations, including reviewing the financial statements, annual reports and accounts, interim reports as well as major comments concerning financial reporting in the financial statements and reports; reviewing the reappointment of external auditor and making suggestions to the Board; reviewing and pre-approving the annual engagement letter of the external auditors including the proposed service fees, all audit and non-audit services permitted under the Sarbanes-Oxley Act and the rules and regulations published by U.S. Securities and Exchange Commission as well as the relationship between the Company and its external auditors. Besides, the Committee also reviewed and discussed with the external auditors on the annual audit plan (including the timeline and scope of audit activities), supervised the annual progress and results of the plan, reviewed the Company's internal control project, received reports from the internal audit department on a regular basis and reviewed connected transactions other than those required to be reviewed by the independent board committee as prescribed under the Listing Rules.

The Board recognizes its responsibility for the financial statements. The auditor's statement on its responsibility for the financial statements is set out in the auditor's report on the financial statements on Page 75 to 76 of this annual report.

During the reporting period ended December 31, 2007, the fees that are paid to the external auditors by the Company for both audit and non-audit services are listed as follows:

Nature of Services	Amount (RMB thousands)
Audit services	54,000
Audit-related services	5,039
Non-audit services	
(i) taxation services and transfer pricing report	542
(ii) other services	395

Compensation Committee

The primary duties of the Compensation Committee include making recommendations to the Board in respect of the overall compensation policies and structure of the Directors and senior management of the Company and the establishment of formal and transparent procedures for the formulation of these policies; determining the specific compensation package of the senior management on behalf of the Board and making recommendations to the Board in respect of the compensation of the non-executive Directors; reviewing and supervising the share option scheme and option allocation plan proposal of the Company; and assessing the performance of the Directors as well as the senior management.

The Compensation Committee of the Board is chaired by Dr. Qian Yingyi, an Independent Non-Executive Director; other members include Mr. Zhang Xiaotie, Mr. Li Fushen, Mr. John Lawson Thornton and Mr. Timpson Chung Shui Ming.

In 2007, the Compensation Committee held three meetings. Its work included the organization and implementation of the performance evaluation for directors in 2006, the implementation of the performance assessment and compensation scheme for the senior management in 2006, the consideration and approval of the performance assessment and compensation implementation plan for senior management in 2007, the organization of market study on the compensation for senior managements of industry peers in PRC and abroad, and the supervision of the implementation of the Company's share option scheme.

Nominating and Corporate Governance Committee

The Nominating and Corporate Governance Committee is dedicated to the formation of a sound composition with industry experience and professional capability within the Board. The primary duties of the committee include the nomination of Directors and senior management, supervising the implementation of corporate governance system and the operation efficiency of the Board and making recommendations to the Board with regard to the optimization of the corporate governance structure. In accordance with the Guidelines for Directors of the Company, the Nominating and Corporate Governance Committee is responsible for formulating the criteria for selecting directors, working out Directors' succession plan, suggesting candidates of Directors, and submitting the related proposals to the Board and/or shareholders' meeting for review and approval. For the nomination of candidates for new appointments of directors, the committee primarily considers whether the candidates have the necessary professional expertise or experience to help the Board perform its duties in a better way and promote the development of the Company. The independence of independent non-executive Directors is examined by the committee.

The committee is chaired by Mr. John Lawson Thornton, an Independent Non-Executive Director. Other members include: Mr. Zhang Chunjiang, Mr. Zuo Xunsheng, Dr. Qian Yingyi and Mr. Victor Cha Mou Zing.

The Nominating and Corporate Governance Committee is committed to the continued optimization of the composition of the Board and the management and the continuous enhancement of the corporate governance system of the Company. It has been playing a very positive role in the optimisation of the structure and mechanism of the Company's corporate governance system. In 2007, the Nominating and Corporate Governance Committee held six meetings. Its work included the consideration of the working plan on the enhancement of the corporate governance in 2007, the evaluation report on the performance of the Board and its committees in 2006, the report on proposals for improving the Board committees in 2007 and other documents including 2007 performance evaluation form for the Board and Board committees; the review of the revised version of constitutional documents such as "Management Rules for Information Disclosure", "Articles of Association", "Procedural Rules for the Board of Directors and Board Committees", "Guidelines for the Board of Directors", "Guidelines for Directors" and "Interim Measures on Performance Assessment of Senior Executives of the Management" ; and the consideration of the changes of directors, committee members and senior vice presidents, the proposed list of directors who will retire and seek re-election at the Annual General Meeting, and the independence of the Company's independent non-executive Directors, which were submitted to the Board for approval.

Strategy Committee

The Strategy Committee is primarily responsible for reviewing the medium to long-term strategies, annual operation plans and budgets and significant investment plans of the Company. It also reviews and monitors the procedures and system for the risk management of the Company and supervises the implementation of its development strategies.

The committee is chaired by Mr. Zhang Chunjiang. Other members include: Mr. Zuo Xunsheng, Ms. Li Jianguo, Mr. Li Fushen, Mr. José María Álvarez-Pallete, Dr. Qian Yingyi and Mr. Hou Ziqiang.

In 2007, the Strategy Committee held four meetings to review and approve the southern China Strategy adjustment plan, the innovation and development plan and the 2008 operation plan and budget of the Company, and to hear the Company's reports on its implementation of strategies and its capital expenditure (CAPEX) management and its risk management, which were submitted to the Board for discussions and approval.

Supervision Committee

The Supervision Committee is primarily responsible for identifying and handling disciplinary breach, violation of regulations and corruption of the middle-to-senior management by establishing and improving the supervisory system and procedures and opening up channels for reporting such behaviors in accordance with the Listing Rules and regulatory requirements. It requests the directors and the middle-to-senior management as well as other staff to abide by the rules, be conscious of self-discipline and faithfully discharge their duties.

The committee is chaired by Ms. Li Jianguo. Other members include Mr. Zhang Xiaotie, Mr. Victor Cha Mou Zing, Mr. Hou Ziqiang and Mr. Timpson Chung Shui Ming.

In 2007, the Supervision Committee held two meetings and approved and published some institutional documents including the "Interim Measures on the Public Awareness Campaign of the Code of Ethics of the Supervision Committee of the Board of

Directors" and the "Interim Measures on the Inspection Work of the Supervision Committee of the Board of Directors"; in addition, the committee also considered and approved other reports and matters including the "Summary of China Netcom Group's Disciplinary Inspection and Supervision Work in 2006 and Work Plan for 2007", "Report on the Implementation of the Codes of Ethics for Directors and Middle-to-Senior Management and Codes of Conducts of Employees in 2006" and "Report on the handling of Allegations and Complaints of the Company in 2006".

Attendance at the Meetings of the Board and its Committees

Current Directors*	Board of Directors	Independent Board Committee	Audit Committee	Compensation Committee	Nominating & Corporate Governance Committee	Strategy Committee	Supervision Committee
Executive Directors							
ZHANG Chunjiang *(Chairman)*	6/7	N/A	N/A	N/A	5/6	4/4	N/A
ZUO Xunsheng *(CEO)*	7/7	N/A	N/A	N/A	4/6	3/4	N/A
LI Jianguo	3/3	N/A	N/A	N/A	N/A	1/1	1/1
ZHANG Xiaotie^	7/7	N/A	N/A	3/3	N/A	N/A	2/2
LI Fushen	6/6	N/A	N/A	3/3	N/A	3/3	N/A
Non-executive Directors							
YAN Yixun^	7/7	N/A	N/A	N/A	N/A	N/A	N/A
Cesareo ALIERTA IZUEL	0/0	N/A	N/A	N/A	N/A	N/A	N/A
José María ÁLVAREZ-PALLETE^	7/7	N/A	N/A	N/A	N/A	4/4	N/A
Independent Non-executive Directors							
John Lawson THORNTON^	7/7	7/7	N/A	3/3	4/6	N/A	N/A
Victor CHA Mou Zing^	7/7	6/7	3/4	N/A	6/6	N/A	2/2
QIAN Yingyi	7/7	7/7	4/4	3/3	6/6	4/4	N/A
HOU Ziqiang^	7/7	7/7	4/4	N/A	N/A	4/4	2/2
Timpson CHUNG Shui Ming	7/7	7/7	4/4	3/3	N/A	N/A	2/2
Resigned Directors#							
MIAO Jianhua	3/4	N/A	N/A	N/A	N/A	N/A	1/1
LI Liming	0/1	N/A	N/A	N/A	N/A	0/1	N/A
TIAN Suning *(Vice Chairman)*	1/4	N/A	N/A	N/A	N/A	0/2	N/A
Mauricio SARTORIUS	7/7	N/A	N/A	N/A	N/A	N/A	N/A

* *Mr. Li Fushen has been a director and member of the Compensation Committee and the Strategy Committee since January 15, 2007; Ms. Li Jianguo has been a director and member of the Supervision Committee since July 12, 2007 and member of the Strategy Committee since August 22, 2007; Mr. Cesareo Alierta Izuel has been a director since December 5, 2007.*

\# *Ms. Li Liming resigned as a director and member of the Compensation Committee and the Strategy Committee on January 15, 2007; Mr. Miao Jianhua resigned as a director and member of the Supervision Committee on July 12, 2007; Dr. Tian Suning resigned as a director and member of the Strategy Committee on July 12, 2007; Mr. Mauricio Sartorius resigned as a director on December 5, 2007.*

^ *Each of Mr. Zhang Xiaotie, Mr. Yan Yixun, Mr. Victor Cha Mou Zing and Mr. Hou Ziqiang was represented by his alternate director at one of the Board meetings; Mr. José María Álvarez-Pallete was represented by his alternate director at five of the Board meetings and one of the Strategy Committee meetings; Mr. John Lawson Thornton was represented by his alternate director at three of the Board meetings, two of the Independent Board Committee meetings and one of the Nominating and Corporate Governance Committee meetings.*

Share Transactions of Directors

In respect of the requirements for directors' share transactions, the Board has adopted the provisions of the Model Code under Appendix 10 to the Listing Rules for the share transactions of Directors and has required directors to comply with these provisions. The Company has received the confirmation from the Directors that during the reporting period, all the Directors have complied with these requirements.

Comparison between corporate governance requirements of the New York Stock Exchange and the Hong Kong Listing Rules

According to the Corporate Governance Standards set out in Section 303A of New York Stock Exchange (NYSE) Listing Company Manual, foreign issuers listed on NYSE (including China Netcom Group Corporation (Hong Kong) Limited) are required to disclose major differences in requirements of corporate governance between its place of incorporation and those of NYSE applicable to local US issuers. A summary of such differences is available on the website of the Company at http://www.china-netcom.com/eng/about/summary.htm.

Internal Controls

The Board is responsible for the internal control system of the Company and has the responsibility to review its effectiveness. In 2007, the Board conducted a review of the effectiveness of the internal control system of the Company.

The Company began to improve its internal control system on a Company-wide basis in October 2004. The Company's internal control system is in line with the international laws and regulations and was established based on the actual situation of the Company after the Company had fully reformed and reviewed the effectiveness of its internal control system relating to financial reporting. Given compliance with Sarbanes-Oxley Act in respect of internal control audit in 2006, the Company further improved and optimized its internal control system and put in place a sound and long-term system of internal control based on the actual situation of the Company and taking into account of the latest international regulatory requirements in 2007.

As a result of the above, the Board found no significant issues in its internal control system in 2007.

Shareholder Communications

In 2007, the Company continued to commit its efforts in improving both the scope and quality of information disclosure in order to enhance the transparency of its operation. In 2007, the Company began to disclose the number of the subscribers of its primary services on a monthly basis. This enables the investors to know about the Company's operation and the effect of the strategies implementation in a timely manner and to work out a more reasonable forecast on our development trend, which will minimize investment risks caused by information opacity.

In 2007, we have been, as always, proactive in improving our communications with shareholders. Efforts had been made to improve the quality of our response to the questions received via our Investors Hotline and Investors Mailbox, to increase the frequency and quality of meeting between the management and the investors and to improve the user-friendliness of our investor relations website. In addition, we had actively taken part in the investor conferences held by major investment banks. In 2007, we met the representatives from over 220 investors and held about 120 meetings with the investors, of which nearly 100 meetings were attended by the Chairman, Chief Executive Officer and Chief Financial Officer of the Company.

General Meetings

The most recent General Meeting was the Extraordinary General Meeting held on December 6, 2007 at the Ballroom, Island Shangri-la, Hong Kong. The major items discussed at the meeting and the voting results are set out below:

— Approval of the continuing connected transactions contemplated under the Engineering and Information Technology Services Agreement 2008 - 2010 and the relevant annual caps (99.9999%).

— Approval of the continuing connected transactions contemplated under the Domestic Interconnection Settlement Agreement 2008 - 2010 and the International Long Distance Voice Services Settlement Agreement 2008 - 2010 for which no annual caps have been proposed (99.9999%);

— Approval of the amendments to the Articles of Association of the Company (99.9846%).

The above resolutions were all passed at the Extraordinary General Meeting. The results of the voting by poll were published on the Company's website and the website of the Hong Kong Stock Exchange.

The next General Meeting will be the Annual General Meeting to be held on May 22, 2008.

The Company is engaged in building up a sound corporate governance system. The Board of the Company firmly believes that better corporate governance will help the Company increase its competitiveness and create value to the shareholders. On the basis of the "Corporate Governance Consultancy Project" initiated in 2005, the Board proposed a number of revisions to the Articles of

Association of the Company. The revisions, approved by the shareholders at the Extraordinary General Manager held on December 6, 2007, cover the following items: (a) procedure for appointment and removal of chief executive officer, senior vice presidents and chief financial officer; (b) term of directors; (c) participation of employees in the management of the Company; (d) minimum number of Board members and quorum for meetings of the Board; and (e) election of the chairman of the meetings of the Board. Please refer to the Shareholders' Circular dated November 9, 2007 for the details of the amendments.

Information relating to the details of shareholders, their shareholdings and the Company's public float status are set out in the Report of the Directors (page 72) in this annual report.

Performance of share price

Our ordinary shares are listed on The Stock Exchange of Hong Kong Limited, and our shares are also listed and traded in the form of depositary shares on the New York Stock Exchange.

The closing price of our ordinary shares on The Stock Exchange of Hong Kong Limited on the last trading day in 2007 was HK$23.45, representing an increase of 12.47% over that of 2006. The Company's market capitalization was HK$156,513 million. In 2007, the average daily trading volume of our ordinary shares amounted to 12,402,234.02 shares, representing an increase of 23.74% over 2006.

The closing price of our ADS on the last trading day in 2007 was US$59.40, representing an increase of 10.99% over that of 2006, and the average daily trading volume amounted to 189,273.9 ADS, representing an increase of 197.87% over 2006.

In 2007, the Company strengthened the establishment of the management team, regularized remuneration distribution and performance appraisals, and enhanced labor management and staff trainings, so as to facilitate the Company's overall goal of successful strategic transformation.

Employees

As of December 31, 2007, we had 142,110 full-time employees, representing an increase of 0.97% over the same period of last year; 39,891 temporary staff, representing a decrease of 28.02% over the same period of last year.

Enhance establishment of the management team

In 2007, the Company completed a strict, fair and objective performance evaluation on the senior management of some of the provincial branches. We also strengthened the training of the back-up team of nearly a hundred expertise, so as to create a talent pool for the Company.

In 2007, the Company changed its singular administration management promotion through the establishment of position system, and established a two-way promotion channel for the staff through management process and professional technique process, so as to provide the talented staff with multi-dimensional development and promotion opportunities.

Regulation of Remuneration distribution and Performance Appraisal

In 2007, the Company further regularized the remuneration distribution system, and established a unified position and remuneration system. The new system fully reflected the "market-oriented, performance priority, harmonious and systematic"management concept, with the effect of catalyzing a more proactive attitude among our staff and providing a strong support for realization of the Company's strategic objectives.

In 2007, the Company further improved the performance appraisal system, enhanced guidance and supervision on the appraisal works, strengthened the supports of the front-line staff to the back office staff, and the appraisals of the back office staff to the front-line staff, with the aim to create a performance-oriented corporate culture to ensure the realization of the Company's strategic objectives.

Strengthen Staff Training

In 2007, the Company strengthened staff training on innovative businesses, management transformation and Olympic Games services:

- With the theme of "Innovation and Development", we organized seminars on innovative business, where over 100 middle and high-level executives attended, and through the promotion of online program trainings, an aggregate of 59,000 persons have received trainings;
- In accordance with the Olympic Strategy and the requirements posed by the Olympic sponsorship, 83 Olympic training classes have been held, with an aggregate of 4,292 persons received training;
- According to the training plan, 22 training classes on management theory and practice have been provided to managers of county-level companies, with 907 people received training;
- Training courses for operational R&D and maintenance staff and for managers of important clients;
- With the aim of introducing international best management experiences, we continued the exchanges of staff with other well-known overseas operators, through which 10 persons have been sent to PCCW and Telefonica.

Regularize Labor Management

In 2007, pursuant to the Labor Contract Law, the Company unified and regularized its labor contract management, unified the text of labor contracts, regularized the forms of labor, and a mechanism of staff entry and exit was put in place.

Full-scale Implementation of Information System

In 2007, an overall human resources information management system was being promoted and implemented through systematic and extensive trainings, which significantly enhanced the accuracy and timeliness in the exchange of human resources data, leading to a regulated, single and transparent approach for work force management.

- Innovative businesses grew by 38.9% and accounted for 34.7% of total revenues, representing an increase of 9.5 percentage points over the same period of last year;

- The number of broadband subscribers continued to grow at a high speed and reached 19,768 thousand, representing an increase of 37% over the same period of last year;

- Value-added services continued to enjoy robust growth. The number of "Personalised Ring" subscribers reached 28,137 thousand, representing an increase of 78.6% over the same period of last year, and the number of caller identification subscribers reached 79,984 thousand, representing a penetration rate of 72.2%;

- The Company continuously strengthened the capability of providing enterprise customers with services of integrated telecommunications, IT and IT-related applications, and recorded an ICT revenue of RMB3,990 million, accounting for 4.8% of the total revenues;

- In the telecommunications industry customer satisfaction investigation organized by the Ministry of Information Industry, the Company's fixed-line telephone and broadband access both ranked first in subscribers' satisfaction index once again.

Summary of Key Product lines

Fixed-line Telephone Services	Broadband and Other Internet-related Services	ICT and Business Data Communication	Advertising and Media Services
110,820 thousand subscribers (including PHS)	19,768 thousand subscribers	Targeting at enterprise customers	Yellow Pages Phone Navigation Online Advertising
90.4% market share[(1) (2)]	88.9% broadband market share[(1) (2)]	Unique competitive strength	Broad space for development
70.0% of revenue[(3)]	17.4% of revenue[(3)]	9.4% of revenue[(3)]	0.5% of revenue[(3)]
Decrease of 9.9% [(3)]	37.7% growth[(3)]	62.1% growth	691.7% growth

(1) As of December 31, 2007

(2) In our northern service regions

(3) Excluding upfront connection fees

In 2007, amid market competition context of intensifying mobile substitution, we accelerated our strategic transformation towards becoming a "broadband communications and multimedia services provider" under the theme of "innovations and transformation", and fully captured the opportunities brought by 2008 Beijing Olympics and the society informatization promoted by the State.

In line with strategic transformation, the Company commenced reform of the operation concept of single product promotion, and gradually shifted to a customer-oriented marketing system. As for the Large Corporates and Government customers, the Company was dedicated in providing integrated information technology solutions and postioning itself as an "information service expert". As for SME (Small and Medium Enterprises) customers, the Company provided information technology solutions and applications facilitating the linkage between the SME customers and their upstream and downstream businessesunder the brand of "CNC Connected" to satisfy their needs in enterprise communication, business activities and office management. As for Residential customers, the Company leveraged its "Family 1+" brand to boost the growth of broadband access and broadband content and applications while reducing the churn rate of fixed-line telephone subscribers. Meantime, through the gradual convergence of access terminals, the Company pursuited the conversion of "Family 1+" from service bundling to satisfying family demands for multimedia information services.

In 2007, the Company realized continuing operation revenue of RMB82,488 million (excluding upfront connection fees), representing an increase of 0.9% over the same period of the previous year. The innovative businesses, including broadband, value-added services, ICT and advertising and media services were the major drivers for revenue growth.

Key operating statistics for 2007 and 2006:

	2006	**2007**	Growth rate
Fixed-line subscribers ('000)	113,972	**110,820**	-2.8%
Including: PHS subscribers	27,316	**26,189**	-4.1%
Broadband subscribers ('000)	14,429	**19,768**	37.0%
Total usage (pulses in millions)	214,474	**202,547**	-5.6%
Excluding Internet dial-up usage (pulses in millions)	209,223	**198,887**	-4.9%
Internet dial-up usage (pulses in millions)	5,251	**3,660**	-30.3%
Domestic long distance calls (minutes in millions)	28,809	**28,797**	-0.04%
International long distance calls[1] (minutes in millions)	324	**344**	6.2%
Number of ports for DDN (ports)	115,315	**101,815**	-11.7%
Number of ports for Frame Relay (ports)	41,254	**37,337**	-9.5%
Number of ports for ATM (ports)	6,361	**6,876**	8.1%
Digital circuits leased (x2Mbps)	161,582	**219,881**	36.1%
Volume of PHS short messages (in millions)	7,815	**7,531**	-3.6%
"Personalised Ring" service subscribers ('000)	15,758	**28,137**	78.6%
Penetration rate for caller identification (%)	68.8%	**72.2%**	3.4%
Telephone information services (million minutes)	2,457	**1,696**	-31.0%

(1) International long distance call volume includes calls to Hong Kong, Macau and Taiwan

Fixed-line Telephone Services

In 2007, as domestic mobile operators launched service packages at competitive prices and the implemented calling party pay policy, the voice migration from fixed-line to mobile intensified. As at the end of 2007, the aggregate number of our fixed-line subscribers was 110,820 thousand, down by 2.8% over the same period of the previous year. In 2007, our local voice traffic also declined. Stripping out dial-up internet access, the usage volume of local telephone services was 198,887 million pulses, down by 4.9% over the same period of last year.

In 2007, the Company fully exploited its advantage of multi-services and rich network resources, and launched "Family 1+" bundled services and "Same Number" providing convergent functions of fixed-line and mobile voice services. Through the trial launching of intelligent terminals and "Home Box", the Company has been gradually changing the "Family 1+" from simple services bundling to satisfying family demands for multimedia information services. In 2007, "Family 1+" greatly drove the growth of the innovative businesses, and enhanced the overall values of fix-line telephone subscribers. As at the end of 2007, the number of our "Family 1+" subscribers reached 8,378 thousand, of which 59.5% subscribed to the broadband services provided by the Company.

It is believed that, with the increasing penetration rate of "Family 1+" and "Same Number" and with the transformation of "Family 1+" to family multimedia information services, the values of fixed-line telephone subscribers will be exploited to the greater extent.

Unit: '000 Subscribers	2005	2006	**2007**
Fixed-line subscribers	114,658	113,972	**110,820**
Including: Residential	70,273	68,803	**67,162**
Business	10,725	10,946	**10,575**
PHS	27,329	27,316	**26,189**
Public telephones	6,331	6,907	**6,894**

In 2007, we proactively implemented marketing programs to stimulate long distance voice traffic. Under the fierce competition in the long distance business market, the domestic long distance voice traffic approximately equaled to that of the previous year, while the international long distance voice traffic increased by 6.2% over the corresponding period of the previous year.

Unit: million minutes	2005	2006	**2007**
Domestic long distance calls	27,775	28,809	28,797
Including: Traditional network	15,653	17,327	18,482
VOIP	12,122	11,482	10,315
International long distance calls	352	324	344
Including: Traditional network	156	144	155
VOIP	196	180	189

Broadband and Other Internet-related Services

Broadband services are the most valuable core businesses in the Company's strategic transformation. In 2007, in response to the State's initiative of "Integrating IT Application with Industrialization", the Company fully implemented the "Super Broadband Plan", and launched the development model of "access + content & applications" fee mechanism and the "PC + TV" multi-terminal broadband service, sustaining rapid growth trend of the broadband services.

In 2007, the Company fully upgraded broadband access speed, and provided multi-level high speed access service to customers. The Company also actively performed Olympics marketing, and enhanced the promotion activities of "Broadband Carnival". By fully leveraging its status as an official partner of Olympic Games , the Company promoted "2008 Broadband Hotel" service in earnest. By the end of 2007, we had converted 1,741 hotels into "2008 Broadband Hotels". Driven by the above factors as well as "Family 1+". The aggregate number of broadband subscribers increased by 5,339 thousand to 19,768 thousand, representing an increase of 37.0% over the previous year. In our service regions, the Company continued to maintain its leading market share of 88.9%, representing an increase of 1.4 percentage points over the previous year.

Unit: '000 subscribers	2005	2006	**2007**
Number of broadband subscribers	11,036.2	14,428.6	**19,767.7**
Including: DSL	8,529.2	11,287.9	**15,777.1**
LAN	2,507.0	3,140.7	**3,990.6**

In 2007, the Company was dedicated in the strengthening of broadband content and applications and in the innovation of marketing model for such services. In 2007, the Company launched "CNC MAX" Clients directly providing the rich broadband content and applications to users' desktops. Based on application of video, the Company developed such major programs as "Interactive Oral-English" and "Car World" channel, and initiated innovative business model in respect of corporate video advertising, product video advertising, etc. through "My Commercial World" channel.

Meanwhile, the Company was still dedicated in extending broadband content and applications from PC to TV in 2007. As at the end of 2007, the Company's AVS-IPTV technical experiments in Dalian district successfully passed the acceptance testing of the Ministry of the Information Industry (the present Ministry of Industry and Information), and started commercial applications in the Dalian region. As at the end of 2007, the number of the Company's IPTV subscribers reached 324 thousand, representing an increase of 49.4% over the corresponding period of the previous year.

In 2007, under the brand "CNC Connected", the Company provided integrated communication and information services, including information technology application, communication value-added services and basic communication products, to Small and Medium Enterprise customers of different industries and with different needs. In 2007, the number of subscribers of the Company's "CNC Connected" platform continued to grow rapidly.

Value-added Services

In 2007, the Company completed the renovation of intelligent network and developed NGN value-added business. As for Residential customers, the Company made great efforts in promoting such services as fixed-line "Personalised Ring" and "Phonemate", bundled with "Family 1+". As for SME customers, the Company promoted switchboard, corporate "Personalised Ring", virtual fax and internet hard disk, etc., bundled with "CNC Connected". As at the end of 2007, the number of the Company's "Personalised Ring" subscribers was 28,137 thousand, representing approximately 78.6% over the corresponding period of the previous year, of which the number of "Personalised Ring" subscribers in fixed-line telephones was 19,970 thousand, representing an increase of 124.1% over the corresponding period of the previous

year. The number of Phonemate subscribers was 5,322 thousand, representing an increase of 401.2% over the corresponding period of the previous year. The penetration rate of caller identification reached 72.2%, representing an increase of 3.4 percentage points over the corresponding of the previous year.

ICT Services and Business Data Communications Business

In 2007, through integration of resources, rationalization of process and the building of professional team, the Company has significantly strengthened its capability of providing solutions to the corporate customers, R&D capability, project management capability and system maintenance capability. In 2007, the Company has established its own core advantage and its capabilities in providing integrated solutions in E-Government, environmental monitoring, "Safe City" and Olympic Admin&Games.

With the growth of the professional team, in 2007, the Company gradually moved up the value chain of ICT business, and strengthened its capabilities in solution designs, software development and operation management and maintenance. With the extension of the Company's ICT business to the high end of the value chain, the Company will explore the call centers and IDC outsourcing service sectors by leveraging the advantages of Company's brands, customer base and network resources, migrating from resources leasing to provision of integrated information solutions to customers.

The ICT business allows the Company to establish deeper business relationship with corporate customers while satisfying the growing demand of corporate customers for information services so as to more effectively retain customers and generate new revenue sources. In 2007, revenue from the Company's ICT business amounted to RMB3,990 million, representing an increase of 366.7% over the corresponding period of the previous year.

Summary of Business Data Communications Business

	2005	2006	**2007**
Number of ports			
DDN (ports)	131,713	115,315	**101,815**
Frame Relay (ports)	43,449	41,254	**37,337**
ATM (ports)	4,193	6,361	**6,876**
Leasing of broadband lines			
DDN (x64 kbps)	197,925	192,395	**172,573**
Frame Relay (x128 kbps)	171,251	183,757	**173,896**
ATM (x2 Mbps)	11,907	15,857	**13,837**
MPLS VPN (x2Mbps)	73	157	**3,834**
Leasd circuit bandwidth (x2 Mbps)	126,276	161,582	**219,881**
Corporate subscriber (x2 Mbps)	96,674	137,792	**198,793**
Operator subscriber (x2 Mbps)	29,602	23,790	**21,088**

Advertising and Media Services

As a leading telecommunications services provider with a century's operating history, the Company has rich media resources and has started to establish its competitive edge in the advertising and media business since 2007 through integrating and leveraging the Company's diversified media related resources with extensive coverage and comprehensive support.

The Company's advertising and media business focuses on yellow pages, voice search and online advertising.

- Yellow pages is a traditional business of telecommunication operators. In 2008, the Company will take advantage of the business opportunities brought by the Olympic Games to make innovation in its products, to expand the B2C market, and to create leading media by combining with internet and voice products;
- As for voice search, the Company will focus on "Phone Navigation" to create the image of expert in voice search;
- As for online advertising, the Company will rely on "CNC MAX" Clients to expand the internet user base and create the "Focus" media of the Internet.

In 2007, the Company's advertising and media business achieved rapid growth in revenue, generating a revenue of RMB380 million for the full year, up 691.7% from last year.

Branding

In 2007, capturing the opportunities presented by 2008 Olympic Games, the Company further strengthened its corporate image of a "broadband communications and multimedia services provider". Meanwhile, in accordance with the strategic transformation and in line with the customers' increasing demand for integrated information and communication services, the Company systematically built and promoted customer brands based on customer-oriented principle.

- Created the corporate image of a "broadband communication and multimedia services provider"
  - ➢ Integrated the brand concept of "A Broadbanden World" with Olympic spirits, to initiate extensive advertising activities and create the corporate image of a "broadband communications and multimedia services provider";
  - ➢ Organized a series of events with the theme of "CNC Broadband Olympic China Tour", organically integrated the concept of the Olympic Games with the connotation of the corporate brand so that the corporate image was more deeply rooted in the hearts of people.
- Strengthened the building and promotion of customer brands
  - ➢ Established the brand image of "Family 1+" as improving the quality of family life through multimedia information services, refined the products and services under the "Family 1+"brand and created an edge in service differentiation by launching brand special services, subscription services and extended services;

- Built the brand "CNC Connected" and established the brand image of assisting Small and Medium enterprises in their rapid development, based on the principle of "strengthening corporate competitiveness and continually upgrading our business";

- Established the brand image of "network information & communication expert" among Large Corporates and Government customer through the implementation of a series of key industry information solutions; strengthened one-stop services, optimized the failure handling and feedback system for Large Corporates and Government customers and established the platform for communication and enhanced relationship with customers through the"VIP Club".

Olympic Games Marketing

In 2007, focusing on the theme of "Broadband Olympic Games", the Company proceeded with Olympic Games marketing in four aspects, namely brand upgrading, product innovation, market expansion and strategic partnership, so as to create opportunities for the leap-forward development of the Company into a "broadband communications and multimedia services provider".

- Based on the demand of the Company's target customers during the Olympic Games, the Company implemented strategic transformation of devoting full efforts to developing innovative businesses, strongly integrated the Company's innovative businesses resources, and lunched 26 broadband products for the Olympic Games of the three categories of "Perfect Services", "Convenient Information"and"Value Addition"in order to expediting the leap-forward growth of the innovative businesses by capturing opportunities presented by the Olympic Games;

- The Company promoted Olympic Games products and innovative businesses with the utilization of scarce resources such as Olympic Games tickets,

- The Company cooperated with other Olympic Games official partners such as Legend, Kodak, PICC, Air China, VISA and Bank of China in resources sharing, mutual business utilization and joint promotion. By fully capitalizing the demands for communication in various industries brought by Olympic Games and the status of Olympic Games official partners to acquire major customers, the Company enlarged its market share and made innovation in the service model.

Transformation of the Customer-oriented Marketing System

In 2007, with the transformation of the marketing system as the trigger of breakthrough in transforming the operating system, the Company completed all kinds the preparatory work for the construction of the customer-oriented sales and marketing system.

The sales and marketing system was established with three primary customer groups, namely Large Corporates and Government, Small and Medium Enterprises (SME) and Residentials, in order to satisfy customer needs for integrated multimedia and information services as well as to improve and enhance customer experiences. Resources were allocated on the basis of customer groups and various products and applications were bundled according to the needs of customer groups. By moving from marketing standard products to satisfying customized needs, value was created for customers. Meanwhile, by changing the functional organization structure which was separated by market lines and network lines, by laterally integrating various professional lines, and by vertically streamlining the management structure, the execution efficiency and the customer response rate were enhanced.

Network Construction

In 2007, our network construction and CAPEX investment continued to focus on supporting the strategic transformation of the Company to ensure continuing rapid growth of the innovative businesses.

In 2007, our network supporting capabilities for innovative businesses were enhanced at various network levels, including infrastructural and portal networks etc., and the structure and security of our networks were optimized:

- Continuously enhanced the network capabilities of the infrastructural networks such as trunk transmission network, IP network, etc. to support the rapid development of broadband services;
- Accelerated the deployment and application of soft switches by using local intelligent transformation, new business applications and network exit equipment substitution as the breakthrough point;
- Promoted the process of replacing copper cables with optical fibres for developing the broadband business and upgrading the overall network. The Company gave priority to fibre-optic access in newly constructed networks, while systematically transforming copper wire access into fibre-optic access in the operating networks, so that fibres-optic access was further extended to users, broadband access speed was enhanced and the costs of construction and maintenance were reduced.
- Tracked closely the developments of new technology and new businesses and actively commenced commercial tests to support the development of new businesses. In 2007, the Company completed the construction of valued-added business platforms for CNC Connected, Phone Navigation and integrated terminal user businesses, etc., creating a sound foundation for the rapid development of innovative businesses.

In 2007, we continued to improve the CAPEX budget management system, and created an improved system for initial assessment and final appraisal of investment projects, increasing utilization efficiency of investments. In 2007, our total CAPEX amounted to RMB20,684 million, representing a year-on-year decrease of 15.8%. CAPEX accounted for 25.1% of our revenue, down by 4.9 percentage points compared with the corresponding period of the previous year. In 2007, we continued to optimize the CAPEX investment structure to create a concept of investing for the future. In 2007, the proportion of total investments in traditional businesses to the total CAPEX fell by 10.6 percentage point compared with the corresponding period of previous year, while the proportion of investments in the innovative businesses to the total CAPEX increased by 10.2 percentage points compared with the corresponding period of the previous year. The CAPEX structure became more scientifc and reasonable.

Management's Discussion and Analysis of Financial Condition and Results of Operations

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

On December 5, 2007, China Netcom Group System Integration Limited Corporation ("System Integration Corporation"), a wholly-owned subsidiary of the Company, entered into an Equity Interest Transfer Agreement with China Netcom Group Beijing Communications Corporation, pursuant to which System Integration Corporation agreed to acquire the entire equity interest of Beijing Telecommunications Planning and Designing Institute Corporation Limited ("Beijing Telecom P&D Institute"). The acquisition was completed on December 31, 2007. Before the acquisition, Beijing Telecom P&D Institute was a wholly owned subsidiary of China Netcom Beijing Communications Corporation, which is a wholly owned subsidiary of China Netcom Group. Since China Netcom Group is the ultimate holding company of the Group, the acquisition is a business combination under common control. Therefore, the Group accounted for this acquisition using the pooling of interest method according to Accounting Guideline No. 5 - Merger Accounting for Common Control Transactions ("AG 5"). The acquired businesses and assets are recorded at book value under HKFRS as if the businesses and assets of Beijing Telecom P&D Institute have been owned by the Group from the earliest comparative period presented. Accordingly, the financial information for year 2006 has been restated.

Unless otherwise specified, the following analysis is made on the basis of continuing operations.

Summary

Our revenue for 2007 amounted to RMB84,005 million, including upfront connection fees of RMB1,517 million. If excluding upfront connection fees, our revenue for 2007 amounted to RMB82,488 million, representing an increase of 0.9% from 2006. Our operating expenses for 2007 amounted to RMB66,739 million. If excluding upfront connection fees, our profit for the year from continuing operations amounted to RMB9,954 million, if including profit from discontinued operations of RMB624 million, our profit for the year was RMB10,578 million, which approximately equaled to RMB10,559 million in 2006.

Benefiting from the effective control over capital expenditures, our cash flows and financial situation have been further improved. In 2007, our capital expenditures amounted to RMB20,684 million, representing a decrease of 15.8% from 2006. Our free cash flow amounted to RMB11,775 million, representing an increase of 57.2% from 2006. Our debt to capital ratio[1] was 39.8%, representing a decrease of 7.5 percentage points from 2006.

(1) *Debt to capital ratio refers to the ratio of our total indebtedness to the sum of our total indebtedness, shareholders' equity and balance of deferred revenue.*

Revenue

Sources of our revenue consisted of revenues from fixed-line telephone services, broadband and other Internet-related services, information and communications technology services and other services.

Our revenue for 2007 amounted to RMB84,005 million, of which upfront connection fees amounted to RMB1,517 million. If excluding upfront connection fees, our revenue for 2007 amounted to RMB82,488 million, representing a growth of RMB700 million or 0.9% from RMB81,788 million in 2006. The growth primarily reflected increase in revenues from broadband services, information and communications technology services and value-added services.

The following table illustrated a breakdown of our revenue and their percentages of total revenue in 2006 and 2007.

	For the year ended December 31			
	2006		**2007**	
	Amount	Percentage of Revenue	**Amount**	**Percentage of Revenue**
	(RMB millions, except percentage data)			
Fixed-line telephone services:				
Local:				
Local usage fees	22,059	26.2%	**19,989**	**23.8%**
Monthly fees	16,546	19.6%	**12,387**	**14.8%**
Upfront installation fees	1,364	1.6%	**1,283**	**1.5%**
Subtotal	39,969	47.4%	**33,659**	**40.1%**
Domestic long-distance	9,495	11.3%	**8,769**	**10.4%**
International long-distance	819	1.0%	**791**	**0.9%**
Value-added services	5,341	6.3%	**6,114**	**7.3%**
Interconnection fees	8,432	10.0%	**8,376**	**10.0%**
Upfront connection fees	2,406	2.9%	**1,517**	**1.8%**
Subtotal	66,462	78.9%	**59,226**	**70.5%**
Broadband services	9,916	11.8%	**13,835**	**16.5%**
Other Internet-related services	516	0.6%	**532**	**0.6%**
Managed data	1,413	1.7%	**1,284**	**1.5%**
Leased line	2,540	3.0%	**2,521**	**3.0%**
Information and communications technology services	855	1.0%	**3,990**	**4.8%**
Other services	2,492	3.0%	**2,617**	**3.1%**
Total	84,194	100 %	**84,005**	**100%**

Fixed-line telephone services

Local telephone services

Revenue from our local telephone services amounted to RMB33,659 million in 2007, representing a decrease of RMB6,310 million, or 15.8%, from RMB39,969 million in 2006. Revenue from local telephone services accounted for 40.1% of our total revenue in 2007, representing a decrease of 7.3 percentage points from 2006. In 2007, competition in the telecommunications market was even more intense with increasing trend of mobile substitution, leading to a decrease in the number of fixed-line telephone services customers and the volume of local usage and a downward adjustment of our realized tariff, which were the main causes of the decrease in revenue from local telephone services.

Local usage fees

Revenue from local usage fees amounted to RMB19,989 million in 2007, representing a decrease of RMB2,070 million, or 9.4%, from RMB22,059 million in 2006. In 2007, the usage volume of local calls amounted to 202.55 billion pulses, representing a decrease of 11.93 billion pulses, or 5.6%, from 2006. The decline in revenue of local usage fees was mainly attributable to reduced usage volume of local calls and the decrease in our realized tariff as a result of the policy to adjust the inter-district tariff as well as market competition.

Monthly fees

Revenue from our monthly fees amounted to RMB12,387 million in 2007, representing a decrease of RMB4,159 million, or 25.1%, from RMB16,546 million in 2006. The revenue decline was mainly attributable to the intensifying market competition. The Company enhanced its promotion of special price package, which resulted in the decrease in the level of actual monthly fees.

Upfront installation fees

Revenue from our upfront installation fees amounted to RMB1,283 million in 2007, representing a decrease of RMB81 million, or 5.9%, from RMB1,364 million in 2006.

Domestic long-distance calls

Our revenue from domestic long-distance calls amounted to RMB8,769 million in 2007, representing a decrease of RMB726 million, or 7.6%, from RMB9,495 million in 2006.The usage volume of domestic long-distance calls was 28,797 million minutes, approximixately equaled to 28,809 million minutes in 2006. The decrease in our realized tariff was the main reason for the decrease in our domestic long-distance calls revenue.

International long-distance calls

Our revenue from our international long-distance calls amounted to RMB791 million in 2007, representing a decrease of RMB28 million, or 3.4%, from RMB819 million in 2006. The usage volume of international long-distance calls was 344 million minutes in 2007, representing an increase of 20 million minutes, or 6.2%, from 324 million minutes in 2006. The decrease in revenue was mainly attributable to the decrease in realized tariff.

Value-added services

Revenue from our value-added services amounted to RMB6,114 million in 2007, representing an increase of RMB773 million, or 14.5%, from RMB5,341 million in 2006. Increase in revenue was mainly attributable to the rapid growth in the personalized ring and voice mail-box businesses. The main reason for the increase in revenue was the continued development and launching of new value-added services by the Company, and the increasing penetration rate of the existing value-added operations such as personalized ring and voice mail-box.

Interconnection services

Revenue from our interconnection services amounted to RMB8,376 million in 2007, representing a decrease of 0.7%, from RMB8,432 million in 2006. The decrease in revenue from settlement of interconnection fees was mainly due to the decrease in voice traffic from other telecommunications carriers resulted from mobile substitution and the decrease in our realized tariff as a result of the policy to adjust the inter-district tariff.

Upfront connection fees

Revenue from our upfront connection fees amounted to RMB1,517 million in 2007, decreased by RMB889 million, or36.9%, from RMB2,406 million in 2006. Upfront connection fees represent the amortized amount of the upfront fees for the initial activation of fixed-line telephone services, which the Company amortizes over the expected customer relationship period of 10 years. Starting from July 2001, the Company ceased to charge upfront connection fees so that such revenue will continue to decline in the coming years until they are amortized completely.

Broadband services

Revenue from our broadband services amounted to RMB13,835 million in 2007, representing an increase of RMB3,919 million, or 39.5%, from RMB9,916 million in 2006. At the end of 2007, the number of our broadband services subscribers was 19,768 thousand, representing an increase of 5,339 thousand, or 37.0%, from14,429 thousand at the end of 2006. The growth in revenue from broadband services was mainly attributable to the sustained expansion of our subscriber base and the sustained growth in ARPU due to the increasing number of subscribers of high-speed broadband access and broadband content services and applications.

Other Internet-related services

Revenue from our other Internet-related services amounted to RMB532 million in 2007, representing an increase of RMB16 million, or 3.1%, from RMB516 million in 2006. The growth in revenue was mainly due to the significant increase of the Internet private access revenue, which offseted the decrease of the narrowband dial-up access revenue.

Managed data services

Revenue from our managed data services amounted to RMB1,284 million in 2007, representing a decrease of RMB129 million, or 9.1%, from RMB1,413 million in 2006, which was mainly due to the decrease in usage of traditional services as result of the substitution by new means of access.

Leased line services

The operating revenue from our leased line services amounted to RMB2,521 million in 2007, representing a decrease of RMB19 million, or 0.7%, from RMB2,540 million in 2006. This was mainly due to the decrease in realized tariff as result of competition, which offseted the increase in the demand of customers for network resources.

Revenue from information and communications technology services

In 2007, revenue from information and communications technology services amounted to RMB3,990 million, representing an increase of RMB3,135 million, or 366.7%, from RMB855 million in 2006. Revenue from information and communications technology accounted for 4.8% of our total revenue in 2007, representing an increase of 3.8 percentage points from 2006. Information and communications technology had started to become an important factor driving the increase in the Company's revenue. The increase was mainly due to continued strengthening of our capability to provide total solutions to large corporates and government, which results in the significant increase in the number of contracts signed in our information and communications technology services business.

Other services

The revenue from other services amounted to RMB2,617 million in 2007, representing an increase of RMB125 million, or 5.0%, from RMB2,492 million in 2006. The increase in revenue was mainly derived from the increase in the revenue from advertising and media business. In 2007, the Company recorded revenue from advertising and media business of RMB380 million, representing an increase of RMB332 million over 2006.

Operating expenses

The key components of our operating expenses are depreciation and amortization expenses, network, operations and support expenses, selling, general and administrative expenses, staff costs and other operating expenses. Our operating expenses amounted to RMB66,739 million in 2007, representing an increase of RMB2,096 million, or 3.2%, from RMB64,643 million in 2006. The ratio of operating expenses to revenue excluding upfront connection fees increased from 79.0% in 2006 to 80.9% in 2007.

The following table sets forth a breakdown of our operating expenses and their percentage of revenue excluding upfront connection fees in 2006 and 2007:

	For the year ended December 31			
	2006		**2007**	
	Amount	Percentage of revenue excluding upfront connection fees	**Amount**	**Percentage of revenue excluding upfront connection fees**
	(RMB millions, except percentage data)			
Depreciation and amortization expenses	24,913	30.5%	**25,495**	**30.9%**
Network, operations and support expenses	13,344	16.3%	**14,145**	**17.1%**
Staff costs	11,849	14.5%	**12,223**	**14.8%**
Selling, general and administrative expenses	12,607	15.4%	**10,615**	**12.9%**
Other operating expenses	1,930	2.3%	**4,261**	**5.2%**
Total operating expenses	64,643	79.0%	**66,739**	**80.9%**

Depreciation and amortization

Our depreciation and amortization expenses amounted to RMB25,495 million in 2007, representing an increase of RMB582 million, or 2.3%, from RMB24,913 million in 2006. The ratio of depreciation and amortization expenses to revenue excluding upfront connection fees increased from 30.5% in 2006 to 30.9% in 2007. The increase in depreciation and amortization expenses was mainly due to the increase in the total fixed assets and intangible assets for which the Company made provisions for depreciation and amortization.

Network, operations and support expenses

Network, operations and support expenses amounted to RMB14,145 million in 2007, representing an increase of RMB801 million, or 6.0%, from RMB13,344 million in 2006. The ratio of network, operations and support expenses to revenue excluding upfront connection fees increased from 16.3% in 2006 to 17.1% in 2007. The increase in network, operations and support expenses was mainly due to the increase of customer access cost as a result of the change in the broadband operation mode. In addition, the costs of both the power and fuel consumed by our equipment also increased under the impact of the rise in energy prices.

Staff costs

Our staff costs amounted to RMB12,223 million in 2007, representing an increase of RMB374 million, or 3.2%, from RMB11,849 million in 2006. The ratio of staff costs to revenue excluding upfront connection fees increased from 14.5% in 2006 to 14.8% in 2007. The increase in staff costs was mainly due to our increase in the staff cost in innovative businesses and the increase in the insurance premiums and welfare brought by the average increase in social salaries.

Selling, general and administrative expenses

Our selling, general and administrative expenses amounted to RMB10,615 million in 2007, representing a decrease of RMB1,992 million, or 15.8%, from RMB12,607 million in 2006. The ratio of selling, general and administrative expenses to revenue excluding upfront connection fees decreased from 15.4% in 2006 to 12.9% in 2007. Decrease in selling, general and administrative expenses was mainly due to the decrease in the selling expenses, which in turn was due to the Company's decrease in investments in low-end users, leading to the decrease in the cost of acquiring customers and the cost of retaining customers. Another reason was the Company's change in the mode of developing broadband business, leading to the decrease in the cost of acquiring broadband users.

Other operating expenses

Other operating expenses amounted to RMB4,261 million in 2007, representing an increase of RMB2,331 million, or 120.8%, from RMB1,930 million in 2006. The ratio of other operating expense to revenue excluding upfront connection fees increased from 2.3% in 2006 to 5.2%. The increase in other operating expenses was mainly due to the significant increase in the information and communications technology services related costs.

Other income

Other income amounted to RMB1,221 million in 2007, representing an increase of RMB600 million from RMB621 million in 2006. Other income is the subsidy income the Company received from reinvesting the profit distributions received from a subsidiary in the PRC to that subsidiary.

Finance costs

In 2007, our finance costs amounted to RMB3,333 million, representing a decrease of RMB434 million, or 11.5%, from RMB3,767 million in 2006. The decrease in finance costs was mainly due to the Company's utilizing the sufficient cash flow to repay substantial amount of interest bearing debts, at the same time eliminating the impact caused by the increasing bank loan interest rates through the issue of short-term commercial papers and corporate bonds which reduced the average level of our funding costs.

Taxation

Our income tax for 2007 amounted to RMB3,796 million, representing an effective taxation rate of 24.9%. Our statutory taxation rate in the PRC was 33% in 2007. The effective taxation rate was lower than the statutory taxation rate, mainly because upfront connection fees and other income was exempt from income tax.

Profit for the year from continuing operations

Our profit for the year from continuing operations amounted to RMB11,471 million in 2007. If the effect of the income from upfront connection fees is excluded, our profit for 2007 from continuing operations would amount to RMB9,954 million, representing an increase of RMB882 million, or 9.7% from RMB9,072 million in 2006. The main reason for the increase was that a deficit on revaluation of fixed assets of RMB1,335 million was recognized as an expense in 2006.

Net profit for the year from discontinued operations

Net profit for the year from discontinued operation in 2007 amounted to RMB624 million as a result of the disposal of the Guangdong and Shanghai Branches by CNC China, our wholly-owned subsidiary, on February 28, 2007. Of that amount, the net loss of the Guangdong and Shanghai Branches prior to the completion date amounted to RMB2 million, and the investment gain net of taxes from the disposal of the Guangdong and Shanghai Branches amounted to RMB626 million.

Consolidated profit for the year

Our consolidated profit including discontinued operations for 2007 amounted to RMB12,095 million. If excluding the upfront connection fee, our profit for 2007 would amount to RMB10,578 million, which approximately equaled to RMB10,559 million in 2006.

Profit for the year reconciled to US GAAP

Our consolidated profit for 2007 under US GAAP was RMB8,950 million. Our profit for 2007 under US GAAP was lower than that under Hong Kong GAAP. This was principally due to the revaluation of certain classes of fixed assets under Hong Kong GAAP, which resulted in lower depreciation charges recorded of RMB4,482 million under Hong Kong GAAP compared to that under US GAAP. At the same time, a gain net of taxes from the disposal of the Guangdong and Shanghai Branches of RMB626 million was recognised in the income statement under Hong Kong GAAP, while the gain was recognised directly in the shareholders' equity under U.S. GAAP.

Capital expenditure

The following table sets forth our total actual and planned capital expenditure for the periods indicated:

	(RMB millions)
2006	24,560
2007	20,684
2008 (planned)	19,600

Our capital expenditure in 2007 amounted to RMB20,684 million, representing a decrease of RMB3,876 million, or 15.8%, from RMB24,560 million in 2006, which was mainly due to our emphasis on enhancing the utilization rate of our existing network and our implementation of a policy which focused on cost-effectiveness, which reasonably reduced capital expenditure. In 2007, we continued to increase our investment in broadband and Internet, and we also accordingly reduced our investment in local telephones and network transmission equipment.

We expected to further reduce our capital expenditure in 2008, which was estimated at RMB19,600 million. Many factors could affect the timing, amount and nature of our capital expenditure, including the overall economic environment, customer demand, technology development and other related factors. Our estimated capital expenditure had a certain degree of uncertainty, and the future actual capital expenditure may deviate from the estimated amount.

We anticipate that we will meet our capital expenditure requirements with cash generated from operating activities, short-term and long-term loans, debentures and other borrowings and equity financing. We consider that we shall have sufficient capital to meet our future capital expenditure requirements.

Cash flow and capital resources

Cash flow

The following table sets out our cash flow for the periods indicated

	For the year ended 31 December,	
	2006	**2007**
	(RMB millions)	
Net cash inflow from operating activities	32,050	**32,459**
Net cash outflow from investment activities	(24,051)	**(19,138)**
Net cash outflow from financing activities	(6,477)	**(19,131)**
Net cash inflow from discontinued operations	1,164	**3,491**
Net cash inflow/(outflow)	2,686	**(2,319)**

Our net cash inflow from operating activities in 2007 amounted to RMB32,459 million, representing an increase of RMB409 million, or 1.3%, from RMB32,050 million in 2006. The reason for the increase of the net cash outflow from operation activities in 2007 was mainly due to the decrease in interest expenses brought by the improvements in our financial situation. If excluding effect of interest expenses and cash payout for income taxes, our cash-flow from operation activities would amount to RMB39,309 million, which approximately equaled to RMB39,156 million in 2006.

Our net cash outflow in investment activities in 2007 amounted to RMB19,138 million, representing a decrease of RMB4,913 million, or 20.4%, from RMB24,051 million in 2006, which was mainly due to the significant decrease in our capital expenditures in 2007 than in 2006.

Our net cash outflow in financing activities in 2007 amounted to RMB19,131 million, representing an increase of RMB12,654 million, or 195.4%, from RMB6,477 million in 2006, which was mainly due to the increase in the repayment of interest bearing debts in 2007 than in 2006.

Free cash-flow arising from our continuing operations amounted to RMB11,775 million, representing an increase of RMB4,285 million, or 57.2%, from RMB7,490 million in 2006. Our cash-flow was significantly optimized, and company value continued to enhance.

Our cash inflow from discontinued operations amounted to RMB3,491 million, the main reason for which was that we received RMB3,500 million as consideration for the disposal of assets, liabilities and operations on telecommunications in the branches in Guangdong province and Shanghai in the PRC by CNC China, our wholly-owned subsidiary.

For these reasons, our net cash outflow in 2007 amounted to RMB2,319 million, representing a decrease of RMB5,005 million compared with a net cash inflow of RMB2,686 million in 2006.

Working capital

As at December 31, 2007, the shortfall of our working capital amounted to RMB59,085 million, a decrease of RMB13,522 million or 18.6% in shortfall from RMB72,607 million in 2006. The decrease in shortfall of working capital was mainly due to the decrease in short-term loans of the Company.

Indebtedness

Our indebtedness as at the dates indicated:

	For the year ended December 31	
	2006	**2007**
	(RMB millions)	
Short term bank loans	30,980	**11,850**
Current portion of long term bank and other loan	7,304	**5,322**
Long term bank and other loans net of current portion	23,219	**14,425**
Short term commercial paper	9,811	**20,000**
Corporate bonds	—	**2,000**
Current portion of amounts due to holding companies and fellow subsidiaries	1,960	**1,960**
Amounts due to holding companies and fellow subsidiaries net of current portion	5,880	**6,169**
Total indebtedness	79,154	**61,726**

Management's Discussion and Analysis of Financial Condition and Results of Operations

As at December 31, 2007, our total indebtedness amounted to RMB61,726 million, representing a decrease of RMB17,428 million or 22% from RMB79,154 million as at the end of 2006. The source of capital for the repayment was our free cash-flow and the consideration for the disposal of assets, liabilities and operations of telecommunications in the branches in Guangdong province and Shanghai in the PRC by CNC China, our wholly-owned subsidiary.

As at December 31, 2007, the proportion of our short-term debts to our total indebtedness was 63.4%, which approximately equaled to 63.2% as at December 31, 2006.

As at December 31, 2007, our debt to capital ratio was 39.8%, representing a decrease of 7.5 percentage points from 47.3% as at December 31, 2006. Our financial position was significantly improved.

As at December 31, 2007, our aggregate outstanding banking facilities available amounted to RMB106,824 million in total.

Contractual obligations and commitments

The following table sets forth our aggregate payments as at December 31, 2007 in respect of contractual obligations and commercial commitments (including interest expense) in the years to come:

	Payments Due (by stages as indicated) (RMB millions)						
	Total	**2008**	**2009**	**2010**	**2011**	**2012**	**Thereafter**
Short-term bank loans	12,134	12,134	—	—	—	—	—
long term bank and other loans	21,616	6,407	10,272	1,887	106	104	2,840
Short term commercial paper	20,629	20,629	—	—	—	—	—
Corporate bonds	2,900	90	90	90	90	90	2,450
Amounts due to holding companies and fellow subsidiaries	8,870	2,319	2,214	4,337	—	—	—
Operating lease commitments	2,004	579	346	305	247	236	291
Capital commitments	677	661	—	16	—	—	—
Total	68,830	42,819	12,922	6,635	443	430	5,581

Market risks and risk management

Market risks are the risks of loss of financial instruments held or issued by us for non-trading purposes arising from adverse changes in market prices, including adverse charge in interest rates and foreign exchange rates. The Company is subject to various risks in the normal course of its business, including market risks associated with interest rate movements and exchange rate movements on non-Renminbi denominated assets and liabilities.

Foreign exchange risk

We conduct our business primarily in Renminbi, which is our booking and reporting currency. Fluctuations in Renminbi exchange rates may adversely affect the value, translated or converted into United States dollars or Hong Kong dollars (which are pegged to the US dollars), of our net assets, earnings and any declared dividends.

We are exposed to foreign currency risk primarily as a result of our foreign currency borrowings for the purchase of telecommunication equipment from overseas suppliers in the past. In addition, we receive some of our revenue from our international telecommunications services and pay related expenses in foreign currencies. As a result, our foreign currency exposure relates to our foreign currency-denominated businesses and, to a limited extent, cash and cash equivalents denominated in foreign currencies.

Interest rate risk

The People's Bank of China has the sole authority in the PRC to establish the official interest rates for Renminbi-denominated loans. Financial institutions in the PRC set their effective interest rates within the range established by the People's Bank of China. Interest rates and payment methods in the PRC on loans denominated in foreign currencies are set by the financial institutions based on interest rate changes in the international financial market, cost of funds, risk levels and other factors.

The Company's interest-rate risk arise from interest bearing debts. Borrowing issued at variable rates expose the Company to cash flow interest-rate risk. Borrowing issued at fixed rates expose the Company to fair value interest-rate risk. As at December 31, 2007, 83.96% of our total indebtedness were with fixed interest rate.

Report of the Directors

The directors are pleased to present their annual report together with the audited financial statements for the year ended December 31, 2007.

Principal activities

The Group is a dominant provider of fixed-line telephone services, broadband, other Internet-related services, and business and data communications services in ten northern municipalities and provinces in China, namely Beijing Municipality, Tianjin Municipality, Hebei Province, Henan Province, Shandong Province, Liaoning Province, Heilongjiang Province, Jilin Province, Neimenggu Autonomous Region and Shanxi Province. The principal activity of the Company is investment holding.

For a short period during 2007, the Group also provided telecommunications services to selected business and residential customers in two southern municipality and province, namely Guangdong Province and Shanghai Municipality in China. On January 15, 2007, China Netcom (Group) Company Limited ("**CNC China**"), a wholly owned subsidiary of the Company, and China Network Communications Group Corporation ("**China Netcom Group**") entered into an asset transfer agreement to dispose of the Group's telecommunications assets, liabilities and operations in Guangdong Province and Shanghai Municipality. The asset transfer was approved by shareholders at the extraordinary general meeting held on February 14, 2007 and was completed on February 28, 2007. After completion of the asset transfer, the Group no longer provides telecommunications services in these two southern municipality and province.

The turnover of the Group during the financial year consisted primarily of income generated from the provision of fixed-line telecommunications and related services.

Major customers and suppliers

The Group's aggregate sales attributable to its five largest customers did not exceed 30 per cent. of the Group's total sales in 2007.

The Group's aggregate purchases from its five largest suppliers did not exceed 30 per cent. the Group's total purchases in 2007.

Subsidiaries

Particulars of the Company's subsidiaries as at December 31, 2007 are set out in note 27 to the financial statements.

Financial statements

The results of the Group for the year ended December 31, 2007 and the Company's and the Group's financial positions as at that date are set out in the financial statements on pages 77 to 154.

Dividends

The Company has always held in the highest regard the interests of and returns achieved for its shareholders. Having taken into account such factors as our results of operations, cash flows, financial condition, future prospects, and statutory and regulatory restrictions on the payment of dividend by the Company, the Board recommends payment of a final dividend of HK$0.592 per share for the financial year ended December 31, 2007. The dividend payout ratio for 2007 is 35%. If the relevant resolution relating to the declaration of dividend is passed, the dividend will be distributed on or about June 12, 2008 to shareholders whose names are registered on the Company's shareholders' register on May 22, 2008.

Charitable donations

Donations made by the Group during the year amounted to RMB0.35 million (2006: RMB0.53 million).

Fixed assets

Changes of the fixed assets of the Group and the Company during the year are set out in note 21 to the financial statements.

Bank and other loans

Particulars of bank and other loans of the Group as at December 31, 2007 are set out in note 30 to the financial statements.

Share capital and share option scheme

Details of the Company's share capital and share option scheme are set out in note 35 and note 36 respectively, to the financial statements. Information on the share option scheme can also be found in the paragraph "Share option scheme" below.

Debenture

The Group issued two tranches of commercial paper for the aggregate amount of RMB20 billion in 2007. One tranche of the commercial paper was issued for the amount of RMB10 billion at an interest rate of 3.34% with a maturity period of 365 days, and the other tranche of the commercial paper was issued for the amount of RMB10 billion at an interest rate of 3.93% with a maturity period of 270 days. In addition, the Group issued corporate bonds for the aggregate amount of RMB2 billion in 2007. The corporate bonds were issued at a coupon rate of 4.5% with a maturity period of 10 years and a credit rating of AAA. The proceeds from the issue of the aforesaid commercial paper and corporate bonds are used for general working capital purposes.

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

During the year, neither the Company nor any of its subsidiaries purchased, sold or redeemed any of the Company's listed securities.

Reserves

Changes to the reserves of the Company and the Group during the year are set out in the consolidated statement of changes in equity and in note 37 to the financial statements.

Financial summary

A summary of the audited results and of the audited assets and liabilities of the Group for the last five financial years is set out on pages 162 to 164.

Connected Transactions

(1) (a) Asset transfer

As at December 31, 2007, China Netcom Group, as the ultimate controlling shareholder of the Company, beneficially owned 69.6% of the Company's issued share capital. China Netcom Group is therefore a connected person of the Company. On January 15, 2007, CNC China entered into an assets transfer agreement with China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its telecommunications assets, liabilities and business operations in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality ("**China Netcom Shanghai and Guangdong**") in the People's Republic of China ("**PRC**") for the consideration of RMB3.5 billion ("**Asset Transfer**"). On February 14, 2007, the independent shareholders passed an ordinary resolution to approve the asset transfer and the asset transfer was completed on February 28, 2007 upon the approval from the Ministry of Information Industry ("MII").

(b) Acquisition

China Netcom Group System Integration Limited Corporation ("**China Netcom System Integration**"), an indirect wholly-owned subsidiary of the Company, entered into the Equity Interest Transfer Agreement on December 5, 2007 with China Netcom Group Beijing Communications Corporation ("**China Netcom Beijing**"), a wholly-owned subsidiaries of China Netcom Group, pursuant to which China Netcom System Integration agreed to acquire the entire equity interest of Beijing Telecommunications Planning and Designing Institute Corporation Limited ("**Beijing Telecommunications Design Institute**"), a wholly-owned subsidiary of China Netcom Beijing from China Netcom Beijing for a total consideration of RMB298,915,300.The transaction was completed on December 31, 2007.

(2) Continuing connected transactions

On September 12, 2005, China Netcom Group, CNC China and China Netcom Group New Horizon Communications Corporation Limited ("**New Horizon Communications**", an indirectly wholly-owned subsidiary of the Company) entered into certain connected transactions agreements. CNC China completed its merger with New Horizon Communications on November 3, 2006 ("**Merger**"). Pursuant to the aforesaid connected transactions agreements, all New Horizon Communications' rights and obligations under the agreements were taken over by CNC China after the Merger and the agreements remained effective between China Netcom Group and CNC China. On November 7, 2006, China Netcom System Integration entered into a connected transaction agreement ("**Information and Communications Technology Agreement**") with China Netcom Group (and its subsidiaries). The aforesaid connected transactions agreements remained effective as at December 31, 2007.These transactions between CNC China and China Netcom Group and between China Netcom System Integration and China Netcom Group (the "**Continuing Connected Transactions**") constitute continuing connected transactions of the Company under the Listing Rules. For the financial year ended December 31, 2007, the Continuing Connected Transactions have not exceeded their respective upper limits set by the Hong Kong Stock Exchange. In respect of all the connected transactions of the Company as stated in this report, the Company has complied with the disclosure requirements under the Listing Rules in force from time to time.

The aforesaid connected transaction agreements (save for the Information and Communications Technology Agreement) have expired on December 31, 2007. On November 6, 2007, the Board of the Company approved the renewal of certain connected transactions agreements between CNC China and China Netcom Group in order to extend the term of the existing connected transactions agreements between CNC China, New Horizon Communications and China Netcom Group. The new agreements will be effective from January 1, 2008 for a term of 3 years. China Netcom System Integration and China Netcom Group entered into a new agreement on November 6, 2007 for a term of 3 years commencing from January 1, 2008 to replace the existing Information and Communications Technology Agreement.The aforesaid renewal connected transactions agreements were disclosed in the Company's Announcement entitled "Renewal of Continuing Connected Transactions / Amendments to the Articles of Association" dated on November 6, 2007 and the Circular dated on November 9, 2007.

Continuing connected transactions relating to CNC China

Domestic Interconnection Settlement Agreement

Pursuant to the Domestic Interconnection Settlement Agreement:

CNC China and China Netcom Group agreed to interconnect the network of China Netcom Group on the one hand and that of CNC China on the other and settle the charges received in respect of domestic long distance voice services within their respective service regions on a quarterly basis.

For domestic long distance voice services between China Netcom Group and CNC China, the telephone operator in the location of the calling party makes a settlement payment to the telephone operator in the location of the called party at the rate of RMB0.06 per minute (in case where the call terminates within the network of either China Netcom Group or CNC China) or RMB0.09 per minute (in case where the call terminates outside the network of either China Netcom Group or CNC China).

This agreement was renewed on November 6, 2007 for a term of 3 years commencing on January 1, 2008. Pursuant to the renewal agreement, the settlement of payment relating to domestic long distance voice services shall be made by the telephone operator in the location of the calling party to the telephone operator in the location of the called party. For domestic long distance voice services between China Netcom Group and CNC China, the telephone operator in the location of the calling party makes a settlement payment to the telephone operator in the location of the called party at the rate of RMB0.06 per minute, irrespective of whether the call terminates within the network of either China Netcom Group or CNC China or outside the network of either China Netcom Group or CNC China. The rate of RMB0.06 per minute mentioned above shall be adjusted with reference to the relevant standards, tariffs or policies formulated by the relevant regulatory authorities in China from time to time. The aforesaid settlement rate takes retrospective effect from April 1, 2007.

International Long Distance Voice Services Settlement Agreement

Pursuant to the International Long Distance Voice Services Settlement Agreement:

CNC China and China Netcom Group agreed to interconnect the networks of China Netcom Group and CNC China and settle the charges received in respect of international long distance voice services on a quarterly basis.

For outbound international calls, China Netcom Group reimburses CNC China for any amount it has paid to overseas telecommunications operators. The revenues received by China Netcom Group less the amount paid to overseas telecommunications operators are shared between China Netcom Group and CNC China in proportion to the estimated costs incurred by China Netcom Group and CNC China in connection with the provision of outbound international long distance voice services.

For inbound international calls, the revenues received by CNC China from overseas telecommunications operators (other than the Company and its controlled entities) less the amount paid to China Netcom Group at the rate of RMB0.06 per minute (in case where the call terminates within the network of China Netcom Group) or RMB0.09 per minute (in case where the call terminates within the network of other operators) are shared between China Netcom Group and CNC China in proportion to the estimated costs incurred by China Netcom Group and CNC China in connection with the provision of inbound international long distance voice services.

This agreement was renewed on November 6, 2007 for a term of 3 years commencing on January 1, 2008. Pursuant to the renewal agreement, for inbound international calls, the settlement rate between CNC China and China Netcom Group will be RMB0.06 per minute, irrespective of whether the call terminates within the network of China Netcom Group or within the network of other operators.The rate of RMB0.06 per minute mentioned above shall be adjusted with reference to the relevant standards, tariffs or policies formulated by the relevant regulatory authorities in China from time to time. The aforesaid settlement rate takes retrospective effect from April 1, 2007.

Property Leasing Agreement

Pursuant to the Property Leasing Agreement:

(a) CNC China leases to China Netcom Group certain properties located throughout the service regions of CNC China, for use as offices and other ancillary purposes; and

(b) China Netcom Group leases to CNC China certain properties located throughout the service regions of CNC China, for use as offices, telecommunications equipment sites and other ancillary purposes.

The charges payable by CNC China and by China Netcom Group are based on market rates or the depreciation and maintenance charges in respect of each property, provided such depreciation and maintenance charges shall not be higher than the market rates. The charges are payable quarterly in arrears and are subject to review every year to take into account the then prevailing market rates of the properties leased in that year.

This agreement was renewed on November 6, 2007 for a term of 3 years commencing on January 1, 2008. Pursuant to the renewal agreement, one party can sub-lease the aforesaid property to a third party with the prior written consent of the other party and provided that the third party assumes the responsibilities under the renewal agreement.

Property Sub-leasing Agreement

Pursuant to the Property Sub-leasing Agreement:

China Netcom Group agreed to sub-let to CNC China certain properties owned by and leased from independent third parties, for use as offices, telecommunications equipment sites and other ancillary purposes.

The amounts payable by CNC China under the Property Sub-leasing Agreement are the same as the rental charges and other fees (including management fees) payable by China Netcom Group to the relevant third parties.

This agreement has expired on December 31, 2007.

Master Sharing Agreement

Pursuant to the Master Sharing Agreement:

(a) CNC China will provide customer relationship management services for large enterprise customers of China Netcom Group;

(b) CNC China will provide network management services to China Netcom Group;

(c) CNC China will share with China Netcom Group the services provided by administrative and managerial staff in respect of central management of the business operations, financial control, operation and maintenance of network, human resources and other related matters of both CNC China and China Netcom Group;

(d) CNC China will provide to China Netcom Group supporting services such as billing and settlement provided by the business support centre;

(e) China Netcom Group will provide to CNC China supporting services, including telephone card production, development and related services and IC card inter-provincial and inter-network clearing services;

(f) China Netcom Group will provide to CNC China certain other shared services, including advertising, publicity, research and development, business hospitality, maintenance and property management;

(g) China Netcom Group will provide certain office space in its headquarters to CNC China for use as its principal executive office; and

(h) CNC China and China Netcom Group will share the revenues received by China Netcom Group from other operators whose networks interconnect with the Internet backbone network of China Netcom Group and will share the monthly connection fee that China Netcom Group pays to the State Internet Switching Centre.

CNC China and China Netcom Group own certain equipment and facilities forming the Internet backbone network of China Netcom Group. This Internet backbone network interconnects with the networks of other operators. Such interconnection generates revenue which is settled with China Netcom Group and shared between China Netcom Group and CNC China under the Master Sharing Agreement.

The services set out in paragraphs (a) to (g) above and the revenue and fee set out in paragraph (h) above are shared between CNC China and China Netcom Group on an on-going basis from time to time and the aggregate costs incurred by CNC China or China Netcom Group for the provision of the services set out in paragraphs (a) to (g) above and the revenue and fee receivable and payable by China Netcom Group as referred to in paragraph (h) above are apportioned between CNC China and China Netcom Group according to their respective total assets value as shown in their respective financial statements on an annual basis.

This agreement was renewed on November 6, 2007. The renewal agreement is effective from January 1, 2008 for a term of 3 years.

Engineering and Information Technology Services Agreement

The Engineering and Information Technology Services Agreement governs the arrangements with respect to the provision of certain engineering and information technology-related services to CNC China by China Netcom Group, which include planning, surveying and design services in relation to telecommunications engineering projects, construction services in relation to telecommunications engineering projects, supervision services in relation to telecommunications engineering projects and information technology services.

The charges payable for engineering and information technology-related services described above are determined with reference to market rates. In addition, where the value of any single item of engineering design or supervision-related service exceeds RMB0.5 million or where the value of any single item of engineering construction-related service exceeds RMB2 million, the award of such services will be subject to tender. The charges are settled between CNC China and China Netcom Group as and when the relevant services are provided.

This agreement was renewed on November 6, 2007. The renewal agreement is effective from January 1, 2008 for a term of 3 years.

Materials Procurement Agreement

Pursuant to the Materials Procurement Agreement, CNC China may request China Netcom Group to act as its agent for the procurement of imported and domestic telecommunications equipment and other domestic non-telecommunications equipment, and may purchase from China Netcom Group certain products, including cables, modems and yellow pages telephone directories. China Netcom Group further agreed to provide to CNC China storage and transportation services related to the procurement and purchase of materials or equipment.

Commission and/or charges for the domestic materials procurement services shall not exceed the maximum rate of 3% of the contract value. Commission and/or charges for the above imported materials procurement services shall not exceed the maximum rate of 1% of the contract value. The price for the purchase of China Netcom Group's products is determined with reference to the following principles and limits (the "**Pricing Principles**") and shall not exceed:

(a) the government fixed price;

(b) where there is no government fixed price but a government guidance price exists, the government guidance price;

(c) where there is neither a government fixed price nor a government guidance price, the market price; or

(d) where none of the above is applicable, the price to be agreed between the relevant parties and determined on a cost-plus basis.

Commission charges for the storage and transportation services are determined with reference to market rates.

Payments under the Materials Procurement Agreement will be made as and when the relevant equipment or products have been procured and delivered.

This Agreement was renewed on November 6, 2007. The renewal agreement is effective from January 1, 2008 for a term of 3 years.

Ancillary Telecommunications Services Agreement

The Ancillary Telecommunications Services Agreement governs the arrangements with respect to the provision of ancillary telecommunications services to CNC China by China Netcom Group, which include certain telecommunications pre-sale, on-sale and after-sale services, sales agency services, printing and invoice delivery services, maintenance of telephone booths, customers acquisition and servicing and other customers' services.

The charges payable for the services described above are determined with reference to the Pricing Principles and the service charges are settled between CNC China and China Netcom Group as and when the relevant services are provided.

This agreement was renewed on November 6, 2007. The renewal agreement is effective from January 1, 2008 for a term of 3 years.

Support Services Agreement

Pursuant to the Support Services Agreement, China Netcom Group provides CNC China with various support services, including equipment leasing (other than equipment covered under the Telecommunications Facilities Leasing Agreement) and maintenance services, motor vehicles services, security services, basic construction agency services, research and development services, employing training services and advertising services and other support services.

The charges payable for the services described above are determined with reference to the Pricing Principles, and are settled between CNC China and China Netcom Group as and when relevant services are provided.

This Agreement was renewed on November 6, 2007. The renewed agreement becomes effective on January 1, 2008 for a term of 3 years.

Telecommunications Facilities Leasing Agreement

Pursuant to the Telecommunications Facilities Leasing Agreement, China Netcom Group leases inter-provincial fiber-optic cables within the service regions of CNC China to CNC China, and leases certain international telecommunications resources (including international telecommunications channel gateways, international telecommunications service gateways, international submarine cable capacity, international land cables and international satellite facilities) to CNC China, and China Netcom Group leases certain other telecommunications facilities required by CNC China for its operations.

The rental charges and service charges for the leasing of inter-provincial fibre-optic cables, international telecommunications resources and other telecommunications facilities are based on the annual depreciation charges of such fibre-optic cables, resources and telecommunications facilities provided that such charges shall not be higher than market rates. CNC China shall be responsible for the on-going maintenance of such inter-provincial fibre-optic cables and international telecommunications resources. CNC China and China Netcom Group shall determine and agree on which party is to provide maintenance services to the other telecommunications facilities leased by China Netcom Group to CNC China based on the latter's operational requirements. Unless otherwise agreed by CNC China and China Netcom Group, such maintenance service charges shall be borne by CNC China. If China Netcom Group shall be responsible for maintaining the other telecommunications facilities that it leases to CNC China based on the latter's operational requirements, CNC China shall pay to China Netcom Group the relevant maintenance service charges which shall be determined with reference to market rates. Where there are no market rates, the maintenance charges shall be agreed between the parties and determined on a cost-plus basis. The net rental charges and service charges due to China Netcom Group under the Telecommunications Facilities Leasing Agreement will be settled between CNC China and China Netcom Group on a quarterly basis.

This agreement was renewed on November 6, 2007. The renewal agreement is effective from January 1, 2008 for a term of 3 years.

Continuing Connected Transactions Relating to China Netcom System Integration

Information and Communications Technology Agreement

Pursuant to Information and Communications Technology Agreement:

(i) China Netcom System Integration (and its subsidiaries) provides information and communications technology services to China Netcom Group (and its subsidiaries (other than the Group)), which include system integration services, software development services, operational maintenance services, consultancy services, equipment leasing-related services and product sales and distribution related services.

(ii) China Netcom System Integration will also subcontract services ancillary to the provision of information and communications technology services, namely the system installation and configuration services, to the subsidiaries and branches of China Netcom Group in China Netcom Group's southern service regions in the PRC.

The charges payable for the services provided under the Information and Communications Technology Agreement are determined with reference to the following pricing principles and limits:

(i) the government fixed price;

(ii) where there is no government fixed price but a government guidance price exists, the government guidance price; or

(iii) where there is neither a government price nor a government guidance price, the market price.

In relation to the charges payable for the services provided under the Information and Communications Technology Agreement that are to be determined with reference to the market price:

(a) If the value of any single item of system installation and configuration services provided by China Netcom Group (and its subsidiaries) to China Netcom System Integration (and its subsidiaries) exceeds RMB0.3 million, the award of such services will be subject to tender; or

(b) If the value of any single item of system integration, software development, operational maintenance, consultancy and equipment leasing-related services exceeds RMB0.5 million, or where the value of any single item of product sales and distribution related services exceeds RMB2 million, the award of such services will be subject to tender.

This agreement was renewed on November 6, 2007. The renewal agreement is effective from January 1, 2008 for a term of 3 years.

In the opinion of the independent non-executive directors of the Company, the Continuing Connected Transactions were entered into by the Group:

(a) in the ordinary and usual course of its business;

(b) either on normal commercial terms or, where there are no sufficient comparables, on terms no less favourable than the terms the Company could have obtained from an independent third party; and

(c) in accordance with the relevant agreements governing such transactions and on terms that are fair and reasonable and in the interests of the shareholders of the Company as a whole.

The board of directors has received a letter from the auditors of the Company stating that the Continuing Connected Transactions:

(A) have received the approval of the Company's board of directors;

(B) were carried out in accordance with the pricing policy as stated on pages 58 to 64 of this report;

(C) have been entered into in accordance with the relevant agreements governing the Continuing Connected Transactions; and

(D) have not exceeded their respective upper limits set by The Stock Exchange of Hong Kong Limited ("**Hong Kong Stock Exchange**") for the financial year ended December 31, 2007.

Directors

The directors for this financial year are:

Executive Directors

Zhang Chunjiang	
Zuo Xunsheng	
Li Jianguo	(appointed on July 12, 2007)
Zhang Xiaotie	
Li Fushen	(appointed on January 15, 2007)
Miao Jianhua	(resigned on July 12, 2007)

Non-executive Directors

Tian Suning	(resigned on July 12, 2007)
Li Liming	(resigned on January 15, 2007)
Yan Yixun	
Cesareo Alierta Izuel	(appointed on December 5, 2007)
José María Álvarez-Pallete	
Mauricio Sartorius	(resigned on December 5, 2007)

Independent Non-executive Directors

John Lawson Thornton
Victor Cha Mou Zing
Qian Yingyi
Hou Ziqiang
Timpson Chung Shui Ming

Alternate Director

Hong Chen Jin (alternate to Mr. Cesareo Alierta Izuel and Mr. José María Álvarez-Pallete)	(appointed as alternate to Mr. Cesareo Alierta Izuel on December 5, 2007; and ceased to be the alternate to Mr. Mauricio Sartorius since December 5, 2007).

In accordance with Article 99 of the Company's Articles of Association, Mr. Zhang Chunjiang, Mr. Zhang Xiaotie, Mr. John Lawson Thornton and Mr. Victor Cha Mou Zing will retire by rotation at the forthcoming annual general meeting of the Company and they (except Mr. Victor Cha Mou Zing), being eligible, offer themselves for re-election. In accordance with Article 103 of the Company's Articles of Association, Ms. Li Jianguo and Mr. Cesareo Alierta Izuel will also retire at the forthcoming annual general meeting and, being eligible, offer themselves for re-election.

The biographical details of the directors proposed for re-election at the forthcoming annual general meeting ("**Directors for Re-election**") are set out on pages 16 to 20. Except as disclosed in such biographical details, the Directors for Re-election have not held any other directorships in any listed public companies in the last three years. Further, except as noted in the biographical details, none of the Directors for Re-election is connected with any directors, senior management or substantial or controlling shareholders of the Company and, except for the share options granted to the Directors for Re-election (other than Ms. Li Jianguo, Mr. Cesareo Alierta Izue and Mr. John Lawson Thornton) as set out in the paragraph "Share option scheme" below, none of them has any interests in the shares of the Company within the meaning of Part XV of the Securities and Futures Ordinance ("**SFO**").

The service contracts for Mr. Zhang Chunjiang, Ms. Li Jianguo and Mr. Zhang Xiaotie do not provide for a specified length of services. Mr. Cesareo Alierta Izuel and Mr. John Lawson Thornton have not entered into any service contract with the Company. Each of the Directors for Re-election will be subject to retirement by rotation and re-election at annual general meetings of the Company at least every three years. Each of such directors (other than executive directors and all non-executive directors nominated by China Netcom Group) is entitled to an annual director's fee of HK$200,000 as proposed by the board of directors and approved by the shareholders of the Company at the extraordinary general meeting held on February 14, 2007. Director's fees are payable on a time pro-rata basis for any non full year's service. Such directors shall also be entitled to an additional fee of HK$10,000 for each Board meeting which such directors attend. In addition, Mr. John Lawson Thornton is entitled to an additional annual fee of HK$120,000 as the Chairman of the Nominating and Corporate Governance Committee and a member of the Compensation Committee. Such directors shall also be entitled to an additional fee of HK$5,000 for each committee meeting which such directors attend.

None of the Directors for Re-election has an unexpired service contract which is not determinable by the Company or any of its subsidiaries within one year without payment of compensation, other than under normal statutory obligations.

Save as disclosed herein, there are no other matters relating to the re-election of the Directors for Re-election that need to be brought to the attention of the shareholders of the Company nor is there any information that needs to be disclosed pursuant to any of the requirements of Rule 13.51(2) of the Listing Rules.

Directors' interests in contracts

No contract of significance to which the Company, its holding company, or any of its fellow subsidiaries or subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Directors' interest in competing businesses

China Netcom Group is engaged in fixed-line telecommunications business and other related businesses in the PRC and Asia-Pacific region which are similar to that of the Company. The executive directors of the Company also hold executive positions with China Netcom Group. On September 6, 2004, China Netcom Group, the Company and CNC China entered into a non-competition agreement, under which China Netcom Group undertakes not to compete with the Company in the businesses as prescribed in the agreement without the Company's prior written consent.

Mr. Zhang Chunjiang, the Company's executive director, have served as director of PCCW Limited since April 1, 2005. Mr. Zuo Xunsheng and Mr. Li Fushen, the Company's executive directors, have served as directors of PCCW Limited since July 9, 2007. Mr. José María Álvarez-Pallete is a director of the following companies: Telefónica S.A., Telefónica Internacional, S.A., Telecomunicacoes de Sao Paulo, S.A. (listed on the Stock Exchanges of Sao Paulo and New York), Compañía de Telecomunicaciones de Chile, S.A. (listed on the Stock Exchanges of Santiago de Chile and New York), Telefónica de España S.A., Telefónica Móviles España S.A., Telefónica Datacorp, S.A., Telefónica de Argentina, S.A. (listed on the Stock Exchanges of Buenos Aires and New York), Telefónica de Perú S.A.A. (listed on the Stock Exchange of Lima), Colombia Telecomunicaciones, S.A. ESP, Telefónica Móviles Colombia, S.A., Telefónica Móviles México, S.A., Brasilcel, N.V., Allianca Atlantica Holding B.V. and Telefónica O2 Europe, plc. Mr. Cesareo Alierta Izuel is the director of Telefónica S.A., and has served as the Executive Chairman of Telefónica S.A. since July 2000, and he is the director of Telecom Italia (listed on the Stock Exchange of Milan). Ms. Hong Chen Jin has been an alternate director to both Mr. José María Álvarez-Pallete and Mr. Mauricio Sartorius since December 19, 2006 although she ceased to be the alternate director to Mr. Mauricio Sartorius since his resignation on December 5, 2007. She became the alternate director to Mr. Cesareo Alierta Izuel since December 5, 2007 and was appointed deputy general manager of the Asia Representative Office of Telefónica Internacional, S.A. in early 2005. Apart from the above, none of the directors of the Company is or was interested in any business, apart from the Company's business, that competes or competed or is or was likely to compete, either directly or indirectly, with the Company's business at any time during the 2007 financial year up to and including the date of this report.

Directors' and chief executive's interest and short positions in shares, underlying shares and debentures

Certain directors and the chief executive of the Company personally hold options to subscribe for ordinary shares of the Company. Details of such options are disclosed under the paragraph "Share option scheme" below. These share options were granted to the relevant directors and the chief executive pursuant to the terms of the share option scheme adopted by the Company.

Apart from those disclosed herein, as at December 31, 2007, none of the directors nor the chief executive of the Company had any interests or short positions in any of the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of the SFO) that is required to be recorded and kept in the register in accordance with section 352 of the SFO, or any interests required to be notified to the Company and the Hong Kong Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers ("**Model Code**").

Emolument policy

The emolument policy of the Company has always been operation-centred and performance-oriented, in order to provide the support for the achievement of the Company's strategic objectives and promote the Company's long-term development. Employees are remunerated with a combination of a fixed salary, a performance-based salary and a long-term incentive scheme in the form of a share option scheme for eligible employees, details of which can be found in the paragraph "Share option scheme" below.

The Company has established the Compensation Committee, which is responsible for making recommendations to the Board on the Company's emolument policy in relation to all directors, the chief executive officer and other senior management. The Compensation Committee, on behalf of the Board, determines the remuneration packages of executive directors and senior management, and makes recommendations to the Board on the remuneration of non-executive directors. In making such determination, the Compensation Committee considers factors such as salaries payable by comparable companies, the time commitment and responsibilities involved in the relevant position, employment conditions elsewhere in the group of companies to which the Company belongs and the desirability of performance-based remuneration with reference to corporate goals and objectives resolved by the Board from time to time. No director is involved in deciding his or her own remuneration.

Employee retirement benefits

Particulars of the employee retirement benefits of the Group are set out in note 4(s)(i) and note 15 to the financial statements.

Share option scheme

The shareholders of the Company passed a resolution on September 30, 2004 to approve and adopt the share option scheme (the "**Share Option Scheme**"). On December 6, 2005, the Board convened a meeting and made minor amendments to the Share Option Scheme. The shareholders of the Company passed a resolution at an extraordinary general meeting held on May 16, 2006 to approve certain changes to the rules of Share Option Scheme so that the benefits to the grantees under the Share Option Scheme are closely aligned to the performance of the Company and the individual grantees.

The main contents of the amended Share Option Scheme are as follows:

(a) Purpose of the Share Option Scheme

The purpose of the Share Option Scheme is to provide the Company with a means to incentivise its middle-to-senior management, to attract and retain talent and to encourage other eligible participants to enhance the value of the Company.

(b) Participants of the Share Option Scheme

The directors may invite any person belonging to any of the following classes of participants to take up options to subscribe for the ordinary shares of the Company:

(i) The directors (including executive directors and non-executive directors but not independent non-executive directors);

(ii) Members of the middle-to-senior management; and

(iii) Such class of "specialised professionals" identified by the Compensation Committee.

For the purpose of sub-paragraph (b)(iii) above, "specialised professionals" means such professionals or management staff or technical or marketing staff holding important positions that are important to the development of the Group's business. The Compensation Committee has the right to interpret "specialised professionals" and identify them.

(c) Maximum number of shares and effective options

(i) The maximum number of shares which may be allotted and issued upon the exercise of all outstanding options granted and yet to be exercised under the Share Option Scheme and any other share option scheme must not in aggregate exceed 30 per cent. of the shares of the Company then in issue.

(ii) The total number of shares which may be allotted and issued upon the exercise of all options to be granted under the Share Option Scheme must not in aggregate exceed 10 per cent. of the shares in issue immediately after the completion of the global offering of shares (and American depositary shares) of the Company in November 2004 (the "**General Scheme Limit**").

(iii) Subject to (c)(i) above, the Company may seek approval of the shareholders in general meeting to refresh the General Scheme Limit and may seek separate approval of the shareholders in general meeting to grant options beyond the General Scheme Limit.

(iv) "Effective Options" means the share options granted under the Share Option Scheme, irrespective of whether such options are exercisable in accordance with the relevant vesting schedule; and "Vesting Schedule" means the arrangement whereby options can be exercised by batch in accordance with the timetable pre-determined by the Share Option Scheme.

(d) As at the latest practicable date prior to the printing of this report, the total number of securities available for issue under the Share Option Scheme is 140,988,260, representing 2.11 per cent. of the issued share capital of the Company as at that date.

(e) Maximum entitlement of each participant

Unless otherwise approved by the shareholders in general meeting, the total number of shares issued and which may fall to be issued upon the exercise of the options granted under the Share Option Scheme (including both exercised or outstanding options) to any participant in any 12-month period shall not exceed 0.2 per cent. of the issued share capital of the Company on the date of grant.

(f) Minimum period for which an option must be held before it can be exercised

With respect to the share options granted prior to the listing of the Company's shares on the Hong Kong Stock Exchange, there is a minimum period of 18 months from the later of the date of grant or the date of the listing of the shares on the Hong Kong Stock Exchange before an option can be exercised; with respect to the share options granted after the listing of the Company's shares on the Hong Kong Stock Exchange, there is a minimum period of 24 months from the later of the date of grant or the date of the listing of the shares on the Hong Kong Stock Exchange before an option can be exercised.

(g) Period within which the shares must be taken up under an option

Any option shall lapse if not exercised within 6 years from the later of the date of grant or the date of the listing and commencement of trading of the shares on the Hong Kong Stock Exchange.

(h) The basis of determining the exercise price for shares

The exercise price is a price determined by the Board or the Compensation Committee but shall not be less than the highest of: (i) the closing price of the shares on the Hong Kong Stock Exchange on the date of grant; (ii) the average closing price of shares on the Hong Kong Stock Exchange for the five trading days immediately preceding the date of grant; and (iii) the nominal value of the shares.

(i) Consideration

No consideration is payable on acceptance of the grant of an option.

(j) The remaining life of the Share Option Scheme

Unless otherwise terminated by the Board of Directors in exercise of its powers in accordance with the rules governing the Share Option Scheme, the Share Option Scheme will remain in force for a period of 10 years commencing on the date on which the Share Option Scheme is adopted.

(k) Amendment to and termination of the Share Option Scheme

(i) The Board of the Company may amend any of the provisions of the Share Option Scheme and the terms of the options at any time.

(ii) Any alterations to the matters set out in the Listing Rules and alterations which are to the advantage of existing or future grantees of options shall only be made with the approval of shareholders at general meeting.

(iii) Any alterations to the terms and conditions of the Share Option Scheme which are of a material nature shall be approved by the shareholders of the Company at general meeting, except where the alterations take effect automatically under the existing terms of the Share Option Scheme.

(iv) Any change to the authority of the Board in relation to alteration of the terms of the Share Option Scheme shall be approved by shareholders of the Company at general meeting. The amended Share Option Scheme or the terms thereof shall comply with the relevant requirements of the Listing Rules.

(v) During the effective term of the Share Option Scheme, the Board may at any time terminate the Share Option Scheme or decide not to grant any options under the Share Option Scheme, and in such event the options granted under this Scheme (to the extent not already exercised) may still be exercisable pursuant to the rules of the Share Option Scheme or may be cancelled by the Board pursuant to rules thereof.

(vi) The Share Option Scheme will be terminated upon the expiry of its effective term and any new share option scheme to be adopted by the Board shall be approved by the shareholders of the Company at general meeting.

As at December 31, 2007, the directors, chief executive and employees of the Company had the following personal interests in options to subscribe for shares of the Company granted under the Share Option Scheme.

	No. of shares involved in the options outstanding at the beginning of the year	No. of shares involved in the options outstanding at the end of the year	Date of the grant of the options	No of shares involved in the options granted during the year	No. of shares involved in the options cancelled during the year	No. of shares acquired on exercise of options during the year	Price per share payable for the exercise of the options
							(in HK$)
Directors							
Zhang Chunjiang	920,000	920,000	October 22, 2004	—	—	—	8.40
Zuo Xunsheng	480,000	480,000	October 22, 2004	—	—	—	8.40
Zhang Xiaotie	480,000	380,000	October 22, 2004	—	—	100,000	8.40
Li Fushen	480,000	480,000	October 22, 2004	—	—	—	8.40
Yan Yixun	354,000*	354,000	October 22, 2004	—	—	—	8.40
Employees and other persons granted with options after the date of listing of the Company's shares on the Hong Kong Stock Exchange	79,034,200	71,580,700	December 6, 2005	—	—	7,453,500	12.45
Employees and other persons granted with options before the date of listing of the Company's shares on the Hong Kong StocK Exchange	94,898,700	76,649,860	October 22, 2004	—	2,117,440	16,131,400	8.40
Total	176,646,900	150,844,560		—	2,117,440	23,684,900	

Notes:

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

(a) The total number of shares involved in the options outstanding represents 2.11 per cent. of the issued share capital of the Company as at the latest practicable date prior to the printing of this report.

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

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

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

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

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

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

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

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

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

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

(d) During the year ended December 31, 2007, no share option was granted by the Company under the Share Option Scheme.

Details of share options exercised during the period:

Period during which options were exercised	**Exercise price**	**Weighed average closing price per share immediately before dates of exercise of options**	**Proceeds received**	**Number of shares involved in the options**
	(HK$)	*(HK$)*	*(HK$)*	
From January 1, 2007 to December 31, 2007	8.40	22.23	136,343,760	16,231,400
	12.45	23.92	92,796,075	7,453,500

Apart from the foregoing, at no time during the year ended December 31, 2007 was the Company, any of its holding companies or subsidiaries or fellow subsidiaries, a party for any arrangement to enable the directors or senior management of the Company or any of their spouses or children under eighteen years of age to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

Report of the Directors

Substantial shareholders' and other persons' interests and short positions in shares and underlying shares

The Company has been notified of the following interests in the Company's issued shares as at December 31, 2007 amounting to 5 per cent. or more of the ordinary shares in issue:

	Capacity	Number of ordinary shares held	Percentage of total issued shares
China Network Communications Group Corporation	Interest of controlled corporations	4,945,148,000[(1)(2)]	74.09%
China Netcom Group Corporation (BVI) Limited	Beneficial owner	4,647,449,014	
	Interest of controlled corporations	1	
	Trustee	297,698,985	
	Total	4,945,148,000[(1)(2)(3)]	74.09%
AllianceBernstein L.P.	Interest of controlled corporations	41,514,400	
	Investment manager	357,326,792	
	Total	398,841,192	5.98%
Telefónica Internacional, S.A.U.	Beneficial owner	333,971,305[(3)]	5.00%

Notes:

(1) China Network Communications Group Corporation ("**China Netcom Group**") beneficially owns 4,647,449,014 shares held by its wholly owned subsidiary, China Netcom Group Corporation (BVI) Limited ("**CNC BVI**") and 1 share held by CNC Cayman, Limited, a wholly owned subsidiary of CNC BVI. The percentage of total issued share capital beneficially held by China Netcom Group is 69.63%.

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

(3) On January 18, 2008, the Company was informed by the beneficiary owners of 148,015,436 shares of the Company which were held in trust with CNC BVI that they have entered into a share purchase agreement with Telefónica Internacional, S.A. to transfer an aggregate of 148,015,436 shares to Telefónica Internacional, S.A. or its related entities. Upon the completion of this transaction, the shares held by Telefónica Internacional, S.A. and its associates will reach 7.22% of the outstanding shares of the Company.

Apart from the foregoing, as at December 31, 2007 no person or corporation had any interest in 5 per cent. or more of or any short position in the issued share capital of the Company as recorded in the registers required to be kept under section 336 of the SFO.

Public Float

As at the date of this report, the Company has maintained the prescribed public float of not less than 23 per cent of the issued share capital of the Company pursuant to the Listing Rules and as agreed with the Stock Exchange, based on the information that is publicly available to the Company and within the knowledge of the directors of the Company.

Auditors

A resolution for the reappointment of PricewaterhouseCoopers as auditors of the Company shall be proposed at the forthcoming annual general meeting.

By Order of the Board

Zhang Chunjiang
Chairman

Hong Kong, March 25, 2008

Notice is hereby given that the Annual General Meeting of China Netcom Group Corporation (Hong Kong) Limited (the "**Company**") will be held on May 22, 2008 at 3:00 p.m. in The Ballroom, Island Shangri-la, Hong Kong for the following purposes:

As Ordinary Business:

1. To receive and consider the financial statements for the year ended December 31, 2007 and the Reports of the Directors and the Auditors.

2. To declare a final dividend for the year ended December 31, 2007.

3. To elect Directors.

4. To re-appoint Auditors and authorise the Directors to fix their remuneration.

And as Special Business, to consider and, if thought fit, to pass the following as ordinary resolutions:

ORDINARY RESOLUTIONS

5. "**THAT**:

   (a) subject to paragraph (b) below, the exercise by the Directors during the Relevant Period of all the powers of the Company to purchase shares of US$0.04 each in the capital of the Company including any form of depositary receipt representing the right to receive such shares ("Shares") be and is hereby generally and unconditionally approved;

   (b) the aggregate nominal amount of Shares which may be purchased on The Stock Exchange of Hong Kong Limited or any other stock exchange on which securities of the Company may be listed and which is recognised for this purpose by the Securities and Futures Commission of Hong Kong and The Stock Exchange of Hong Kong Limited pursuant to the approval in paragraph (a) above shall not exceed or represent more than 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution, and the said approval shall be limited accordingly;

   (c) for the purpose of this Resolution "Relevant Period" means the period from the passing of this Resolution until whichever is the earlier of:

      (1) the conclusion of the next annual general meeting of the Company;

      (2) the expiration of the period within which the next annual general meeting of the Company is required by law to be held; and

      (3) the revocation or variation of the authority given under this Resolution by an ordinary resolution of the shareholders of the Company at a general meeting."

6. "**THAT** a general mandate be and is hereby unconditionally given to the Directors to exercise full powers of the Company to allot, issue and deal with additional shares in the Company (including the making and granting of offers, agreements and options which might require shares to be allotted, whether during the continuance of such mandate or thereafter) provided that, otherwise than pursuant to (i) a rights issue where shares are offered to shareholders on a fixed record date in proportion to their then holdings of shares; (ii) the exercise of options granted under any share option scheme adopted by the Company; or (iii) any scrip dividend or similar arrangement providing for the allotment of shares in lieu of the whole or part of a dividend in accordance with the Articles of Association of the Company, the aggregate nominal amount of the shares allotted shall not exceed the aggregate of:

   (a) 20 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution, plus

(b) (if the Directors are so authorised by a separate ordinary resolution of the shareholders of the Company) the nominal amount of the share capital of the Company repurchased by the Company subsequent to the passing of this Resolution (up to a maximum equivalent to 10 per cent. of the aggregate nominal amount of the share capital of the Company in issue at the date of passing this Resolution).

Such mandate shall expire at the earlier of:

(1) the conclusion of the next annual general meeting of the Company;

(2) the expiration of the period within which the next annual general meeting of the Company is required by law to be held; and

(3) the date of any revocation or variation of the mandate given under this Resolution by an ordinary resolution of the shareholders of the Company at a general meeting."

7. "**THAT** the Directors be and they are hereby authorised to exercise the powers of the Company referred to in the resolution set out in item 6 in the notice of this meeting in respect of the share capital of the Company referred to in paragraph (b) of such resolution."

By Order of the Board
China Netcom Group Corporation (Hong Kong) Limited
Huo Haifeng **Mok Kam Wan**
Joint Company Secretaries

Hong Kong, April 7, 2008

Notes:

1. Any member entitled to attend and vote at the above Meeting is entitled to appoint one or more proxies to attend and, on a poll, vote in his stead. A proxy need not be a member of the Company.

2. In order to be valid, a form of proxy together with the power of attorney or other authority (if any) under which it is signed, or a notarially certified copy thereof, must be deposited at the Company's registered office at Room 6701, The Center, 99 Queen's Road Central, Hong Kong at least 48 hours before the time for holding the above Meeting. Completion and return of a form of proxy will not preclude a member from attending and voting in person if he is subsequently able to be present.

3. The Board of Directors has recommended a final dividend for the year ended December 31, 2007 of HK$0.592 per share and, if such dividend is declared by the members passing Resolution 2, it is expected to be paid on or about June 12, 2008 to those shareholders whose names appear on the Company's register of members on May 22, 2008.

4. The register of members of the Company will be closed from May 19, 2008 to May 22, 2008 (both days inclusive), during which period no transfer of shares in the Company will be effected. In order to qualify for the proposed final dividend, all transfers, accompanied by the relevant share certificates, must be lodged with the Company's registrar, Computershare Hong Kong Investor Services Limited, Rooms 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wan Chai, Hong Kong, not later than 4:30 p.m. on May 16, 2008.

5. Concerning Resolution 5 above, the Directors wish to state that they will exercise the powers conferred thereby to repurchase shares of the Company in circumstances which they deem appropriate for the benefit of the shareholders. The Explanatory Statement containing the information necessary to enable the shareholders to make an informed decision on whether to vote for or against the resolution to approve the repurchase by the Company of its own shares, as required by the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited will be set out in a separate letter from the Company to be enclosed with the 2007 Annual Report.

PRICEWATERHOUSECOOPERS

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To the shareholders of China Netcom Group Corporation (Hong Kong) Limited
(incorporated in Hong Kong with limited liability)

We have audited the consolidated financial statements of China Netcom Group Corporation (Hong Kong) Limited (the "Company") and its subsidiaries (together, the "Group") set out on pages 77 to 154, which comprise the consolidated and company balance sheets as at 31 December 2007, and the consolidated income statement, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Directors' responsibility for the financial statements

The directors of the Company are responsible for the preparation and the true and fair presentation of these consolidated financial statements in accordance with Hong Kong Financial Reporting Standards issued by the Hong Kong Institute of Certified Public Accountants, and the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit and to report our opinion solely to you, as a body, in accordance with section 141 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2007 and of the Group's profit and cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards and have been properly prepared in accordance with the Hong Kong Companies Ordinance.

PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, March 25, 2008

Consolidated Income Statement

For the year ended December 31, 2007

	Note	Year ended December 31	
		2007	2006
		RMB million	RMB million Restated Note 2
Continuing operations:			
Revenues	7	**84,005**	84,194
Operating expenses			
Depreciation and amortisation		**(25,495)**	(24,913)
Networks, operations and support		**(14,145)**	(13,344)
Staff costs	15	**(12,223)**	(11,849)
Selling, general and administrative		**(10,615)**	(12,607)
Other operating expenses		**(4,261)**	(1,930)
Total of operating expenses	8	**(66,739)**	(64,643)
Other income	9	**1,221**	621
Interest income		**113**	135
Deficit on revaluation of fixed assets	21(c)	**—**	(1,335)
Profit from operations		**18,600**	18,972
Finance costs	10	**(3,333)**	(3,767)
Profit before taxation		**15,267**	15,205
Taxation	11	**(3,796)**	(3,727)
Profit for the year from continuing operations		**11,471**	11,478
Discontinued operations:			
Profit for the year from discontinued operations	26	**624**	1,487
Profit for the year		**12,095**	12,965
Dividends proposed after the balance sheet date	13	**3,700**	3,695
Earnings per share for profit from continuing operations attributable to shareholders of the Company for the year			
Basic earnings per share	14	**RMB 1.72**	RMB 1.74
Diluted earnings per share	14	**RMB 1.70**	RMB 1.72

Consolidated Income Statement *(continued)*

For the year ended December 31, 2007

	Note	2007	2006
		Year ended December 31	
		RMB million	RMB million Restated Note 2
Earnings per share for profit from discontinued operations attributable to shareholders of the Company for the year			
Basic earnings per share	14	**RMB 0.09**	RMB 0.22
Diluted earnings per share	14	**RMB 0.09**	RMB 0.22
Earnings per share from operations attributable to shareholders of the Company for the year			
Basic earnings per share	14	**RMB 1.81**	RMB 1.96
Diluted earnings per share	14	**RMB 1.79**	RMB 1.94

The notes on pages 86 to 154 are an integral part of these consolidated financial statements.

Consolidated Balance Sheet

As at December 31, 2007

	Note	2007	2006
		As at December 31	
		RMB million	RMB million Restated Note 2
Assets			
Current assets			
Cash and bank deposits	17	**5,395**	7,728
Accounts receivable	18	**8,458**	8,283
Inventories and consumables	19	**287**	416
Prepayments, other receivables and other current assets	20	**1,021**	1,441
Due from holding companies and fellow subsidiaries	31	**347**	358
Total current assets		**15,508**	18,226
Non-current assets			
Fixed assets	21	**156,948**	168,141
Construction in progress	22	**3,990**	6,335
Lease prepayments	23	**2,494**	2,364
Intangible assets	24	**1,552**	1,591
Deferred tax assets	34	**2,693**	3,459
Other non-current assets	25	**3,243**	3,966
Total non-current assets		**170,920**	185,856
Total assets		**186,428**	204,082

The notes on pages 86 to 154 are an integral part of these consolidated financial statements.

Consolidated Balance Sheet *(continued)*

As at December 31, 2007

	Note	2007	2006
		As at December 31	
		RMB million	RMB million Restated Note 2
Liabilities and equity			
Current liabilities			
Accounts payable	28	**15,639**	17,661
Accruals and other payables	29	**2,950**	3,074
Short term commercial paper	30(a)(i)	**20,000**	9,811
Short term bank loans	30(a)(ii)	**11,850**	30,980
Current portion of long term bank and other loans	30(b)	**5,322**	7,304
Due to holding companies and fellow subsidiaries	31	**4,598**	7,505
Current portion of deferred revenues	32	**7,103**	7,733
Current portion of provisions	33	**3,381**	3,736
Taxation payable		**3,750**	3,029
Total current liabilities		**74,593**	90,833
Net current liabilities		**(59,085)**	(72,607)
Total assets less current liabilities		**111,835**	113,249
Non-current liabilities			
Long term bank and other loans	30(b)	**14,425**	23,219
Corporate bonds	30(c)	**2,000**	—
Due to holding companies and fellow subsidiaries	31	**6,169**	5,880
Deferred revenues	32	**4,314**	6,198
Provisions	33	**2,007**	2,586
Deferred tax liabilities	34	**856**	1,156
Other non-current liabilities		**12**	16
Total non-current liabilities		**29,783**	39,055
Total liabilities		**104,376**	129,888
Financed by:			
Share capital	35	**2,206**	2,199
Reserves		**79,846**	71,995
Shareholders' equity		**82,052**	74,194
Total liabilities and equity		**186,428**	204,082

The notes on pages 86 to 154 are an integral part of these consolidated financial statements.

Zuo Xunsheng	**Li Fushen**
Director	*Director*

Balance Sheet - Company

As at December 31, 2007

	Note	As at December 31 2007 RMB million	2006 RMB million
Assets			
Current assets			
Cash and bank deposits	17	**113**	1,772
Due from subsidiaries	27	**10,490**	9,411
Prepayments, other receivables and other current assets	20	**16**	268
Total current assets		**10,619**	11,451
Non-current assets			
Investments in subsidiaries	27	**71,000**	62,937
Total assets		**81,619**	74,388
Liabilities and equity			
Current liabilities			
Accruals and other payables	29	**46**	136
Due to subsidiaries	27	**14,271**	12,754
Total current Liabilities		**14,317**	12,890
Net current liabilities		**(3,698)**	(1,439)
Total assets less current liabilities		**67,302**	61,498
Non-current liabilities			
Long term bank and other loans		**9**	—
Due to holding company and fellow subsidiaries	31(c)	**403**	—
Total non-current liabilities		**412**	—
Total liabilities		**14,729**	12,890
Financed by:			
Share capital	35	**2,206**	2,199
Reserves	37	**64,684**	59,299
Shareholders' equity		**66,890**	61,498
Total liabilities and equity		**81,619**	74,388

The notes on pages 86 to 154 are an integral part of these financial statements.

Consolidated Statement of Changes in Equity

For the year ended December 31, 2007

	Attributable to equity holders of the company							
	Share capital	Share premium	Capital reserve	Statutory reserve	Revaluation reserve	Other reserve	Retained earnings	Total equity
	RMB million (Note 35)	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million
Balance as at January 1, 2006	2,181	42,750	387	8,550	4,101	(5,203)	10,244	63,010
Adjustments for the acquisition (Note 2)	—	—	—	—	—	238	39	277
Balance at January 1, 2006, as restated	2,181	42,750	387	8,550	4,101	(4,965)	10,283	63,287
Transfer to statutory reserve (Note 12)	—	—	—	2,406	—	—	(2,406)	—
Appropriation to statutory reserve (Note 12)	—	—	—	855	—	—	(855)	—
Transfers to retained earnings in respect of depreciation differences on revalued assets	—	—	—	—	(1,933)	(51)	1,984	—
Revaluation surplus (Note 21)	—	—	—	—	1,071	—	—	1,071
Currency translation differences (i)	—	—	—	—	—	(79)	—	(79)
Movement of deferred tax recognised in equity (Note 34)	—	—	—	—	(353)	—	—	(353)
Net income/(expense) recognised directly in equity	—	—	—	3,261	(1,215)	(130)	(1,277)	639
Profit for the year from continuing operations	—	—	—	—	—	—	11,478	11,478
Profit for the year from discontinued operations	—	—	—	—	—	—	1,487	1,487
Total income recognised for 2006	—	—	—	3,261	(1,215)	(130)	11,688	13,604
Dividends for 2005 distributed during the year (Note13)	—	—	—	—	—	—	(3,196)	(3,196)
Exercise of share options (Note 35)	18	545	(73)	—	—	—	—	490
Distributions to owners	—	—	—	—	—	—	(66)	(66)
Share-based payments	—	—	75	—	—	—	—	75
Balance as at December 31, 2006	2,199	43,295	389	11,811	2,886	(5,095)	18,709	74,194

(i)Including accumulated currency translation differences realized upon disposal of ANC Group amounting to RMB29 million.

The notes on pages 86 to 154 are an integral part of these consolidated financial statements.

	Attributable to equity holders of the company							
	Share capital	Share premium	Capital reserve	Statutory reserve	Revaluation reserve	Other reserve	Retained earnings	Total equity
	RMB million (Note 35)	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million
Balance as at January 1, 2007	2,199	43,295	389	11,811	2,886	(5,095)	18,709	74,194
Transfer to statutory reserve (Note 12)	—	—	—	1,517	—	—	(1,517)	—
Appropriation to statutory reserve (Note 12)	—	—	—	868	—	—	(868)	—
Transfers to retained earnings in respect of depreciation differences on revalued assets	—	—	—	—	(2,031)	(104)	2,135	—
Transfers to retained earnings in respect of revaluation reserve relating to disposal of Guangdong and Shanghai branches	—	—	—	—	(69)	20	49	—
Currency translation differences	—	—	—	—	—	(15)	—	(15)
Movement of deferred tax recognised in equity (Note 34)	—	—	—	—	111	(664)	—	(553)
Net income/(expense) recognised directly in equity	—	—	—	2,385	(1,989)	(763)	(201)	(568)
Profit for the year from continuing operations	—	—	—	—	—	—	11,471	11,471
Profit for the year from discontinued operations	—	—	—	—	—	—	624	624
Total income recognised for 2007	—	—	—	2,385	(1,989)	(763)	11,894	11,527
Dividend related to 2006 distributed during the year (Note 13)	—	—	—	—	—	—	(3,600)	(3,600)
Distributions to owners	—	—	—	—	—	—	(48)	(48)
Exercise of share options (Note 35)	7	243	(31)	—	—	—	—	219
Consideration for the acquisition (Note 1)	—	—	—	—	—	(299)	—	(299)
Share-based payments	—	—	59	—	—	—	—	59
Balance as at December 31, 2007	2,206	43,538	417	14,196	897	(6,157)	26,955	82,052

The notes on pages 86 to 154 are an integral part of these consolidated financial statement.

Consolidated Statement of Cash Flow

For the year ended December 31, 2007

	Note	2007	2006
		Year ended December 31	
		RMB million	RMB million Restated Note 2
Cash flows from operating activities			
Net cash inflows from operations	38(a)	**39,309**	39,156
Interest received		**113**	136
Interest paid		**(2,856)**	(3,564)
Profits tax paid		**(4,107)**	(3,678)
Cash inflow from operating activities of continuing operations		**32,459**	32,050
Cash inflow from operating activities of discontinued operations	26	**388**	2,085
Net cash inflow from operating activities		**32,847**	34,135
Cash flows from investing activities			
Purchase of fixed assets and construction in progress		**(20,488)**	(24,064)
Prepayments for leased network capacity		**—**	(318)
Prepayments for leased land		**(196)**	(178)
Sale of fixed assets		**65**	127
Net decrease in time deposits with maturity over three months		**14**	7
Other income		**1,467**	375
Cash outflow from investing activities of continuing operations		**(19,138)**	(24,051)
Cash inflow/(outflow) from investing activities of discontinued operations	26	**3,103**	(921)
Net cash outflow from investing activities		**(16,035)**	(24,972)

For the year ended December 31, 2007

	Note	Year ended December 31 2007 RMB million	2006 RMB million Restated Note 2
Cash flows from financing activities			
New bank loans and other loans		**66,396**	89,002
Issue of short-term commercial paper		**20,000**	9,676
Issue of corporate bonds		**2,000**	—
Repayment of commercial paper		**(9,676)**	—
Repayment of bank loans		**(92,390)**	(98,512)
Capital element of finance lease payments		**(890)**	(1,347)
Payment of prior years distribution to owner		**(1,180)**	(630)
Payment to ultimate holding company for the acquisition of Beijing P&D Institute		**(299)**	—
Payment to ultimate holding company for the acquisition of New Horizon (Note 1)		**(1,960)**	(1,960)
Dividend payment		**(3,600)**	(3,196)
Loans from fellow subsidiaries and holding company		**2,249**	—
Issue of shares upon exercise of share options		**219**	490
Cash outflow from financing activities of continuing operations		**(19,131)**	(6,477)
Cash inflow from financing activities of discontinued operations	26	**—**	—
Net cash outflow from financing activities		**(19,131)**	(6,477)
Cash flows from continuing operations		**(5,810)**	1,522
Cash flows from discontinued operations		**3,491**	1,164
Increase/(decrease) in cash and cash equivalents		**(2,319)**	2,686
Cash and cash equivalents at beginning of year		**7,623**	4,937
Cash and cash equivalents at end of year	17	**5,304**	7,623

The notes on pages 86 to 154 are an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

1 The Group and its principal activities

Background of the Group

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

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

Pursuant to a resolution passed at the extraordinary general meeting of the shareholders on October 25, 2005, the Company acquired the principal telecommunications operations, assets and liabilities in the four Northern provinces/autonomous region, namely Shanxi Province, Neimenggu Autonomous Region, Jilin Province and Heilongjiang Province from China Netcom Group (the "Acquisition of New Horizon"). The consideration for the Acquisition of New Horizon was determined at RMB12,800 million. The consideration consists of an initial cash payment of RMB3,000 million and deferred payments of RMB9,800 million. The deferred payments will be settled in half-yearly installments over five years. The interest charged on the deferred payments is to be calculated at 5.265% per annum.

Following the Listing Reorganisation and the Acquisition of New Horizon, the Company and its subsidiaries (the "Group") is the dominant provider of fixed line voice and value-added services, broadband and other internet-related services, information communications technology services, business and data communications services and advertising and media services in ten northern provinces, municipalities and autonomous region in PRC, namely Beijing Municipality, Tianjin Municipality, Hebei Province, Liaoning Province, Shandong Province, Henan Province, Shanxi Province, Neimenggu Autonomous Region, Jilin Province, and Heilongjiang Province. The Group also provided telecommunications services to selected business and residential customers in two southern municipality and province, namely Shanghai Municipality and Guangdong Province in the PRC.

On June 2, 2006, the Group entered into an agreement with third party buyers to dispose of its entire interest in the Asia Netcom Corporation Limited ("ANC Group") for an aggregate cash consideration of US$168.84 million, at fair value determined by both parties. The transaction was completed on August 22, 2006. For detailed information, please refer to note 26.

On January 15, 2007, the Company's wholly owned subsidiary, China Netcom (Group) Company Limited ("CNC China"), entered into an assets transfer agreement with its ultimate holding Company, China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality branches ("Guangdong and Shanghai Branches") in the PRC for consideration of RMB3.5 billion. On February 14, 2007, the independent shareholders passed an ordinary resolution to approve the disposal. The disposal was completed on February 28, 2007 upon the approval granted from the Ministry of Information Industry ("MII"). After the disposal of the Guangdong and Shanghai branches the Group only provides telecommunications operations in the ten northern provinces, municipalities and autonomous region. For detailed information, please refer to note 26.

On December 5, 2007, China Netcom Group System Integration Limited Corporation ("System Integration Corporation"), a wholly-owned subsidiary of CNC China, entered into an Equity Interest Transfer Agreement with China Netcom Group Beijing Communications Corporation, pursuant to which System Integration Corporation agreed to acquire the entire equity interest of Beijing Telecommunications Planning and Designing Institute Corporation Limited ("Beijing Telecom P&D Institute") from China Netcom Group Beijing Communications Corporation for a total consideration of RMB298.9 million. The consideration was paid through a one-off cash payment. The acquisition was registered with Beijing Property Transaction Administrative House and the ownership was transferred on December 31, 2007. Prior to the acquisition, Beijing Telecom P&D Institute was a wholly owned subsidiary of China Netcom Group Beijing Communications Corporation, which is a wholly owned subsidiary of China Netcom Group. For detailed information, please refer to note 2.

1 The Group and its principal activities *(continued)*

Background of the Group *(continued)*

Currently, the Group's principal services consist of:

- Fixed line voice and value-added services, comprising:
  - (a) Local, domestic long distance and international long distance services;
  - (b) Value-added services, including caller identity, personalized ring etc.; and
  - (c) Interconnection services provided to other domestic telecommunications service providers including the fellow subsidiaries owned by China Netcom Group operating outside the ten service regions;
- Broadband services and other Internet-related services;
- Information Communications Technology Services, including system integration, software services, outsourcing services, professional consulting services, professional services related with network information and disaster recovery, and other integrated solutions to client based on information and communications industry;
- Business and data communications services, including managed data services and leased line services; and
- Advertising and media services.

2 Basis of presentation

The financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS"), Hong Kong Accounting Standards ("HKAS") and interpretations issued by the Hong Kong Institute of Certified Public Accountants (''HKICPA''). They have also been prepared in accordance with the disclosure requirements of the Companies Ordinance and Rules Governing the Listing Securities on The Stock Exchange of Hong Kong Limited. They have been prepared under the historical cost convention modified by the revaluation of certain fixed assets as explained in the accounting policies in Note 4 below, and on a going concern basis.

A significant percentage of the Group's funding requirements is achieved through short term borrowings. Consequently, the balance sheet indicates a significant working capital deficit. In the past, a substantial portion of the Group's short term borrowings have been rolled over upon maturity. In addition, on April 30, 2007 and September 18, 2007, the Group issued commercial paper to raise additional funding of total RMB20 billion. On June 8, 2007, the Group issued corporate bonds to raise additional funding of RMB2 billion. Based on the Group's history of obtaining financing, its relationship with its bankers and its operating performance, the board of directors considers that the Group will continue to be able to roll over such short term financing, or will be able to obtain sufficient alternative sources of financing to enable it to operate and meet its liabilities as and when they fall due.

On June 2, 2006, the Group entered into an agreement with third party buyers to dispose of the entire interests in the ANC Group and the disposal was completed on August 22, 2006. On January 15, 2007, CNC China entered into an assets transfer agreement with China Netcom Group to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong and Shanghai branches in the PRC and the disposal was completed on February 28, 2007. In accordance with HKFRS 5 "Non-current assets held for sale and discontinued operations" issued by the HKICPA, the results and cash flows of the operations of the ANC Group and the Guangdong and Shanghai branches have been presented as discontinued operations. The 2006 comparative figures in the income statement and statement of cash flow were restated to reflect the disposal of Guangdong and Shanghai branches accordingly. For detailed information, please refer to note 26.

2 Basis of presentation *(continued)*

On December 5, 2007, System Integration Corporation entered into an Equity Interest Transfer Agreement with China Netcom Beijing Communications Corporation, pursuant to which System Integration Corporation agreed to acquire the entire equity interest of Beijing Telecom P&D Institute from China Netcom Group Beijing Communications Corporation. Before the acquisition, Beijing Telecom P&D Institute was a wholly owned subsidiary of China Netcom Group Beijing Communications Corporation, which is a wholly owned subsidiary of China Netcom Group. Since China Netcom Group is the ultimate holding company of the Group, the acquisition is a business combination under common control. Therefore, the Group accounted for this acquisition using the pooling of interest method according to Accounting Guideline No. 5 - Merger Accounting for Common Control Transactions ("AG 5"). The acquired businesses and assets are recorded at book value under HKFRS as if the businesses and assets of Beijing Telecom P&D Institute have been owned by the Group from the earliest comparative period presented. Accordingly, the financial information for year 2006 has been restated.

The impact of the restatement is summarized as below.

	Year ended December 31, 2006				
	Originally stated	**Disposal of Guangdong and Shanghai Branches**	**Acquisition of Beijing Telecom P&D Institute**	**Elimination of intercompany transactions**	**Restated**
	RMB million	RMB million	RMB million	RMB million	RMB million
Continuing operations:					
Revenues	86,921	(3,222)	165	330	84,194
Profit for the year from continuing operation	11,141	332	27	(22)	11,478
Discontinued operations :					
Profit/(loss) from discontinued operations	1,819	(332)	—	—	1,487
Profit for the year	12,960	—	27	(22)	12,965
Net cash inflow from operating activities	34,133	—	20	(18)	34,135
Net cash outflow from investing activities	(24,991)	—	(2)	21	(24,972)
Net cash outflow from financing activities	(6,447)	—	(30)	—	(6,477)
Total current assets at December 31, 2006	18,059	—	218	(51)	18,226
Total assets at December 31, 2006	203,835	—	318	(71)	204,082
Total current liabilities at December 31, 2006	90,802	—	80	(49)	90,833
Total liabilities at December 31, 2006	129,857	—	80	(49)	129,888
Shareholders' equity at December 31, 2006	73,978	—	238	(22)	74,194

3 Changes in accounting policies

(a) Standards, amendment and interpretations effective in 2007

HKFRS 7, 'Financial instruments: Disclosures', and the complementary amendment to HKAS 1, 'Presentation of financial statements - Capital disclosures', introduces new disclosures relating to financial instruments and does not have a material impact on the classification and valuation of the Group's financial instruments.

HK(IFRIC) - Int 8, 'Scope of HKFRS 2', requires consideration of transactions involving the issue of equity instruments, where the identifiable consideration received is less than the fair value of the equity instruments issued in order to establish whether or not they fall within the scope of HKFRS 2. This standard does not have any impact on the Group's financial statements.

HK(IFRIC) - Int 10, 'Interim financial reporting and impairment', prohibits the impairment losses recognised in an interim period on goodwill and investments in equity instruments and in financial assets carried at cost to be reversed at a subsequent balance sheet date. This standard does not have any impact on the Group's financial statements.

(b) Interpretation early adopted by the Group

HK(IFRIC) - Int 13, 'Customer loyalty programmes' (effective from July 1, 2008) was early adopted. HK(IFRIC) - Int 13 clarifies that where goods or services are sold together with a customer loyalty incentive (for example, loyalty points or free products), the arrangement is a multiple-element arrangement and the consideration receivable from the customer is allocated between the components of the arrangement using fair values. The Group only carried out a limited customer loyalty program in 2007 and thus it has no material impact on the Group's financial statements.

(c) Standards, amendments and interpretations effective in 2007 but not relevant

The following standards, amendments and interpretations to published standards are mandatory for accounting periods beginning on or after January 1 2007 but they are not relevant to the Group's operations:

- HK(IFRIC) - Int 7, 'Applying the restatement approach under HKAS 29, Financial reporting in hyper-inflationary economies';
- HK(IFRIC) - Int 9, 'Re-assessment of embedded derivatives'; and
- HKFRS 4 (revised) - 'Amendment to 'Financial guarantee contracts'.

(d) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after January 1, 2008 or later periods, but the Group has not early adopted them:

- HK(IFRIC) - Int 11, 'HKFRS 2 - Group and treasury share transactions'. HK(IFRIC) - Int 11 provides guidance on whether share-based transactions involving treasury shares or involving Group entities (for example, options over a parent's shares) should be accounted for as equity-settled or cash-settled share-based payment transactions in the stand-alone accounts of the parent and Group companies. This interpretation is not expected to have an impact on the Group's financial statements.
- HK(IFRIC) - Int 12, 'Service concession arrangement' (effective from January 1, 2008). IFRIC 12 applies to contractual arrangements whereby a private sector operator participates in the development, financing, operation and maintenance of infrastructure for public sector services. IFRIC 12, is not expected to have an impact on the Group' financial statements.

3 Changes in accounting policies *(continued)*

(d) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group *(continued)*

- HKAS 23 (Amendment), 'Borrowing costs' (effective from January 1, 2009). The amendment requires an entity to capitalise borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) as part of the cost of that asset. The option of immediately expensing those borrowing costs will be removed. Since the Group does not expense those borrowing cost under the current accounting policies, HKAS 23 (Amendment) has no impact to the Group.

- HKFRS 8, 'Operating segments ' (effective from January 1, 2009). HKFRS 8 replaces HKAS 14 and aligns segment reporting with the requirements of the US standard SFAS 131, 'Disclosures about segments of an enterprise and related information'. The new standard requires a 'management approach', under which segment information is presented on the same basis as that used for internal reporting purposes. The financial statements of the Group are presented on the same basis as that used for internal reporting purpose. Adoption of HKFRS 8 will not have significant impact to the Group.

- HK(IFRIC) - Int 14, 'HKAS 19 - The limit on a defined benefit asset, minimum funding requirements and their interaction' (effective from January 1, 2008). HK(IFRIC) - Int 14 provides guidance on assessing the limit in IAS/HKAS 19 on the amount of the surplus that can be recognised as an asset. It also explains how the pension asset or liability may be affected by a statutory or contractual minimum funding requirement. The Group will apply HK(IFRIC) - Int 14 from January 1, 2008, but it is not expected to have any impact on the Group's accounts.

4 Principal accounting policies

(a) Basis of consolidation

Acquisitions of businesses under common control are accounted for using merger accounting in accordance with AG 5 issued by HKICPA. The acquired assets are stated at carrying amounts as if the acquired assets have been held by the Company from the beginning of the earliest period presented.

When a subsidiary is disposed, the difference between the proceeds from the disposal of the subsidiary and its carrying amount as of the date of disposal, including the cumulative amount of any exchange differences that relates to the subsidiary recognised in equity is recognised in the income statement as the gain or loss on the disposal of the subsidiary.

All significant intercompany transactions and balances within the Group are eliminated on consolidation.

(b) Subsidiaries

Subsidiaries are those entities in which the Company, directly or indirectly, controls the composition of the board of directors, controls more than half the voting power or holds more than half of the issued share capital.

In the Company's balance sheet, the investments in subsidiaries are stated at cost less provision for impairment losses. The results of subsidiaries are accounted for by the Company on the basis of dividends received and receivables.

4 Principal accounting policies

(c) Revenue recognition

(i) The Group's revenues are recognised as follows:

- Revenues derived from local, domestic long distance (''DLD'') and international long distance (''ILD'') telephone usage, which vary depending on the day, the time of day, the distance and duration of the call and the tariffs, are recognised when the services are provided to customers.

- Monthly telephone service fees are recognised in the period during which the telephone services are provided to customers.

- Upfront connection and installation fees received are deferred and recognised over the expected customer relationship period of 10 years. With effect from July 1, 2001, no further upfront fees for connection were charged to customers.

- Revenues from the sale of prepaid calling cards are deferred and recognised as the cards are consumed by customers.

- Revenues from value-added communication services such as personalized ring and caller number display are recognised when the services are provided to customers.

- Revenues from the provision of broadband and other Internet-related services and managed data services are recognised when the services are provided to customers.

- Revenues from information communications technology services are recognised when goods are delivered to the customers (which generally coincides with the time when the customers have accepted the goods and the related risks and rewards of ownership have been transferred to the customers) or when services are rendered to the customers.

- Interconnection fees from domestic and foreign telecommunications operators are recognised when the services are rendered as measured by the minutes of traffic processed.

- Lease income from the leasing of lines and customer-end equipment is recognised over the term of the lease. Lease income from other domestic telecommunications operators and business customers for the usage of the Group's fixed line telecommunications networks is measured by the number of lines leased and the agreed upon rate per line leased. The lease arrangements are primarily determined on a year to year basis.

- Certain PHS bundled service contracts comprise the provision of PHS services and handsets to customers, under which customers either prepay a certain amount of service fee or commit to spend a minimum monthly service fee for a designated period in order to receive a free handset. When all of the following criteria are met, PHS handsets and related services are separately recognised as revenues arising from local, DLD, or ILD services fees and sales of handsets according to their relative fair values. When any one of the following criteria is not met, total revenues from PHS bundled service contracts are recognised on a systematic basis to match the shorter of the pattern of usage of the PHS services by customers and the minimum non-cancellable contractual period. See Note 4(u)(ii) for the policy on accounting for the cost of the handsets.

  i) PHS handsets and relative services have value on a stand-alone basis;

  ii) Objective and reliable fair value of PHS handsets and relative services exists;

  iii) In arrangements that include a general right of refund for the delivered item, performance of the undelivered item is considered probable and substantially in the Group' control.

4 Principal accounting policies *(continued)*

(c) Revenue recognition *(continued)*

(ii) Interest income

Interest income is recognised on a time proportion basis, taking into account the principal amounts outstanding and the interest rates applicable.

(iii) Dividend income

Dividend income is recognised when the right to receive payment is established.

(d) Interest expenses

Interest expense attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalized as part of the cost of that asset.

All other interest expenses are charged to the income statement in the year in which they are incurred.

(e) Interconnection charges

Interconnection charges represent amounts incurred for the use of other telecommunications operators' networks for facilitating the completion of calls that originate from the Group's fixed line telecommunications networks. Interconnection charges are recognised on an accrual basis. Interconnection charges with domestic operators and the fellow subsidiaries of the Group are accrued based on actual amounts, while those with overseas operators are accrued based on the actual amounts, if known, or the Group's estimates.

(f) Translation of foreign currencies

(i) Functional currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"), which is Renminbi.

(ii) Transactions and balances

Transactions in foreign currencies are translated at exchange rates ruling at the transaction dates. Monetary assets and liabilities expressed in foreign currencies at the balance sheet dates are translated at rates of exchange ruling at the balance sheet dates. Exchange differences arising in these cases are dealt with in the income statement.

(iii) The Group

The results and financial position of all the Group entities that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- Assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- Income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and

4 Principal accounting policies *(continued)*

(f) Translation of foreign currencies *(continued)*

(iii) The Group (continued)

- All resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign entities, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is sold, such exchange differences are recognised in the income statement as part of the gain or loss on disposal.

(g) Cash and cash equivalents

Cash and cash equivalents, comprising cash on hand, deposits held at call with banks and cash investments with original maturities of three months or less are carried at cost.

(h) Accounts receivable and other receivables

Accounts and other receivables are recognised initially at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment. A provision for impairment of accounts and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of the provision is recognised in the income statement.

(i) Inventories and consumables

Inventories comprise mainly telephone handsets and are stated at the lower of cost and net realizable value on a first-in, first-out basis, after provisions for obsolescence. Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

Consumables consist of materials and supplies used in maintaining the Group's telecommunication networks and are charged to the income statement when brought into use. Consumables are valued at cost less any provision for obsolescence.

(j) Lease prepayments

(i) Lease prepayments for land

Lease prepayments for land represent payments for land use rights. Lease prepayments for land are stated at cost initially and expensed on a straight line basis over the lease period.

(ii) Lease prepayments for network capacity

Lease prepayments for network capacity represent payments for network capacity on an indefeasible right of use basis for the own use of the Company. Lease prepayments for network capacity are stated at cost initially and expensed on a straight-line basis over the lease period.

4 Principal accounting policies *(continued)*

(k) Fixed assets

(i) Construction-in-progress

Construction-in-progress represents buildings, telecommunications networks plant, transmission and switching equipment under construction and pending installation, and is stated at cost less impairment losses. Cost comprises direct costs of construction including borrowing costs attributable to the construction during the period of construction. When the asset being constructed becomes available for use, the construction-in-progress is transferred to the appropriate category of fixed assets.

(ii) Other fixed assets

Other fixed assets are initially stated at cost less accumulated depreciation and accumulated impairment losses. Historical cost includes expenditure that is directly attributable to the acquisition of the items. The subsequent costs are included in the assets' carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. Any other costs incurred in restoring fixed assets are charged to the income statement as incurred.

Buildings subsequent to initial recognition are stated at cost less accumulated impairment losses and depreciated over their expected useful lives.

(iii) Revaluations

Fixed assets other than buildings are carried at their revalued amounts. Revalued assets are stated at fair value as of the revaluation date less accumulated depreciation. When an item of fixed asset is revalued, any accumulated depreciation at the date of the revaluation is restated proportionately together with the change in the gross carrying amount of the asset so that the carrying amount of the asset after revaluation equals its revalued amount.

Increases in valuation are credited to the revaluation reserve. Decreases in valuation are first set off against any revaluation surplus on earlier valuations in respect of the same item and thereafter are debited to operating profit. Any subsequent increases are credited to operating profit up to the amount previously debited. Each year the difference between depreciation based on the revalued carrying amount of the asset expensed in the income statement and depreciation based on the asset's original cost is transferred from the revaluation reserve to retained earnings.

Revaluations on fixed assets will be performed with sufficient regularity by independent valuers and in each of the intervening years, valuations will be undertaken by executives of the Group.

(iv) Depreciation

Fixed assets are depreciated at rates sufficient to write off their costs or revalued amounts less accumulated impairment losses and estimated residual values over their estimated useful lives on a straight-line basis. The principal useful lives are as follows:

Buildings	8-30 years
Telecommunications networks and equipment	5-10 years
Furniture, fixture, motor vehicles and other equipment	5-10 years

The useful lives and estimated residual values are reviewed and modified periodically at every balance sheet date.

4 Principal accounting policies *(continued)*

(k) Fixed assets *(continued)*

(v) Gain or loss on sale of fixed assets

The gain or loss on disposal of a fixed asset is the difference between the net sales proceeds and the carrying amount of the relevant asset, and is recognised in the income statement, except where the fixed asset is carried at valuation. The relevant portion of the revaluation reserve realized in respect of previous valuations is transferred to retained earnings and is shown as a movement in reserves.

(l) Impairment of assets

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

(m) Assets held under leases

(i) Finance leases

Leases of assets where the Group has substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized upon commencement of the lease at the lower of the fair value of the leased assets and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in current and non-current borrowings. The interest element of the finance cost is recognised in the income statement over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

(ii) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are expensed in the income statement on straight-line basis over the period of the lease.

(n) Intangible assets

(i) Purchased software

Expenditure on purchased software is capitalized and amortized using the straight-line method over the expected useful lives of the software, which vary from two to five years.

(ii) Sponsorship fee

The sponsorship fee for the 2008 Beijing Olympic Games has been capitalized and amortized on a straight-line basis over 4 years, being the estimated beneficial period under the sponsorship program. The cost of the intangible asset is calculated based on the expected cash payment and the fair value of the services to be provided.

(o) Accounts payable

Accounts payable are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

4 Principal accounting policies *(continued)*

(p) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

(q) Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Provisions are not recognised for operating losses arising in future periods.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised in the income statement.

(r) Share capital

Ordinary shares are classified as equity.

Where shares are issued, any consideration received (net of related income tax effects) is included in equity attributable to the Company's equity holders.

(s) Employee benefits

(i) Pension obligations

(a) Employees in the PRC are entitled to retirement benefits equal to a fixed proportion of their salary at their normal retirement age which is paid by the PRC government. As stipulated by the regulations of the PRC, the subsidiaries in the PRC make contributions to the basic defined contribution pension plans organized by their respective municipal governments under which they are governed. The Group is required to make such contributions to these plans at a rate of 20% of the salaries, bonuses and certain allowances of the employees. The Group has no other material obligation for post-retirement benefits beyond these payments as they fall due. Payments made under these plans are expensed as incurred.

(b) The Group also operates a mandatory provident fund scheme ("the MPF scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for employees employed under the jurisdiction of the Hong Kong Employment Ordinance. The MPF scheme is a defined contribution retirement scheme administered by independent trustees. Under the MPF scheme, the employer and its employees are each required to make contributions to the scheme at 5% of the employees' relevant income, subject to a cap of monthly relevant income of HK$20,000. Payments are expensed as incurred.

4 Principal accounting policies *(continued)*

(s) Employee benefits *(continued)*

(ii) Early retirement benefits

Early retirement benefits are recognised as expenses when the Group reaches agreement with the relevant employees for early retirement.

(iii) Employee housing benefits

One-off cash housing subsidies paid to PRC employees are charged to the income statement in the year in which it is determined that the payment of such subsidies is probable and the amounts can be reasonably estimated (see Note 33).

PRC full-time employees of the Group participate in various government-sponsored housing funds. The Group contributes on a monthly basis to these funds based on certain percentages of the salaries of the employees. The Group's liability in respect of these funds is limited to the contributions payable in each period. Contributions to these housing funds are expensed as incurred.

(iv) Share option scheme

The Group operates an equity-settled, share-based compensation plan. The fair value of the employee services received in exchange for the grant of the options is recognised as an expense. Fair values of the options with different vesting periods are determined separately. The total amount to be expensed over the vesting period is determined by reference to the fair value of the options granted, excluding the impact of any non-market vesting conditions (for example, profitability and sales growth targets). Non-market vesting conditions are included in assumptions about the number of options that are expected to become exercisable. At each balance sheet date, the entity revises its estimates of the number of options that are expected to become exercisable. It recognises the impact of the revision of original estimates, if any, in the income statement, and a corresponding adjustment to equity over the remaining vesting period.

When the share option is exercised, the consideration received after deduction of transaction cost directly attributed to the exercise is recorded in share capital (nominal value) and share premium.

(t) Deferred taxation

Deferred taxation is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Tax rates enacted or substantially enacted at the balance sheet date are used to determine deferred taxation. Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized.

4 Principal accounting policies *(continued)*

(u) Other non-current assets

(i) Deferred installation costs

The direct incremental costs associated with the installation of fixed line services are deferred and expensed to the income statement over the expected customer relationship period of 10 years except when the direct incremental costs exceed the corresponding upfront installation fees. In such cases, the excess of the direct incremental costs over the installation fees are recorded immediately as expenses in the income statement.

(ii) Subscriber acquisition costs

As shown in note 4(c)(i), when certain bifurcation conditions are met, revenue attributable to handsets given to customers under bundled service contracts is recognised separately in the income statement of the period the contracts are entered into. The cost of these handsets is expensed immediately to the income statement in the same period. When any one of the aforementioned conditions is not met, the costs of handsets given to customers under bundled service contracts are deferred as subscriber acquisition costs and expensed to the income statement on a systematic basis to match with the pattern of the customer service income over the contract period.

(iii) Prepaid network capacities

Prepayments for the network capacities purchased on an indefeasible rights to use (''IRU'') basis for resale are capitalized and expensed over the corresponding lease period.

(v) Discontinued operations

A discontinued operation is a component of the Group that may be a major line of business or geographical area of operations that has been disposed or is held for sale. The result of that component is separately reported as "discontinued operations" in the income statement. The comparative income statement and cashflow statement are restated as if the operation had been discontinued from the start of the comparative period. The assets and liabilities of such component classified as "discontinued operations" or "held for sale" is presented separately in the assets and liabilities, respectively, of the consolidated balance sheet, from the date it is first determined to be discontinued or held for sale.

(w) Contingent liabilities

A contingent liability is a possible obligation that arises from past events and whose existence will only be confirmed by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Group. It can also be a present obligation arising from past events that is not recognised because it is not probable that outflow of economic resources will be required or the amount of obligation cannot be measured reliably.

A contingent liability is not recognised but is disclosed in the notes to the financial statements when an outflow of economic benefits is less than probable but not remote. When a change in the probability of an outflow occurs such that the outflow is probable, the contingent liability will then be recognised as a provision.

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain events not wholly within the control of the Group. A contingent asset is disclosed when an inflow of economic benefits is probable but only recognised in income statement when realized.

4 Principal accounting policies *(continued)*

(x) Segmental reporting

Business segments provide services that are subject to risks and returns that are different from other business segments. Geographical segments provide services within a particular economic environment that is subject to risks and returns that differ from those of components operating in other economic environments. Currently the Group has one business segment, the provision of fixed line telecommunications services. Less than 10% of the Group's assets and operations are located outside the PRC. Accordingly, no business and geographical segment information is presented.

(y) Earnings per share ("EPS") and per American Depository Shares ("ADS")

Basic EPS is computed by dividing net profit attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year.

Diluted EPS is computed by dividing net profit attributable to shareholders by the weighted average number of ordinary and dilutive ordinary equivalent shares outstanding during the year. Ordinary equivalent shares consist of ordinary shares issuable upon the exercise of outstanding stock options using the treasury stock method.

Earnings per ADS is computed by multiplying the EPS by 20, which is the number of shares represented by each ADS.

5 Critical accounting estimates and judgments

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under circumstances.

(a) Critical accounting estimates and assumptions

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions 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:

(i) Depreciation of property, plant and equipment

The property, plant and equipment of the Group are depreciated at rates sufficient to write off their costs or revalued amounts less accumulated impairment losses and estimated residual values over their estimated useful lives on a straight-line basis. The Group reviews the estimated useful lives and estimated residual values periodically to ensure that the method and rates of depreciation are consistent with the expected pattern of economic benefits from property, plant and equipment. The Group estimates the useful lives of the property, plant and equipment as set out in Note 4(k)(iv) based on the historical experience with similar assets, taking into account anticipated technological changes. The depreciation expenses in the future periods will change if there are significant changes from previous estimates.

As of December 31, 2007, the Group did not change the estimate of useful lives.

5 Critical accounting estimates and judgments *(continued)*

(a) Critical accounting estimates and assumptions *(continued)*

(ii) Revaluation of property, plant and equipment

Apart from lease prepayments for land and buildings, which are carried at cost, other property, plant and equipment are carried at revalued amounts, being the fair value at the date of revaluation, less subsequent accumulated depreciation and impairment. Property, plant and equipment of the Group was revalued as of December 31, 2006 on a depreciated replacement cost basis by an independent valuer. If the revalued amounts differ significantly from the carrying amounts of the property, plant and equipment in the future, the carrying amounts will be adjusted to the revalued amounts. The key assumptions made to determine the revalued amounts include the estimated replacement costs and the estimated useful lives of the property, plant and equipment. This will have an impact on the Group's future results, since any subsequent decreases in valuation are set off first against increases on earlier valuations in respect of the same item and thereafter are charged as an expense to the income statement and any subsequent increases are credited as income to the income statement up to the amount previously charged then to equity. In addition, the depreciation expenses in future periods will change as the carrying amounts of such property, plant and equipment change as a result of the revaluation.

(iii) Impairment of non-current assets

At each balance sheet date, the Group considers both internal and external sources of information to assess whether there is any indication that non-current assets, including property, plant and equipment, are impaired. If any such indication exists, the recoverable amount of the assets is estimated and an impairment loss is recognised to reduce the carrying amount of the asset to its recoverable amount. The recoverable amount is the higher of value in use or net selling price. Estimated values in use are determined based on estimated discounted future cash flows of the cash generating unit at the lowest level to which the asset belongs. Key assumptions made to determine the estimated discounted future cash flows include the estimated future cash flows, estimated growth rate and the estimated weighted average cost of capital of the Group. Such impairment losses are recognised in the income statement, except where the asset is carried at valuation and the impairment loss does not exceed the revaluation surplus for that same asset, in which case the impairment loss is treated as a revaluation decrease and charged to the revaluation reserve. Accordingly, there will be an impact to the future results if there is a significant change in the recoverable amounts of the non-current assets.

At December 31, 2007, the Group did not identify any indication that non-current assets were impaired.

(iv) Revenue recognised for upfront connection and installation fees

The Group defers the recognition of upfront customer connection and installation fees and amortizes them over the expected customer relationship period of 10 years. The related direct incremental installation costs are deferred and amortized over the same expected customer relationship period of 10 years, except when the direct incremental costs exceed the corresponding installation fees, the excess amounts are immediately written off as an expense to the income statement. The Group estimates the expected customer relationship period based on the historical customer retention experience and after factoring in the expected level of future competition, the risk of technological or functional obsolescence to the Group's services, technological innovation, and the expected changes in the regulatory and social environment. If the Group's estimate of the expected customer relationship period changes as a result of increased competition, changes in telecommunications technology or other factors, the amount and timing of recognition of the deferred revenues may change for future periods.

As of December 31, 2007, the Group did not change the estimate of customer relationship period.

5 Critical accounting estimates and judgments *(continued)*

(a) Critical accounting estimates and assumptions *(continued)*

(v) Provision for doubtful debts

The Group maintains an allowance for doubtful debts for estimated losses resulting from the inability of its customers to make the required payments. The Group makes its estimates based on the aging of its accounts receivable balances, customer's creditworthiness, and historical write-off experience. If the financial condition of its customers were to deteriorate, actual write-offs might be higher than expected, and the Group would be required to revise the basis of making the allowance and its future results would be affected.

(vi) Fair value

The Group estimates the fair value of its financial assets and financial liabilities including accounts receivable, other receivables and other current assets, accounts payable, and bank and other loans for disclosure purposes by discounting its future contractual cash flows at the estimated current market interest rate that is available to the Group for similar financial instruments. The future disclosed values will change if there are changes in the estimated market interest rate.

6 Financial risk management

(a) Financial risk factors

The Group's major financial assets include bank deposits, accounts receivable, notes receivable and other receivables. The Group's major financial liabilities include accounts payable, notes payable, other payable, bank borrowings, commercial paper and corporate bonds.

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk and cash flow interest rate risk), credit risk, and liquidity risk. The board has reviewed and approved its relative risk management policy as follows:

(i) Foreign exchange risk

The Group's major operational activities are carried out in mainland China and a majority of the transactions are performed in Renminbi. On December 31, 2007, the Group had certain bank deposits and borrowings were denominated in foreign currencies, mainly in US dollar and HK dollar. Any change in the exchange rates of these currencies to Renminbi will impact the Group's operating results.

As at December 31, 2007 and 2006, the Group had bank balances denominated in foreign currencies amounting to RMB320 million and RMB1,946 million, respectively. As at December 31, 2007 and 2006, the Group had bank borrowings denominated in foreign currencies amounting to RMB1,246 million and RMB1,432 million, respectively.

At December 31 2007, if Renminbi had weakened/strengthened by 5% against the foreign currencies, the impact of the fluctuation on an annual profit is presented in the table below. The analysis covers bank deposits and borrowings. A positive figure means the Renminbi has appreciated against foreign currencies and lead to an increase of profit.

6 Financial risk management *(continued)*

(a) Financial risk factors *(continued)*

(i) Foreign exchange risk (continued)

	Increase/(Decrease) in annual profit	
	December 31, 2007	December 31, 2006
	RMB million	RMB million
HK Dollar exchange rate fluctuation		
5% appreciation	**7**	32
5% depreciation	**(7)**	(32)
US Dollar exchange rate fluctuation		
5% appreciation	**(21)**	30
5% depreciation	**21**	(30)

(ii) Cash flow and fair value interest rate risk

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest-rate risk arises from interest bearing borrowings. Borrowings issued at variable rates expose the Group to cash flow interest-rate risks. Borrowings issued at fixed rates expose the Group to fair value interest-rate risks. The Group does not use derivative financial tools to offset the interest-rate risk. The footnote 30 discloses bank loans with fixed rates and variable rates.

As at December 31, 2007, 83.96% of the Group's loans were with fixed interest rate (2006: 74.69%). If the market interest had (decreased)/increased by 2% ,the impact of the fluctuation on an annual profit is presented in the table below:

	Increase/(Decrease) in annual profit	
	December 31, 2007	December 31, 2006
	RMB million	RMB million
Change of interest rate		
2% increase	**(476)**	(454)
2% decrease	**476**	454

6 Financial risk management *(continued)*

(a) Financial risk factors *(continued)*

(iii) Credit risk

The Group provides telecommunication and related services to residential clients and business clients. The Group will terminate a fixed line service to residential clients if the accounts receivable are over 90 days. Accounts receivable from other telecommunications operators and customers are due generally between 30 to 90 days from the billing date. The Group analyses the aging of accounts receivable and the status of collection on a monthly basis to formulate the appropriate collection strategy to ensure the risk faced is not material.

The carrying amount of accounts receivable included in the balance sheet represents the Group's exposure to credit risk in relation to its financial assets. Most of the Group's accounts receivable with aging over 30 days are overdue. The Group evaluated the risk associated with the accounts receivable balances with aging over 90 days, and made provisions accordingly. The Group believes that adequate provision for uncollectible account receivable has been made.

The accounts receivable of the Group are disclosed in Note 18 to the financial statements.

The credit risk of the Group's other financial assets (including cash and cash equivalents and other receivables) arise from any counter parties' breach of contract. Thus, the highest risk the Group will bear is the book value of the instrument.

The Group's cash management policy is to deposit cash and cash equivalents mainly in state-owned banks and other banks, which are highly rated by an international credit rating company. The rates are between BBB+ to BBBpi. The management does not expect any loss to arise from bank nonperformance.

(iv) Liquidity risk

The Group is financed mainly by short term borrowings. As a result, there is a significant working capital deficit as highlighted in balance sheet. Please refer to Note 2 for more details.

The Group's aim is to maintain the balance between the availability and liquidity of the funding by using interest bearing bank loans and other borrowings, commercial paper, corporate bonds and other suitable financing channels. The Group's policy is to regularly monitor operating capital demands and compliance with current and expected operating capital requirements. The Group reviews cash flow forecasts of each entity on a regular basis to maintain sufficient cash reserves and bank pledged funds and to deal with short and long term capital demands.

The following table shows the undiscounted balances of the financial liabilities (including interest expense) categorized by time period from the balance sheet date to the date of contract expiry.

6 Financial risk management *(continued)*

(a) Financial risk factors *(continued)*

(iv) Liquidity risk (continued)

December 31, 2007	Total	Within 1 year	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years
	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million
Accounts payable	15,639	15,639	—	—	—	—	—
Short-term loans	12,134	12,134	—	—	—	—	—
Long-term bank and other loans	21,616	6,407	10,272	1,887	106	104	2,840
Commercial paper	20,629	20,629	—	—	—	—	—
Corporate bonds	2,900	90	90	90	90	90	2,450
Amounts due to holding companies and fellow subsidiaries	8,870	2,319	2,214	4,337	—	—	—
Total	81,788	57,218	12,576	6,314	196	194	5,290

December 31, 2006	Total	Within 1 year	1-2 years	2-3 years	3-4 years	4-5 years	Over 5 years
	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million
Accounts payable	17,661	17,661	—	—	—	—	—
Short-term loans	31,602	31,602	—	—	—	—	—
Long-term bank and other loans	36,343	8,980	7,814	10,416	431	430	8,272
Commercial paper	10,000	10,000	—	—	—	—	—
Amounts due to holding companies and fellow subsidiaries	8,781	2,352	2,248	2,143	2,038	—	—
Total	104,387	70,595	10,062	12,559	2,469	430	8,272

The directors have the responsibility to consider the future operational capital requirements. The Group has a policy to maintain sufficient cash and cash equivalents and to finance operations through bank lending. For bank facilities, please refer to Note 39.

6 Financial risk management *(continued)*

(b) Fair value estimation

The fair value of financial instruments that are actively traded is based on the market price as of balance sheet date. The market price of the financial assets that the Group holds is the current bidding price. The market price of financial liabilities is the offering price. The fair value of the Group's bank deposits, accounts receivable, notes receivable, corporate bonds, commercial paper and short-term borrowings approximate book value.

The nominal value less estimated credit adjustments of trade receivables and payables are assumed to approximate their fair values. The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

(c) Objective and policy of financial risk management

The Group defines the capital as the shareholders' equity. The Group's objectives of the management of capital are to maintain the ability to operate based on going concern, meet the requirements of capital investment for the business development, bring benefit to shareholders and other stakeholders, and also to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return of capital to shareholders, issue new shares, sell assets to reduce debt.

7 Revenues

Revenues represent the turnover of the Group and are derived from the provision of fixed line telecommunications and related services, net of the PRC business taxes and government levies amounting to RMB2,358 million (2006: RMB2,387 million). The Group's revenues by business nature can be summarized as follows:

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Revenues		
Local usage fees	**19,989**	22,059
Monthly telephone services	**12,387**	16,546
Upfront installation fees	**1,283**	1,364
DLD usage fees	**8,769**	9,495
ILD usage fees	**791**	819
Value-added services	**6,114**	5,341
Interconnection fees	**8,376**	8,432
Upfront connection fees	**1,517**	2,406
Broadband services	**13,835**	9,916
Other Internet-related services	**532**	516
Managed data services	**1,284**	1,413
Leased line income	**2,521**	2,540
Information communications technology services	**3,990**	855
Other services	**2,617**	2,492
Total	**84,005**	84,194

8 Operating expenses by nature

Operating expenses mainly represent:

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Staff cost	**12,223**	11,849
Depreciation and amortisation	**25,495**	24,913
Maintenance cost	**4,373**	4,512
Miscellaneous taxes and fees	**358**	278
Customer installation cost	**2,036**	1,116
Interconnection charges	**4,014**	3,915
Advertising and promotion expenses	**821**	884
Sales channel cost	**2,298**	2,118
Subscriber acquisition and retention cost	**1,582**	3,646
Auditor's remuneration	**54**	61
Bad and doubtful debt expenses	**868**	1,003
Operating leases	**1,900**	1,969
Cost of hardware sold in relation to information communications technology services	**2,830**	598

9 Other income

Other income is the subsidy income the Company received arising from the reinvesting of the profit distributions received from a subsidiary in the PRC to that subsidiary.

10 Finance costs

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Interest expenses on:		
- Bank and other loans wholly repayable within five years	**2,875**	3,185
- Bank and other loans wholly repayable after more than five years	**198**	325
- Deferred consideration related to Acquisition of New Horizon	**375**	479
Total	**3,448**	3,989
Less: Interest expenses capitalized in construction in progress	**(165)**	(233)
Exchange loss/(gain), net	**25**	(8)
Bank charges	**25**	19
	3,333	3,767
Interest expenses were capitalized in construction in progress using the following annual interest rates	**4.75%-5.82%**	4.71%-5.28%

11 Taxation

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
PRC enterprise income tax ("EIT")	**3,901**	4,143
Overseas profit tax	**12**	20
Deferred taxation- Continuing operations (Note 34)	**(66)**	(436)
Deferred taxation -Change in statutory taxation rate (Note 34)	**(51)**	—
Taxation charges	**3,796**	3,727

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

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

11 Taxation *(continued)*

On March 16, 2007, the National People's Congress approved the Corporate Income Tax Law of the People's Republic of China (the "New CIT Law"). This New CIT Law reduces the corporate income tax rate for domestic enterprises from 33% to 25% with effect from January 1, 2008. As a result of the new CIT Law, as at March 16, 2007, the carrying value of deferred tax assets has been written down by RMB775 million, with RMB111 million recognised in income statement and RMB664 million recognised in equity. The carrying value of deferred tax liabilities has been written down by RMB273 million, with RMB162 million recognised in the income statement and RMB111 million recognised in equity. The impact of the change in deferred taxation recognised in either the current income statement or equity as a result of the New CIT Law corresponded to whether the related items were previously recognised in income statement or equity.

On November 28, 2007, the National People's Congress approved the Implementation guide on the Corporate Income Tax Law of the People's Republic of China (the "New CIT Implementation guide"), with effect from January 1, 2008. Per a bilateral tax affairs agreement, enterprises incorporated in Hong Kong is required to pay a 5 percent corporate income tax on profits distributed from its subsidiaries incorporated in the PRC. On February 22, 2008, the Ministry of Finance and the State Administration of Taxation jointly issued CaiShui [2008], Circular No. 1 ("Circular No. 1"). In accordance with the Circular No. 1, accumulated retained earnings of foreign investment enterprises generated before January 1, 2008 and distributed to foreign investors after 2008 are exempt of income tax. Earnings of foreign investment enterprises generated in or after 2008 and distributed to foreign investors should pay the withholding tax. As a result, the Group may accrue deferred tax liability for the undistributed earnings generated by CNC China during or after 2008 according to actual situation.

On December 26, 2007, the State Council promulgated 'Notice Regarding Preferential Policy of Implementing EIT in Intervening Period'. The Group has evaluated the regulation and considered that it will not have material impact on the financial statements.

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

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Profit before taxation	**15,267**	15,205
Weighted average statutory tax rate	**33%**	33%
Tax calculated at the weighted average statutory tax rate	**5,038**	5,018
Non-taxable income (Note i)	**(1,184)**	(1,216)
Expenses not deductible for tax purposes	**68**	64
Change in statutory taxation rate (Note 34)	**(51)**	—
Others	**(75)**	(139)
Tax charge	**3,796**	3,727

Note:

(i) Non-taxable income comprises primarily of upfront connection fees charged to customers which are amortized over the customer relationship and the subsidy income obtained (Note 9).

12 Profit attributable to shareholders

(a) For the year ended December 31, 2007, profit attributable to shareholders includes current year profit of RMB8,714million (2006:RMB17,475 million), which has been recognized in the financial statements of the Company.

(b) The Company's subsidiary, CNC China is registered as a foreign investment enterprise in the PRC. In accordance with the Articles of Association of CNC China, it is required to provide for certain statutory reserves, namely, general reserve and staff bonus and welfare fund, which are appropriated from profits after tax but before any dividend distribution.

CNC China is required to allocate at least 10% of their profit after tax determined under PRC GAAP to the general reserve fund until the cumulative amounts reach 50% of the registered capital. The statutory reserve can only be used, upon obtaining approval from the relevant authority, to offset accumulated losses or increase capital.

Accordingly, CNC China appropriated approximately RMB868 million to the general reserve fund for the year ended December 31, 2007 (2006: RMB855million).

(c) According to a PRC tax approval document issued by the Ministry of Finance and State Administration of Taxation to the Group, the Group's upfront connection fees are not subject to EIT and an amount equal to the upfront connection fees recognised in the retained earnings should be transferred from retained earnings to a statutory reserve. Up to December 31, 2007, the Company has made accumulated appropriation of RMB10,706 million to the statutory reserve (Up to December 31, 2006 : RMB9,189 million).

13 Profit distributions

	Year ended December 31			
	2007		2006	
	HK$ million	**RMB million**	HK$ million	RMB million
Final dividend proposed after balance sheet date of HK$0.592 per share (2006 : HK$0.553 per share)	**3,951**	**3,700**	3,678	3,695
Dividend distributed during the year	**3,678**	**3,600**	3,073	3,196

In the meeting of the board of directors held on March 25, 2008, the directors proposed a final dividend of HK$0.592 per ordinary share for the year ended December 31, 2007. Dividends proposed after the balance sheet date have not been reflected as a dividend payable and will be reflected as an appropriation in the 2008 financial statements.

14 Earnings per share

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

The following table sets forth the computation of basic and diluted earnings per share:

	Year ended December 31	
	2007	2006
	(in RMB millions, except share and per share data)	
		Restated Note 2
Numerator:		
Profit for the year		
- Continuing operations	**11,471**	11,478
- Discontinued operations	**624**	1,487
	12,095	12,965
Denominator		
Weighted average number of ordinary shares outstanding and shares used in computing basic earnings per share	**6,657,045,212**	6,615,520,381
Diluted equivalent shares arising from share options	**80,583,956**	51,955,496
Shares used in computing diluted earnings per share	**6,737,629,168**	6,667,475,877
Basic earnings per share (RMB)		
- Continuing operations	**1.72**	1.74
- Discontinued operations	**0.09**	0.22
- Profit for the year	**1.81**	1.96
Diluted earnings per share (RMB)		
- Continuing operations	**1.70**	1.72
- Discontinued operations	**0.09**	0.22
- Profit for the year	**1.79**	1.94

15 Staff cost including directors' remuneration

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Wages, salaries and welfare	**10,778**	10,504
Contributions to pensions	**1,445**	1,345
Total	**12,223**	11,849

16 Directors' and senior management's emolument

(a) Directors' emoluments

The following table sets out the emoluments paid to the Company's directors during the year of 2007:

	Year ended December 31, 2007 RMB thousand					
	Fees (a)	Basic salaries, housing allowances, other allowances and benefits in kind	Subtotal	Share based compensation	Contributions to retirement schemes	Total
Zhang Chunjiang	—	840	840	149	21	1,010
Zuo Xunsheng (i)	—	824	824	130	21	975
Li Jianguo(ii)	—	344	344	—	9	353
Zhang Xiaotie	—	724	724	130	21	875
Li Fushen (iii)	—	697	697	130	21	848
Miao Jianhua (iv)	—	360	360	182	12	554
Tian Suning (v)	—	—	—	239	—	239
Li Liming (vi)	—	22	22	114	21	157
Yan Yixun	253	—	253	96	—	349
Cesareo Alierta Izuel(vii)	14	—	14	—	—	14
José María Álvarez-Pallete	318	—	318	—	—	318
Mauricio Sartorius (viii)	239	—	239	—	—	239
John Lawson Thornton	464	—	464	—	—	464
Victor Cha Mou Zing	501	—	501	—	—	501
Qian Yingyi	604	—	604	—	—	604
Hou Ziqiang	506	—	506	—	—	506
Timpson Chung Shui Ming	520	—	520	—	—	520
Total	3,419	3,811	7,230	1,170	126	8,526

For the year ended December 31, 2007, the fees disclosed above include RMB2,595 thousand paid to independent non-executive directors.

16 Directors' and senior management's emolument *(continued)*

(a) Directors' emoluments *(continued)*

The following table sets out the emoluments paid to the Company's directors during the year ended December 31 2006:

	Year ended December 31, 2006 RMB thousand					
	Fees (b)	Basic salaries, housing allowances, other allowances and benefits in kind	Subtotal	Share based compensation	Contributions to retirement schemes	Total
Zhang Chunjiang	—	763	763	312	19	1,094
Zuo Xunsheng(i)	—	746	746	272	19	1,037
Zhang Xiaotie	—	671	671	272	19	962
Li Fusheng(iii)	—	671	671	272	19	962
Miao Jianhua(iv)	—	671	671	238	19	928
Jiang Weiping(ix)	—	453	453	238	19	710
Li Liming(vi)	—	420	420	238	19	677
Tian Suning(v)	—	—	—	312	—	312
Yan Yixun	251	—	251	200	—	451
John Lawson Thornton	409	—	409	—	—	409
Victor Cha Mou Zing	453	—	453	—	—	453
Qian Yingyi	545	—	545	—	—	545
Hou Ziqiang	483	—	483	—	—	483
Timpson Chung Shui Ming	460	—	460	—	—	460
José María Álvarez-Pallete	317	—	317	—	—	317
Mauricio Sartorius (viii)	9	—	9	—	—	9
Total	2,927	4,395	7,322	2,354	133	9,809

For the year ended December 31, 2006, the fees disclosed above include RMB2,350 thousand paid to independent non-executive directors.

16 Directors' and senior management's emolument *(continued)*

(a) Directors' emoluments *(continued)*

Note:

(a) According to the ordinary resolution passed at the Second Extraordinary General Meetings held on February 14, 2007, the director's fee for the directors of the Company shall be revised as follows: all non-executive Directors nominated by China Netcom Group and all executive Directors shall not be entitled to any director's fee. This revision shall apply in respect of each financial year commencing from the 2007 financial year.

(b) On December 6, 2006, according to the directors' discretion, Zhang Chunjiang, Zuo Xunsheng, Zhang Xiaotie, Miao Jianhua, Li Liming, Jiang Weiping and Tian Suning waived their emoluments for the years ended December 31, 2006 totalling RMB1,526 thousand. Details of the waivers are as follows: Zhang Chunjiang RMB251 thousand, Zuo Xunsheng RMB158 thousand, Zhang Xiaotie RMB251 thousand, Miao Jianhua RMB251 thousand, Jiang Weiping RMB94 thousand, Li Liming RMB270 thousand, Tian Suning RMB251 thousand.

(i) Appointed in May 2006
(ii) Appointed in July 2007
(iii) Appointed in January 2007
(iv) Resigned in July 2007
(v) Re-designated as non-executive Directors in May 2006, resigned in July 2007
(vi) Resigned in January 2007
(vii) Appointed in December 2007
(viii) Appointed in December 2006, resigned in December 2007
(ix) Resigned in May 2006

(b) Five highest paid individuals

The five individuals whose emoluments were the highest for the year ended December 31, 2007 include three directors (2006: two) whose emoluments are reflected in the analysis presented above. The emoluments payable to the remaining two (2006: three) individuals are as follows:

	Year ended December 31	
	2007	2006
	RMB thousand	RMB thousand
Basic salaries, housing allowances, other allowances and benefits in kind	**1,450**	2,013
Share based compensation	**260**	816
Contributions to retirement schemes	**42**	57
Total	**1,752**	2,886

The number of the remaining individuals whose emoluments fell within the following bands is set out as follows:

	Year ended December 31	
	2007	2006
Nil - RMB936,400 (equivalent of Nil - HK$ 1,000,000)	**2**	3

17 Cash and bank deposits

	Group		Company	
	As at December 31		As at December 31	
	2007	2006	**2007**	2006
	RMB million	RMB million Restated Note 2	**RMB million**	RMB million
Cash and cash equivalents	**5,304**	7,623	**113**	1,772
Time deposits with original maturities over three months	**91**	105	**—**	—
Total cash and bank deposits	**5,395**	7,728	**113**	1,772
Effective interest rate of time deposits with original maturities over three months (% per annum)	**0.72**	0.72	**—**	—

Included in cash and bank deposits as of December 31, 2007 and 2006 are RMB denominated balances kept in the PRC amounting to RMB5,054 million and RMB5,782 million respectively. The conversion of RMB denominated balances into foreign currencies and the remittance of bank balances and cash out of the PRC are subject to the rules and regulation of foreign exchange control promulgated by the PRC government.

Included in the bank deposits were deposits in state-owned banks amounting to RMB4,958 million at December 31, 2007 (2006: RMB7,577 million). For the year ended December 31, 2007, interest income earned from these state-owned banks deposits amounted to RMB106 million (2006: RMB121 million).

18 Accounts receivable

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

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

	As at December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
0-30 days	**5,682**	5,744
31-90 days	**1,866**	1,557
Over 90 days	**2,308**	2,326
Total	**9,856**	9,627
Less: Allowance for doubtful debts	**(1,398)**	(1,344)
Net carrying amounts	**8,458**	8,283

The movement of allowance for doubtful debts is as follows:

	As at December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Balance at beginning of year	**1,344**	1,654
Additional provisions	**844**	1,002
Less: Write-offs	**(750)**	(1,246)
Disposal of ANC Group	**—**	(66)
Disposal of Guangdong and Shanghai Branches	**(40)**	—
Balance at end of year	**1,398**	1,344

The carrying value of accounts receivable approximates their fair values based on cash flows discounted using market rate of 7.47% (December 31, 2006: 6.12%).

Included in the accounts receivable are amounts due from other state-owned telecommunication operators amounting to RMB833 million on December 31, 2007. (December 31, 2006: RMB1,079 million).

19 Inventories and consumables

	As at December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Telephone handsets and other customer end-products held for resale, at cost	**125**	155
Consumables, at cost	**162**	261
Total	**287**	416

20 Prepayments, other receivables and other current assets

	Group		Company	
	As at December 31		As at December 31	
	2007	2006	**2007**	2006
	RMB million	RMB million Restated Note 2	**RMB million**	RMB million
Prepaid expenses, deposits and other current assets	**605**	812	**8**	15
Other receivables	**416**	629	**8**	253
Total	**1,021**	1,441	**16**	268

The carrying value of other receivables approximates their fair values based on cash flows discounted using market rate of 7.47% (2006: 6.12%).

21 Fixed assets

	Buildings	Telecommunications networks and equipment	Furniture, fixture, motor vehicles and other equipment	Total
	RMB million	RMB million	RMB million	RMB million
Cost / valuation:				
Balance at January 1, 2006, as restated (Note 2)	27,149	280,301	19,796	327,246
Additions	52	755	639	1,446
Transferred from construction in progress	688	21,449	2,621	24,758
Disposals/write off	(6)	(1,947)	(524)	(2,477)
Disposal of ANC Group	(172)	(636)	(45)	(853)
Fixed assets revaluation deficit, net	—	(10,659)	(3,588)	(14,247)
Balance at December 31, 2006	27,711	289,263	18,899	335,873
Accumulated depreciation:				
Balance at January 1, 2006, as restated (Note 2)	(6,215)	(142,639)	(9,628)	(158,482)
Depreciation charge for the year	(999)	(21,842)	(2,286)	(25,127)
Disposals/write off	4	1,315	424	1,743
Disposal of ANC Group	51	261	28	340
Fixed assets revaluation deficit, net	—	11,778	2,016	13,794
Balance at December 31, 2006	(7,159)	(151,127)	(9,446)	(167,732)
Net book value at December 31, 2006	20,552	138,136	9,453	168,141
Net book value at January 1, 2006, as restated (Note 2)	20,934	137,662	10,168	168,764

21 Fixed assets *(continued)*

	Buildings	Telecommunications networks and equipment	Furniture, fixture, motor vehicles and other equipment	Total
	RMB million	RMB million	RMB million	RMB million
Cost / valuation:				
Balance at January 1, 2007	27,711	289,263	18,899	335,873
Additions	56	797	725	1,578
Transferred from construction in progress	971	15,540	2,595	19,106
Disposals/write off	(33)	(1,749)	(441)	(2,223)
Disposal of Guangdong and Shanghai Branches	(550)	(7,635)	(344)	(8,529)
Balance at December 31, 2007	28,155	296,216	21,434	345,805
Accumulated depreciation:				
Balance at January 1, 2007	(7,159)	(151,127)	(9,446)	(167,732)
Depreciation charge for the year	(1,030)	(21,977)	(2,004)	(25,011)
Disposals/write off	16	1,337	395	1,748
Disposal of Guangdong and Shanghai Branches	134	1,867	137	2,138
Balance at December 31, 2007,	(8,039)	(169,900)	(10,918)	(188,857)
Net book value at December 31, 2007	20,116	126,316	10,516	156,948
Net book value at January 1, 2007	20,552	138,136	9,453	168,141

(a) The net book value of assets held under finance lease is as follows:

	Buildings	Telecommunications networks and equipment	Furniture, fixture, motor vehicles and other equipment	Total
	RMB million	RMB million	RMB million	RMB million
As at December 31, 2007	—	217	2	219
As at December 31, 2006	—	2,000	62	2,062

The depreciation charge on assets held under finance lease amounted to RMB100 million in the year ended December 31, 2007 (2006: RMB351 million).

21 Fixed assets *(continued)*

(b) The analysis of the cost or revaluation of the fixed assets of the Group is as follows:

	Buildings	Telecommunications networks and equipment	Furniture, fixture, motor vehicles and other equipment	Total
	RMB million	RMB million	RMB million	RMB million
December 31, 2007				
Cost	28,155	—	—	28,155
Valuation	—	296,216	21,434	317,650
	28,155	296,216	21,434	345,805
December 31, 2006				
Cost	27,711	—	—	27,711
Valuation	—	289,263	18,899	308,162
	27,711	289,263	18,899	335,873

(c) As required by the PRC rules and regulations relevant to the Listing Reorganisation, each class of fixed assets other than lease prepayments for land and buildings as at December 31, 2003 was valued by Beijing China Enterprise Appraisal Co. Ltd. (the ''PRC valuer''), an independent valuer registered in the PRC, on a depreciated replacement cost basis. The value of such assets in the PRC injected into the Group was determined at RMB122,456 million. Such revalued amounts served as the tax base of the assets with immediate effect. The surplus on revaluation of certain fixed assets of RMB2,982 million was credited to the revaluation reserve while the deficit arising from the revaluation of certain fixed assets of RMB25,778 million was recognised as an expense for the year ended December 31, 2003.

For the Listing Reorganisation, valuations of the lease prepayments for land and buildings of the Group were also performed. The surplus value of such assets was determined at RMB6,967 million. Such amounts served as the tax base for such assets with immediate effect. Details have been set out in Note 34(iii).

As required by the PRC rules and regulations relevant to the Acquisition of New Horizon, each class of fixed assets, other than lease prepayments for land and buildings in the PRC, acquired as at December 31, 2004, was valued by the PRC valuer, on a depreciated replacement cost basis. The value of such acquired assets in the PRC was determined at RMB42,879 million. Such amounts served as the tax base for such assets with immediate effect. The surplus on revaluation of certain fixed assets of RMB3,863 million was credited to the revaluation reserve while the deficit arising from the revaluation of certain fixed assets of RMB11,318 million was recognised as an expense for the year ended December 31, 2004.

For the Acquisition of New Horizon, valuations of the lease prepayments for land and buildings were also performed. The surplus value of such assets was determined at RMB2,553 million. Such amounts served as the tax base for such assets with immediate effect. Details have been set out in Note 34(iii).

21 Fixed assets *(continued)*

(c) *(continued)*

According to the Group's accounting policies, each class of fixed assets of the Group other than buildings as at December 31, 2006 has been revalued by the PRC valuer on a depreciated replacement cost basis. The value of such fixed assets was determined at RMB147,573 million. The net deficit arising on the revaluation was RMB453 million, the net deficit was split between a credit to the revaluation reserve amounting to RMB1,071 million and an expense to the income statement of RMB1,524 million for that year.

The respective carrying amounts of the telecommunication networks and equipment and furniture, fixtures, motor vehicles and other equipment would have been RMB137,414 million and RMB12,382 million as at December 31, 2007 and RMB153,368 million and RMB11,651 million as at December 31, 2006 had they been stated at cost less accumulated depreciation.

22 Construction in progress

	As at December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Balance at beginning of year	**6,335**	6,822
Additions	**18,294**	24,843
Transferred to fixed assets	**(19,106)**	(24,758)
Transferred to intangible assets	**(399)**	(572)
Disposal of Guangdong and Shanghai Branches	**(1,134)**	—
Balance at end of year	**3,990**	6,335

23 Lease prepayment

	As at December 31	
	2007	2006
	RMB million	RMB million
Lease prepayments for land (i)	**2,183**	2,046
Lease prepayments for network capacity (ii)	**311**	318
	2,494	2,364

(i) Lease prepayments for land

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Held for		
Lease of between 10 to 50 years	**2,162**	2,024
Lease of less than 10 years	**21**	22
	2,183	2,046

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Balance at beginning of year	**2,046**	1,949
Additions	**232**	165
Amortisation for the year	**(87)**	(68)
Disposal of Guangdong and Shanghai Branches	**(8)**	—
Balance at end of year	**2,183**	2,046

23 Lease prepayment *(continued)*

(ii) Lease prepayments for network capacity

The net book value is analysed as follows:

	As at December 31	
	2007	2006
	RMB million	RMB million
Held for		
Lease of between 10 to 50 years	**311**	318

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Balance at beginning of year	**318**	—
Additions	**—**	318
Amortisation for the year	**(7)**	—
Balance at end of year	**311**	318

24 Intangible assets

	Purchased software	Sponsorship fees	Others	Total
	RMB million	RMB million	RMB million	RMB million
Cost:				
Balance at January 1, 2006, as restated (Note 2)	1,919	540	3	2,462
Additions	95	—	—	95
Transferred from construction in progress	572	—	—	572
Disposals/write off	(692)	—	(3)	(695)
Balance at December 31, 2006	1,894	540	—	2,434
Accumulated amortisation:				
Balance at January 1, 2006, as restated (Note 2)	(927)	(135)	(3)	(1,065)
Amortisation for the year	(338)	(135)	—	(473)
Disposals/write off	692	—	3	695
Balance at December 31, 2006	(573)	(270)	—	(843)
Net book value at January 1, 2006, as restated (Note 2)	992	405	—	1,397
Net book value at December 31, 2006	1,321	270	—	1,591

24 Intangible assets *(continued)*

	Purchased software	Sponsorship fees	Total
	RMB million	RMB million	RMB million
Cost:			
Balance at January 1, 2007	1,894	540	2,434
Additions	150	—	150
Transferred from construction in progress	399	—	399
Disposals/write off	(73)	—	(73)
Disposal of Guangdong and Shanghai Branches	(75)	—	(75)
Balance at December 31, 2007	2,295	540	2,835
Accumulated amortisation:			
Balance at January 1, 2007	(573)	(270)	(843)
Amortisation for the year	(394)	(135)	(529)
Disposals/write off	69	—	69
Disposal of Guangdong and Shanghai Branches	20	—	20
Balance at December 31, 2007	(878)	(405)	(1,283)
Net book value at January 1, 2007	1,321	270	1,591
Net book value at December 31, 2007	1,417	135	1,552

25 Other non-current assets

	As at December 31	
	2007	2006
	RMB million	RMB million
Installation costs	**2,847**	3,525
Others	**396**	441
	3,243	3,966

26 Discontinued operations

On January 15, 2007, CNC China, entered into an assets transfer agreement with it's ultimate holding Company, China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality branches. The disposal was completed on February 28, 2007. The gain on disposal amounted to RMB626 million. The results and cash flows of Guangdong and Shanghai Branches for the year ended December 31, 2007 and 2006 are presented as discontinued operations.

On June, 2, 2006, the Group entered into an agreement with third party buyers to dispose of its entire interest in the ANC Group for an aggregate cash consideration of US$168.84 million, or equivalent of RMB1,343.71 million. The disposal was completed on August 22, 2006. The gain on disposal amounted to RMB1,878 million. The results and cash flows of the ANC Group for the year ended December 31, 2006 are presented as discontinued operations.

The income statements and cash flow statements related to discontinued operations are as follows:

	Disposal of Guangdong and Shanghai Branches		Disposal of ANC Group		Total	
	For the period from January 1, 2007 to February 28, 2007	For the year ended December 31, 2006	**For the year ended December 31, 2007**	For the period from January 1, 2006 to August 22, 2006	**For the year ended December 31, 2007**	For the year ended December 31, 2006
	RMB million	RMB million	**RMB million**	RMB million	**RMB million**	RMB million
Discontinued operations						
Revenues	**615**	3,222	**—**	980	**615**	4,202
Expenses	**(618)**	(3,717)	**—**	(1,038)	**(618)**	(4,755)
Loss before taxation of discontinued operations	**(3)**	(495)	**—**	(58)	**(3)**	(553)
Taxation	**1**	163	**—**	(1)	**1**	162
Loss for the period of discontinued operations	**(2)**	(332)	**—**	(59)	**(2)**	(391)
Gain on disposal of discontinued operations before taxation	**927**	—	**—**	1,878	**927**	1,878
Taxation	**(301)**	—	**—**	—	**(301)**	—
Gain on discontinued operations after taxation	**626**	—	**—**	1,878	**626**	1,878
Profit/(loss) for the period/year from discontinued operations	**624**	(332)	**—**	1,819	**624**	1,487

26 Discontinued operations *(continued)*

	Disposal of Guangdong and Shanghai Branches		Disposal of ANC Group		Total	
	For the period from January 1, 2007 to February 28, 2007	For the year ended December 31, 2006	**For the year ended December 31, 2007**	For the period from January 1, 2006 to August 22, 2006	**For the year ended December 31, 2007**	For the year ended December 31, 2006
	RMB million	RMB million	**RMB million**	RMB million	**RMB million**	RMB million
Discontinued operations						
Net cash inflow from operating activities	**388**	1,902	**—**	183	**388**	2,085
Cash outflow from investing activities	**(374)**	(1,903)	**—**	(182)	**(374)**	(2,085)
Cash inflow from disposal of discontinued operations	**3,477**	—	**—**	1,164	**3,477**	1,164
Net cash inflow/(outflow) from investing activities	**3,103**	(1,903)	**—**	982	**3,103**	(921)
Net cash inflow from financing activities	**—**	—	**—**	—	**—**	—
Cash flow from discontinued operations	**3,491**	(1)	**—**	1,165	**3,491**	1,164

27 Investments in subsidiaries and due from/(to) subsidiaries

	Company As at December 31	
	2007	2006
	RMB million	RMB million
Investment cost in subsidiaries	**71,000**	62,937
Due from subsidiaries (Note (b))	**10,490**	9,411
Due to subsidiaries (Note (c))	**(14,271)**	(12,754)
	67,219	59,594

27 Investments in subsidiaries and due from/(to) subsidiaries *(continued)*

Notes:

(a) As at December 31, 2007, the Company has direct interests in the following subsidiaries, which are private companies:

Company name	Place and date of incorporation/ establishment	Registered capital	Percentage of equity interest attributable to the Company	Principal activities and place of operation
Directly held:				
China Netcom (Group) Company Limited (Note (i))	PRC, August 6, 1999	RMB 73,371 million	100%	Provision of network communications services in the PRC
China Netcom Corporation International Limited	Bermuda October 15, 2002	USD 12,000	100%	Provision of Investing Service in Bermuda
Indirect held:				
China Netcom Group System Integration Limited Corporation (Note (ii))	PRC April 30, 2006	RMB50 million	100%	Provision of Information Communications Technology Services in PRC
China Netcom Broadband Online Limited Corporation (Note (ii))	PRC March 29, 2006	RMB30 million	100%	Provision of Internet Information services and value-added telecommunications services in PRC
Beijing Telecommunications Planning and Designing Institute Corporation Limited (Note (iii))	PRC June 1, 2007	RMB264,227,115	100%	Provision of telecommunications network construction, planning and technical consulting services in PRC

(i) The company is a wholly owned foreign enterprise established in the PRC. The accounts of the company for the years ended December 31, 2006 and 2007 were audited by PricewaterhouseCoopers Zhong Tian CPAs Limited Company.

(ii) These companies are wholly owned domestic enterprises established in the PRC. The accounts of these companies for the years ended December 31, 2006 and 2007 were audited by PricewaterhouseCoopers Zhong Tian CPAs Limited Company, respectively.

(iii) The company is a wholly owned domestic enterprise established in the PRC. The accounts of the company for the year ended December 31, 2007 were audited by PricewaterhouseCoopers Zhong Tian CPAs Limited Company.

(b) The balances are unsecured, non-interest bearing and have no fixed repayment terms.

(c) The balances mainly represent deferred payments arising from the Acquisition of New Horizon which have been transferred to CNC China at the carrying amount. The balances are unsecured, non-interest bearing and have no fixed repayment terms

28 Accounts payable

	As at December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
0-30 days	**6,214**	5,763
31-60 days	**1,462**	2,236
61-90 days	**1,266**	1,449
91-180 days	**2,251**	2,990
Over 180 days	**4,446**	5,223
Total	**15,639**	17,661

Included in accounts payable are amounts due to other state-owned telecommunications operators amounting to RMB23 million on December 31, 2007 (2006: RMB97 million).

29 Accruals and other payables

	Group		Company	
	As at December 31		As at December 31	
	2007	2006	**2007**	2006
	RMB million	RMB million Restated Note 2	**RMB million**	RMB million
Interest payable	**441**	106	**—**	—
Payroll payable	**493**	588	**—**	—
Accruals and other payables	**2,016**	2,380	**46**	136
	2,950	3,074	**46**	136

30 Bank and other loans

(a) (i) CNC China issued two lots of RMB10 billion unsecured commercial paper with repayment periods of 1 year and 270 days on April 30, 2007 and September 18, 2007 in the PRC capital market respectively. The effective interest rates are 3.34% and 3.93% respectively. The aggregated net cash proceeds raised in these exercises is RMB20 billion.

The book value of above said commercial paper approximates fair value which derives from discounted cash flow at 3.93%.

On July 20, 2006, the Group issued RMB10 billion one-year non-interest bearing unsecured commercial paper in the PRC capital market and raised net cash proceeds of RMB9,676 million from this exercise. The commercial paper is interest bearing at effective rate of 3.35%. The commercial paper was fully repaid on July 24, 2007.

(ii) The short term bank loans on December 31, 2007 were unsecured and comprise:

		As at December 31	
Currency	**Interest rate and final maturity**	**2007**	2006
		RMB million	RMB million
RMB denominated	Interest rates ranging from 4.86% to 6.72% per annum with maturity through December 11, 2008	**11,850**	30,980

The carrying values of short term bank loans approximate their fair values which are based on cash flows discounted using market rate of 4.86%-6.72% (December 31, 2006: 4.86%-5.51%).

Included in the short-term bank loans were loans from state-owned banks amounting to RMB11,140 million as at December 31, 2007 (December 31, 2006: RMB29,700 million).

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

		As at December 31	
		2007	2006
	Note	**RMB million**	RMB million
Long term bank loans	(i)	**19,645**	29,560
Finance lease obligations	(ii)	**102**	963
		19,747	30,523
Less: Current portion		**(5,322)**	(7,304)
		14,425	23,219

The carrying values of the current portion of long term bank loans approximate their fair values which are based on cash flows discounted using market rate of 7.47% (December 31, 2006: 6.12%).

Included in the long term bank loans were loans from state-owned banks amounting to RMB19,645 million as at December 31, 2007 (2006: RMB29,560 million).

30 Bank and other loans *(continued)*

(i) Long term bank loans

	As at December 31	
	2007	2006
	RMB million	RMB million
Loans		
Unsecured	**19,433**	29,220
Secured	**212**	340
Total	**19,645**	29,560
Less: Current portion	**(5,220)**	(6,446)
Long term loans	**14,425**	23,114

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Within one year	**5,220**	6,446
In the second year	**9,671**	6,491
In the third to fifth year, inclusive	**1,952**	9,723
After the fifth year	**2,802**	6,900
	19,645	29,560

30 Bank and other loans *(continued)*

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

Currency	Interest rate and final maturity	As at December 31 2007	2006
		RMB million	RMB million
Bank loan			
Renminbi denominated	Interest rates ranging from 2.4% to 10.08% per annum with maturity through January 29, 2022	**18,399**	28,128
US Dollar denominated	Interest rates ranging from 1.5% to 6.15% per annum with maturity through October 31, 2039	**588**	721
Japanese Yen denominated	Interest rate is 2.12% per annum with maturity through January 7, 2014	**234**	276
Euro denominated	Interest rates ranging from 1.10% to 7.85% per annum with maturity through March 15, 2034	**415**	435
Hong Kong Dollar denominated	Interest rates is 3.75% per annum with maturity through December 31, 2010	**9**	—
		19,645	29,560

As at December 31, 2007, bank loans of RMB212 million (December 31, 2006: RMB340 million) were secured by the following:

- Corporate guarantees granted by China Netcom Group to the extent of RMB49 million (December 31, 2006: RMB65 million); and
- Corporate guarantees granted by third parties to the extent of RMB163 million (December 31, 2006: RMB275 million).

30 Bank and other loans *(continued)*

(ii) Finance lease obligations

	As at December 31	
	2007	2006
	RMB million	RMB million
Obligation under finance leases	**102**	963
Less: current portion	**(102)**	(858)
	—	105

The accumulated finance lease obligation payable to the related parties as at December 31, 2007 amounted to RMB102 million. (2006: RMB963 million).

The interest rates charged on finance lease are ranging from 5.18% to 5.7% with maturity through December 8, 2008 (2006: 2.68% to 6.83% with maturity through December 8, 2008)

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Within one year	**105**	888
In the second year	**—**	106
	105	994
Less: future finance charges on finance leases	**(3)**	(31)
Present value of finance lease liabilities	**102**	963
The present value of finance lease liabilities is as follows:		
Within one year	**102**	858
In the second year	**—**	105
	102	963

30 Bank and other loans *(continued)*

(c) Corporate bonds

On June 8, 2007, the Group issued RMB2 billion ten-year corporate bonds, bearing interest at 4.5% per annum. The corporate bonds are secured by a corporate guarantee granted by Bank of China Limited.

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Long term bank loans	**12,320**	21,209
Finance lease obligations	**—**	85
	12,320	21,294

The fair value is based on cash flows discounted using rates based on the market rates ranging from 3.25% to 7.05% (December 31, 2006: 3.75% to 8.33%).

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

		Group		Company	
		As at December 31		As at December 31	
		2007	2006	**2007**	2006
	Note	**RMB million**	RMB million Restated Note 2	**RMB million**	RMB million
Current:					
Due from ultimate holding company	(a)	**245**	174	**–**	–
Due from intermediate holding companies	(a)	**6**	3	**–**	–
Due from fellow subsidiaries	(a)	**96**	181	**–**	–
Total		**347**	358	**–**	–
Due to ultimate holding company					
-Deferred consideration	(b)	**1,960**	1,960	**–**	–
-Others	(a)	**1,371**	3,282	**–**	–
Due to fellow subsidiaries	(a)	**1,267**	2,263	**–**	–
Total		**4,598**	7,505	**–**	–
Non-current:					
Due to ultimate holding company					
-Deferred consideration	(b)	**3,920**	5,880	**–**	–
Due to intermediate holding companies	(c)	**78**	—	**78**	–
Due to fellow subsidiaries	(c)	**2,171**	—	**325**	–
Total		**6,169**	5,880	**403**	–

31 Amount due from/(to) holding companies and fellow subsidiaries *(continued)*

Note:

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

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Within one year	**1,960**	1,960
In the second year	**1,960**	1,960
In the third to fifth year, inclusive	**1,960**	3,920
Total	**5,880**	7,840

(c) The balances bear interest rates ranged from 3.0% to 3.8% per annum, unsecured and have repayment terms of 3 years. The fair value of the balances is RMB1,918 million.

32 Deferred revenues

	As at December 31	
	2007	2006
	RMB million	RMB million
Balance at beginning of year:		
-upfront connection fees	**3,099**	5,505
-upfront installation fees	**5,767**	6,769
-advances from network capacity sales	**—**	2,354
-prepaid telephony services	**5,065**	4,272
-others	**—**	—
	13,931	18,900
Additions for the year:		
-upfront connection fees	**—**	—
-upfront installation fees	**226**	357
-advances from network capacity sales	**—**	236
-prepaid telephony services	**31,749**	30,360
-others	**86**	—
	32,061	30,953
Reductions for the year:		
-upfront connection fees	**(1,517)**	(2,406)
-upfront installation fees	**(1,279)**	(1,359)
-advances from network capacity sales	**—**	(2,590)
-prepaid telephony services	**(31,777)**	(29,567)
-others	**(2)**	—
	(34,575)	(35,922)
Included: Disposal of discontinued operations		
-advances from network capacity sales	**—**	(2,450)
-prepaid telephony services	**(183)**	(144)
	(183)	(2,594)
Balance at end of year:		
-upfront connection fees	**1,582**	3,099
-upfront installation fees	**4,714**	5,767
-advances from network capacity sales	**—**	—
-prepaid telephony services	**5,037**	5,065
-others	**84**	—
	11,417	13,931
Representing:		
- Current portion	**7,103**	7,733
- Non-current portion	**4,314**	6,198
	11,417	13,931

33 Provisions

	Early retirement benefits	One-off cash housing subsidies	Total
	RMB million	RMB million	RMB million
	Note b	Note a & b	
As at January 1, 2007	3,137	3,185	6,322
Additional provisions	—	—	—
Payments during the year	(605)	(329)	(934)
As at December 31, 2007	2,532	2,856	5,388
Analysis of total provisions:			
-Current portion	525	2,856	3,381
-Non-current portion	2,007	—	2,007
	2,532	2,856	5,388
As at January 1, 2006	3,763	3,440	7,203
Payments during the year	(626)	(255)	(881)
As at December 31, 2006	3,137	3,185	6,322
Analysis of total provisions:			
-Current portion	551	3,185	3,736
-Non-current portion	2,586	—	2,586
	3,137	3,185	6,322

(a) Certain staff quarters, prior to 1998, have been sold to the Group's employees at preferential prices, subject to a number of eligibility requirements. In 1998, the State Council issued a circular which stipulated that the sale of quarters to employees at preferential prices should be terminated. In 2000, the State Council issued a further circular stating that cash subsidies should be made to certain eligible employees following the withdrawal of the allocation of staff quarters. However, the specific timetable and procedures for the implementation of these policies were to be determined by individual provincial or municipal government based on the particular situation of the provinces or municipality.

Based on the relevant detailed local government regulations promulgated, certain entities within the Group have adopted cash housing subsidy plans. In accordance with these plans, for those eligible employees who had not been allocated with quarters or who had not been allocated with quarters up to the prescribed standards before the discounted sales of quarters were terminated, the Group is required to pay them one-off cash housing subsidies based on their years of service, positions and other criteria. Based on the available information, the Group estimated the required provision for these cash housing subsidies amounting to RMB4,142 million, which was charged to the income statement in the year ended December 31, 2000 (the year in which the Council circular in respect of cash subsidies was issued).

33 Provisions *(continued)*

(b) Pursuant to the Listing Reorganisation and the Acquisition of New Horizon, if the actual payments required for these subsidies and early retirement benefits differ from the amount provided as at June 30, 2004 and June 30, 2005, China Netcom Group will bear any additional payments required or will be paid the difference if the actual payments are lower than the amount provided.

34 Deferred taxation

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

	Balance at December 31 2006	Recognised in income statement: Discontinued operations -Disposed Guangdong and Shanghai Branches	Recognised in income statement: Continuing operations Note 11	Recognised in income statement: Change in statutory tax rate Note 11	Change in statutory Tax rate and recognised in equity Note11	Disposal of Guangdong and Shanghai Branches	Balance at December 31 2007
	RMB million Restated Note 2	RMB million	RMB million	RMB million	RMB million	RMB million	RMB million
Deferred tax assets:							
Deferred revenue, primarily advances from customers	127	—	(11)	(24)	—	—	92
Temporary differences from allowance for doubtful debts	314	(5)	73	(38)	—	(13)	331
Unrecognised revaluation surplus/(deficit)	2,810	—	(104)	—	(664)	20	2,062
Others	208	—	53	(49)	—	(4)	208
Balance at end of year	3,459	(5)	11	(111)	(664)	3	2,693
Deferred tax liabilities:							
Interest capitalized	(789)	—	109	168	—	—	(512)
Fixed assets depreciation	(301)	—	(55)	(15)	111	(28)	(288)
Others	(66)	—	1	9	—	—	(56)
Balance at end of year	(1,156)	—	55	162	111	(28)	(856)
The amounts in the consolidated balance sheet are as follows:							
Deferred tax assets to be recovered after more than 12 months	2,860						2,038
Deferred tax liabilities to be settled after more than 12 months	(1,014)						(740)

34 Deferred taxation *(continued)*

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

34 Deferred taxation *(continued)*

Note:

(i) According to the Group's accounting policy as set out in note 4(k), the fixed assets other than the lease prepayments for land and buildings of the Group were revalued by the PRC valuer on a depreciated replacement cost basis on December 31, 2006, as disclosed in note 21. The revalued amounts are not used to determine the tax bases of these assets in the future years. Accordingly, the Group's deferred tax liabilities on the balance sheet as at December 31, 2006, decreased by RMB150million. The net reduction comprised RMB353 million, being the deferred tax liabilities originated from the revaluation surplus of fixed assets which was debited to revaluation reserves, offset by RMB503 million, being the deferred tax assets originated from the revaluation deficit of fixed assets which was credited to the income statement for the year ended December 31, 2006.

(ii) In connection with the Listing Reorganisation and the Acquisition of New Horizon, certain of the Group's telecommunication networks and equipment and furniture, fixtures, motor vehicles and other equipment were revalued as at December 31, 2003 and 2004. Such revalued amounts determine the tax bases for these assets for future years. In addition, except for the item described in Note (iii) below, the tax bases of certain assets and liabilities have been adjusted to the revalued amounts incorporated as the carrying values in the balance sheet.

In connection with the Acquisition of New Horizon, the Group's net deferred tax assets were subsequently reduced by RMB1,077 million (comprising deferred tax assets of RMB1,273 million and deferred tax liabilities of RMB196 million), and this decrease was recorded as a debit to owners' equity upon the date of the Reorganisation on June 30, 2005. The RMB1,077 million deduction comprises RMB1,097 million, being deferred tax liabilities originating from the revaluation surplus of fixed assets recorded and credited to revaluation reserves offset by RMB2,174 million deferred tax assets debited to retained earnings.

(iii) In addition, in order to determine the tax bases used for future years after the Listing Reorganisation and the Acquisition of New Horizon, the Group's prepayments for the leasehold land and buildings were revalued for PRC tax purposes as at December 31, 2003 and 2004. However, the resulting revaluations of the prepayments for the leasehold land and buildings were not incorporated into the consolidated financial statements. As a result, deferred tax assets were subsequently recorded with corresponding increases in owners' equity upon the Listing Reorganisation on June 30, 2004 and the Acquisition of New Horizon on June 30, 2005. In the opinion of the directors, it is more likely than not that the Group will realize the benefits of the deferred tax asset after making reference to the historical taxable income of the Group. The amount is to be transferred to retained earnings upon the corresponding realization of the underlying deferred tax assets.

During the Listing Reorganisation, the leasehold land and buildings had a net surplus on revaluation of RMB6,967 million as at December 31, 2003. As explained in the preceding paragraph, a deferred tax asset of RMB2,355 million was subsequently recorded with a corresponding increase in owner's equity upon the Listing Reorganisation on June 30, 2004.

During the Acquisition of New Horizon, the leasehold land and buildings had a net surplus on revaluation of RMB2,553 million as at December 31, 2005. As explained above, a deferred tax asset of RMB843 million was subsequently recorded with a corresponding increase in owner's equity upon the Acquisition on June 30, 2005.

The amount of transfer to retained earnings from unrecognised revaluation surplus and deficit for the year ended December 31, 2007 was RMB104 million. (2006: RMB51 million).

35 Share capital

	Authorized							
	Ordinary shares of US$0.04 each			Convertible preference shares of US$0.04 each			Total	
	No. of shares	US$	RMB Million	No. of shares	US$	RMB Million	US$	RMB Million
As at January 1, 2006, 2007 and December 31, 2007	25,000,000,000	1,000,000,000	8,277	7,741,782	309,671	3	1,000,309,671	8,280

	Issued							
	Ordinary shares of US$0.04 each			Convertible preference shares of US$0.04 each			Total	
	No. of shares	US$	RMB million	No. of shares	US$	RMB Million	US$	RMB Million
As at January 1, 2006	6,593,529,000	263,741,160	2,181	—	—	—	263,741,160	2,181
Exercise of share options(Note)	57,114,500	2,284,580	18	—	—	—	2,284,580	18
As at December 31, 2006	6,650,643,500	266,025,740	2,199	—	—	—	266,025,740	2,199
As at January 1, 2007	6,650,643,500	266,025,740	2,199	—	—	—	266,025,740	2,199
Exercise of share options(Note)	23,684,900	947,396	7	—	—	—	947,396	7
As at December 31, 2007	6,674,328,400	266,973,136	2,206	—	—	—	266,973,136	2,206

Note:

The Group issued new shares for the options exercised during this period. During the year ended December 31, 2007, the Company issued 16,231,400 shares (2006: 57,114,500 shares) upon exercise of options by participants in the First Grant Share Option Scheme, and issued 7,453,500 shares (2006: 0 shares) upon exercise of options by participants in the Second Grant Share Option Scheme. The total consideration received amounted to RMB219 million and the portion that exceeds the nominal value of the shares issued was recorded as share premium of the Company.

36 Share option scheme

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

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

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

On December 6, 2005, the board of directors approved the grant of 79,320,000 shares of share options to certain management personnel and other professional personnel designated by the Compensation Committee of the newly acquired four northern provinces/autonomous region ("Second Grant"). The grantees can exercise 40% of the option granted from December 6, 2007, and all unexercised share options will be expired on December 5, 2011.

The grant date fair value of the share options granted in the First Grant is determined by the Black-Scholes model based on the following assumptions: expected dividend pay-out ratio of 35%, expected vesting period of 5 years, expected volatility rate of 23.6% and risk-free interest rate of 4.3%. The weighted average fair value of the share options on grant date was determined as HK$ 1.22 per share (RMB1.28 per share). The grant date fair value of the share options granted in the Second Grant is determined by the Black-Scholes model based on the following assumptions: expected dividend pay-out ratio of 35%, expected vesting period of 4 years, expected volatility rate of 21.46% and risk-free interest rate of 4.3%. The weighted average fair value of the share option on grant date was determined as HK$1.28 per share (RMB1.34 per share). The model that decided the weighted average fair value of the share options and the assumptions mentioned above are subjective, and the changes of these subjective assumptions could affect the weighted average fair value of the share option. Therefore, Black-Scholes model may not reliably calculate the weighted average fair value of the share options.

Modifications to certain clauses of the share options schemes already granted were approved on May 16, 2006, pursuant to a resolution of the Extraordinary General Meeting. The modifications were mainly related to eligibility of the participants, number of options and exercise vesting schedules, rights upon cessation of employment, death and loss of capacity, performance targets, and cancellation of options. The modifications did not have significant impact to the financial statements.

36 Share option scheme *(continued)*

The movement of the share options granted during the year is summarized as follows:

	No. of share options							
	As at January 1 2006	Granted	Exercised	Lapsed and forfeited	As at December 31 2006	Exercise price HK$	Weighted average closing price per share at respective days immediately before the exercises of options HK$	No. of share option exercisable as at December 31 2006
First Grant	156,703,000	—	57,114,500	1,975,800	97,612,700	8.40	14.46	5,670,084
Second Grant	79,320,000	—	—	285,800	79,034,200	12.45	—	—
Total	236,023,000	—	57,114,500	2,261,600	176,646,900			5,670,084

	No. of share options							
	As at January 1 2007	Granted	Exercised	Lapsed and forfeited	As at December 31 2007	Exercise price HK$	Weighted average closing price per share at respective days immediately before the exercises of options HK$	No. of share option exercisable as at December 31 2007
First Grant	97,612,700	—	16,231,400	2,117,440	79,263,860	8.40	22.23	20,728,290
Second Grant	79,034,200	—	7,453,500	—	71,580,700	12.45	23.92	24,490,320
Total	176,646,900	—	23,684,900	2,117,440	150,844,560			45,218,610

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

The compensation cost recognised in staff cost during the year ended December 31, 2007 was RMB59 million (For year ended December 31, 2006: RMB75 million). As at December 31, 2007, there was RMB47 million (As at December 31, 2006, there was RMB106million) of unrecognised compensation cost, adjusted for estimated forfeitures, related to non-vested share-based awards granted to the Company's employees. This cost is expected to be recognised over a weighted-average period of 1.31 years. Total unrecognised compensation cost may be adjusted for future changes in estimated forfeitures.

36 Share option scheme *(continued)*

There were no capitalised share-based compensation costs during the year ended December 31, 2007 and 2006.

The intrinsic value for the options exercised amounted to HK$ 656 million and was calculated as the difference between the market value on the date of exercise and the exercise price of the shares. The intrinsic value of options outstanding as of December 31, 2007 amounted to HK$ 1,980 million (December 31, 2006: 1,879 million), which was calculated as the difference between the closing stock price as of June 30 2007 and the exercise price of the share options.

The weighted average remaining contractual life for outstanding options, vested and expected to vest or exercisable options as of December 31, 2007 were 3.38 years and 3.45 years (as of December 31, 2006 was 4.35 years and 3.88 years), respectively.

37 Reserves - Company

	Share premium	**Capital reserve**	**Retained earnings**	**Total**
	RMB million	RMB million	RMB million	RMB million
As at January 1, 2006	42,750	3,104	(1,381)	44,473
Profit for the year	—	—	17,475	17,475
Dividends distributed during the year (Note 13)	—	—	(3,196)	(3,196)
Share based payments	545	(73)	—	472
Exercise of share options	—	75	—	75
As at December 31,2006	43,295	3,106	12,898	59,299
Profit for the year	—	—	8,714	8,714
Dividends distributed during the year (Note 13)	—	—	(3,600)	(3,600)
Share based payments	243	(31)	—	212
Exercise of share options	—	59	—	59
As at December 31, 2007	43,538	3,134	18,012	64,684

38 Consolidated cash flow statements

(a) Reconciliation of profit before taxation to net cash flows generated from the operating activities of continuing operation

	Year ended December 31	
	2007	2006
	RMB million	RMB million Restated Note 2
Profit before taxation	**15,267**	15,205
Adjusted by:		
Depreciation of fixed assets and amortisation of intangible assets	**25,402**	24,845
Lease prepayments for land	**52**	68
Lease prepayments for network capacity	**6**	—
Deferred costs charged to the income statement	**876**	996
Deficit on revaluation of fixed assets	**—**	1,335
Bad and doubtful debts	**868**	1,003
(Gain)/loss on disposal of fixed assets	**(357)**	432
Share-based payments	**59**	75
Other income	**(1,221)**	(621)
Interest income	**(113)**	(136)
Interest expense	**3,162**	3,757
Foreign exchange net loss/(gain)	**25**	(8)
Changes in working capital		
Increase in accounts receivable	**(1,357)**	(1,944)
Decrease in inventories and consumables	**120**	56
Decrease in prepayments, other receivables and other current assets	**142**	229
Increase in other non-current assets	**(201)**	(339)
Increase in accounts payable	**1,285**	1,142
Decrease in accruals and other payables	**(2,384)**	(4,308)
Decrease in deferred revenues	**(2,322)**	(2,631)
Net cash inflow generated from operating activities of continuing operations	**39,309**	39,156

(b) Major non-cash transactions

During 2005, the Group paid RMB3,000 million as part of the total consideration for the Acquisition of the New Horizon. The remaining balance of RMB9,800 million was recognised as a deferred payment and is included in amounts due to the ultimate holding company. During the year ended December 31, 2007, payments made in respect of the purchase were RMB1,960 million, the unpaid balance at December 31, 2007 was RMB5,880 million.

In 2007, the Group replaced copper cables in some network infrastructure with optical fibers and related equipments. Some of this replacement was done through non-monetary assets exchange with suppliers, which it exchanged optical fibers and related equipments for the Group's own copper cables. The cost of the assets received was recorded at the fair value of asset surrendered. In 2007, the net book value and fair value of copper cables surrendered were RMB182 million and RMB568 million respectively. A gain on the non-monetary assets exchange of RMB386 million is recognized in the current year income statement.

(c) Net investment gain from disposal of Guangdong and Shanghai branches

On January 15, 2007, CNC China entered into an assets transfer agreement with it's ultimate holding Company, China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality branches. The disposal was completed on February 28, 2007. The net assets of Guangdong and Shanghai Branches as at the completion date are as listed below:

	As at February 28, 2007
	RMB million
Net assets disposed of (excluding the cash and cash equivalents):	
Accounts receivable and other current assets	416
Fixed assets and other non-current assets	7,630
Current portion of deferred income	(183)
Accounts payable	(2,046)
Long-term loans	(3,000)
Other liabilities	(267)
	2,550
Gain on disposal recognised in the income statement	927
Net cash inflow from disposal of Guangdong and Shanghai Branches	3,477
Analysis of cash inflow from disposal of Guangdong and Shanghai Branches	
Cash consideration	3,500
Less: Cash and cash equivalents of Disposed Guangdong and Shanghai Branches	(23)
Net cash inflow	3,477

39 Banking facilities

As at December 31, 2007 and 2006, the utilized and unutilized banking facilities are as follows:

	Group		Company	
	As at December 31		As at December 31	
	2007	2006	**2007**	2006
	RMB million	RMB million	**RMB million**	RMB million
Amount utilized	**31,495**	60,541	**9**	—
Amount unutilized	**106,824**	115,588	**2,238**	—
Aggregate banking facilities	**138,319**	176,129	**2,247**	—

40 Commitments

(a) Capital commitments

	As at December 31	
	2007	2006
	RMB million	RMB million
Contracted but not provided for		
- Leasehold land and buildings	**10**	26
- Telecommunication networks and equipment	**530**	2,502
- Others	**9**	5
Total	**549**	2,533
Authorized but not contracted for		
- Leasehold land and buildings	**21**	—
- Telecommunication networks and equipment	**106**	300
- Others	**1**	—
	128	300

40 Commitments *(continued)*

(b) Operating lease commitments

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

	As at December 31	
	2007	2006
	RMB million	RMB million
Not later than one year	**579**	734
Later than one year and not later than five years	**1,134**	1,102
Later than five years	**291**	517
Total	**2,004**	2,353

41 Related party transactions

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

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

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

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

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

41 Related party transactions *(continued)*

	Note	For the year ended December 31 2007 RMB million	2006 RMB million Restated Note 2
Emolument of key management			
- salaries and welfare and contributions to retirement scheme	(i)	13	13
Interconnection fees			
- from fellow subsidiaries	(iv)(b)	602	381
- from other state-owned telecommunications operators	(iv)(b)	6,333	6,726
Subtotal		6,935	7,107
Interconnection charges			
- to fellow subsidiaries	(iv)(b)	687	820
- to other state-owned telecommunications operators	(iv)(b)	1,595	1,758
Subtotal		2,282	2,578
Rental income from properties leased to fellow subsidiaries	(iv)(a),(iv)(c)	1	2
Purchase of materials			
- from fellow subsidiaries	(iv)(a),(iv)(c)	569	1,170
- from other related companies	(iv)(a),(iv)(c)	99	122
Subtotal		668	1,292
Receipt of engineering, project planning, design, construction and information technology services			
- from fellow subsidiaries	(iv)(a),(iv)(b)	1,629	2,084
- from other related companies	(iv)(a),(iv)(b)	317	368
Subtotal		1,946	2,452
Provision of engineering, project planning, design, construction and information technology services			
- from other state-owned telecommunications operators	(iv)(a)	54	45
Ancillary telecommunications support services			
- from fellow subsidiaries	(v),(iv)(a)	373	350
- from other related companies	(v),(iv)(a)	75	58
Subtotal		448	408

41 Related party transactions *(continued)*

	Note	For the year ended December 31 2007 RMB million	2006 RMB million Restated Note 2
Payment of operating lease rentals of premises			
- to fellow subsidiaries	(iv)(a),(iv)(c)	**636**	680
Property sub-lease rentals to fellow subsidiaries	(iv)(a),(iv)(c)	**11**	15
Common corporate services income from ultimate holding company	(vi)	**125**	121
Common corporate services expenditure paid to ultimate holding company	(vi)	**477**	448
Support services received			
- from ultimate holding company	(vii),(iv)(a)	**—**	2
- from fellow subsidiaries	(vii),(iv)(a)	**496**	712
- from other related companies	(vii),(iv)(a)	**40**	23
Subtotal		**536**	737
Telecommunications rental income from other state-owned telecommunications operators	(iv)(b)	**723**	1,327
Payment for lease of Telecommunications facility			
- to ultimate holding company	(viii)	**66**	75
- to fellow subsidiaries	(viii)	**243**	307
Subtotal		**309**	382
Payment for purchase of long-term telecommunications capacity to fellow subsidiaries	(ix),(xii)	**—**	36
Payment for lease of long-term telecommunications capacity to fellow subsidiaries	(x),(xii)	**—**	65
Management fee received from fellow subsidiaries	(xi),(xii)	**—**	23
Information communication technologies service received			
- from ultimate holding company	(xix),(iv)(a)	**71**	2
- from fellow subsidiaries	(xix),(iv)(a)	**61**	60
Subtotal		**132**	62

41 Related party transactions *(continued)*

Notes:

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

(ii) The Group entered into finance lease arrangements with a related party, details have been set out in Note 30 (b)

(iii) Related party represents the non-listed investors of the fellow subsidiaries.

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

(a) market price;

(b) prices based on government guidance; or

(c) cost plus basis.

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

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

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

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

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

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

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

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

41 Related party transactions *(continued)*

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

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

(xv) As at December 31, 2007, China Netcom Group granted corporate guarantees to the Group as set out in Note 30(b).

(xvi) China Netcom Group, the Group's ultimate holding company, entered into an agreement (the "Sponsorship Agreement") with Beijing Organization Committee ("BOCOG") which designated China Netcom Group as the exclusive fixed-line telecommunications services partner in the People's Republic of China ("PRC") to sponsor the 2008 Beijing Olympic Games. China Netcom Group allocated the sponsorship fee to its members based on the estimated future benefits derived from the Sponsorship Agreement to respective members and the Group has contributed a portion of the required support under the Sponsorship Agreement through cash payment and provision of services to BOCOG amounting to RMB0.54 billion. Accordingly, an intangible asset and a payable to the ultimate holding company of the said amount have been recognised on the Group's balance sheet.

(xvii) As at December 31, 2007, the Group has balances with other state-owned telecommunication service providers, cash deposited in and loans granted from state-owned banks as set out in Notes 18, 28, 17 and 30 respectively.

(xviii) Up to December 31, 2007, the deferred consideration in respect of the Acquisition of New Horizon paid to China Netcom Group amounted to RMB3,920 million, and the balance of the deferred consideration amounted to RMB5,880 million (2006: RMB7,840 million). The accumulated related interest charged to income statement up to December 31 2007 amounted to RMB942 million (2006: RMB567 million).

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

(xx) On December 31, 2006, the Group acquired some assets from China Netcom Group at an agreed price of RMB81 million.

(xxi) On January 15, 2007, CNC China entered into an assets transfer agreement with it's ultimate holding Company, China Netcom Group. Pursuant to the agreement, CNC China agreed to dispose of its assets and liabilities in relation to its telecommunications operations in Guangdong Province and Shanghai Municipality branches in the PRC for consideration of RMB3.5 billion. On February 14, 2007, the independent shareholders passed an ordinary resolution to approve the disposal. The disposal was completed on February 28, 2007 upon the approval granted from the Ministry of Information Industry ("MII"). For details, please refer to Note 26.

(xxii) On December 5, 2007, System Integration Corporation, a directly wholly owned subsidiary of CNC China, entered into an equity interest transfer agreement and agreed to acquire the entire equity interest of Beijing Telecom P&D Institute from China Netcom Group Beijing Communications Corporation at a consideration of RMB298.9 million. The acquisition was completed on December 31, 2007. The difference of the consideration paid and the net assets value of the Beijing Telecom P&D Institute is RMB61 million and recognised directly in the other reserve. For details, please refer to Note 2.

(xxiii) In 2007, the Group borrowed loans from fellow subsidiaries and other holding companies. For the related terms, please refer to Note 31(c).

42 Significant subsequent events

(i) After the balance sheet date the directors proposed a final dividend. Further details are disclosed in Note 13.

(ii) The Group borrowed two foreign currency loans of HK$ 1 billion each from a bank in Hong Kong on February 1 and February 4, 2008 respectively. Both of the loans will mature on December 31, 2008. The actual annual interest rates charged are 2.53% and 2.557%.

43 Ultimate holding party

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

44 Approval of financial statements

The financial statements were approved by the Board of Directors on March 25, 2008.

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

The effect on net profit/ (loss) of significant differences between HKFRS and U.S.GAAP for the years ended December 31, 2005, 2006 and 2007 is as follows:

	Note	Years ended December 31			
		2005	2006	**2007**	**2007**
		Restated Note 2	Restated Note 2		
		RMB million except share and per share data			US$ million Except per share data
Profit from continuing operations under HKFRS		14,350	11,478	**11,471**	**1,570**
U.S.GAAP adjustments:					
Revaluation of fixed assets	(a)	—	1,335	**—**	**—**
Depreciation of revalued fixed assets	(a)	(5,056)	(4,571)	**(4,472)**	**(612)**
Tax effect on the above adjustments	(b)	1,668	1,068	**1,476**	**202**
Change in statutory taxation rate	(b)	—	—	**484**	**66**
Profit from continuing operations under U.S.GAAP		10,962	9,310	**8,959**	**1,226**
(Loss)/profit from discontinued operations under HKFRS		(400)	1,487	**624**	**85**
U.S.GAAP adjustments:					**—**
Revaluation of fixed assets	(a)	—	189	**—**	**—**
Depreciation of revalued fixed assets	(a)	(54)	(48)	**(10)**	**(1)**
Tax effect on the above adjustments	(b)	18	(47)	**3**	**—**
Gain on disposal of Guangdong and Shanghai branches	(e)	—	—	**(626)**	**(85)**
(Loss)/profit from discontinued operations under US GAAP		(436)	1,581	**(9)**	**(1)**
Consolidated profit for the period under HKFRS		13,950	12,965	**12,095**	**1,655**
Consolidated profit for the period under U.S.GAAP		10,526	10,891	**8,950**	**1,225**

Supplementary Information for American Depositary Share Holders

	Note	2005	2006	**2007**	**2007**
		Years ended December 31			
		Restated Note 2	Restated Note 2		
		RMB million except share and per share data			US$ million Except per share data
Shares used in computing basic earnings per share (in million)		6,594	6,616	**6,657**	**6,657**
Shares used in computing diluted earnings per share (in million)		6,628	6,667	**6,738**	**6,738**
Earnings per share for profit from continuing operations attributable to shareholders of the Company for the year under U.S GAAP					
- Basic earnings per share		RMB1.66	RMB1.41	**RMB1.35**	**USD 0.18**
- Diluted earnings per share		RMB1.65	RMB1.40	**RMB1.33**	**USD 0.18**
(Loss)/earnings per share for (loss)/profit from discontinued operations attributable to shareholders of the Company for the year under U.S GAAP					
- Basic (loss) /earnings per share		RMB(0.07)	RMB0.24	—	—
- Diluted (loss) /earnings per share		RMB(0.07)	RMB0.24	—	—
Earnings per share for profit attributable to shareholders of the Company for the year under U.S GAAP					
- Basic earnings per share		RMB1.59	RMB1.65	**RMB1.35**	**USD 0.18**
- Diluted earnings per share		RMB1.58	RMB1.64	**RMB1.33**	**USD 0.18**

The effect on shareholders' equity of significant differences between HKFRS and U.S.GAAP as at December 31, 2005, 2006 and 2007 is as follows:

		Years ended December 31			
	Note	2005	2006	**2007**	**2007**
		RMB million Restated Note 2	RMB million Restated Note 2	**RMB million**	**US$ million**
Consolidated shareholders' equity under HKFRS		63,287	74,194	**82,052**	**11,233**
U.S.GAAP adjustments					
Revaluation of fixed assets	(a)	30,251	30,704	**30,704**	**4,203**
Disposal and depreciation of revalued fixed assets	(a)	(8,639)	(13,258)	**(17,740)**	**(2,429)**
Tax effect on the above adjustments	(b)	(7,132)	(5,757)	**(3,241)**	**(444)**
Consolidated shareholders' equity under U.S.GAAP		77,767	85,883	**91,775**	**12,563**

On June 2, 2006, the Group entered into an agreement with third party buyers to dispose of its 100% interest in the ANC Group and the transaction was completed on August 22, 2006. On January 15, 2007, the Group entered into an agreement with China Netcom Group to dispose its telecommunications assets, liabilities and operations in Guangdong Province and Shanghai Municipal branches and the transaction was completed on February 28, 2007. In accordance with HKFRS 5 "Non-current assets held for sales and discontinued operations" issued by the HKICPA, the results and cash flows of the operations of the ANC Group and Guangdong and Shanghai Branches are presented as discontinued operations. Accordingly, certain comparative figures of 2005 and 2006 have been restated.

On December 5, 2007, System Integration Corporation entered into an Equity Interest Transfer Agreement with China Netcom Group Beijing Communications Corporation, pursuant to which System Integration Corporation agreed to acquire the entire equity interest of Beijing Telecom P&D Institute from China Netcom Group Beijing Communications Corporation. Before the acquisition, Beijing Telecom P&D Institute was a wholly owned subsidiary of China Netcom Group Beijing Communications Corporation, which is a wholly owned subsidiary of China Netcom Group. Since China Netcom Group is the ultimate holding company of the Group, the acquisition is a business combination under common control. Therefore, the Group accounted for this acquisition using the pooling of interest method according to Accounting Guideline No. 5 - Merger Accounting for Common Control Transactions "AG 5". The acquired businesses and assets are recorded at book value as if the businesses and assets of Beijing Telecom P&D Institute have been owned by the Group from the earliest comparative period presented. Accordingly, the financial information for 2005 and 2006 has been restated.

(a) Revaluation of fixed assets

In the Listing Reorganisation, certain classes of fixed assets of the Group were revalued as at December 31, 2003. The revaluation was performed based on the depreciated replacement costs of the fixed assets and was not based upon the expected future cash flows of the fixed assets. The revaluation resulted in a charge of RMB25,778 million to the Group's income statement for the year ended December 31, 2003 with respect to the reduction in carrying amounts of certain fixed assets below their historical cost bases. In addition, a surplus arising from the revaluation of certain other fixed assets totaling RMB2,982 million has been credited to the revaluation reserve.

In 2005, the Group acquired telecommunications business and assets of the four northern provinces/autonomous region from China Netcom Group as set out in Note 1 to the Group's financial statements. The acquired fixed assets were revalued as at December 31, 2004. The revaluation was performed based on the depreciated replacement costs of the fixed assets and was not based upon the expected future cash flows of the fixed assets. The revaluation resulted in a charge of RMB11,318 million to the Group's income statement for the year ended December 31, 2004 with respect to the reduction in carrying amounts of certain fixed assets below their historical cost bases. In addition, a surplus arising from the revaluation of certain other fixed assets totaling RMB3,863 million has been credited to the revaluation reserve.

According to the Group's accounting policy under HKFRS as set out in Note4(k)(iii), certain classes of fixed assets of the Group were revalued at December 31, 2006. The revaluation was performed based on the depreciated replacement costs for fixed assets and was not based upon the expected future cash flows of the fixed assets. The revaluation resulted in a charge of RMB1,524 million to the Group's income statement for the year ended December 31, 2006 with respect to the reduction in carrying amounts of certain fixed assets below their historical cost bases. In addition, a surplus arising from the revaluation of certain other fixed assets totaling RMB1,071million has been credited to the revaluation reserve. The effect of the reduction in depreciation of the revalued assets amounted to RMB4,482 million in the year ended December 31, 2007 (2006: RMB4,619 million, 2005: RMB5,110 million).

Under U.S.GAAP, the carrying values of fixed assets are stated at their historical cost less accumulated depreciation and impairment loss without making reference to their respective depreciated replacement cost. An impairment loss on fixed assets is recorded under U.S.GAAP if the carrying value of such assets exceeds its future undiscounted cash flows resulting from the use of the assets and their eventual disposition. The future undiscounted cash flows of the Group's fixed assets, whose carrying amounts were reduced in connection with the Reorganisation, exceed the historical costs of such fixed assets and, therefore, no impairment of such assets is recognised under U.S.GAAP. Accordingly, the deficit on revaluation of fixed assets charged to the Group's income statement and the surplus credited to the revaluation reserve recorded under Hong Kong GAAP and the corresponding effect on the depreciation of the revalued assets in the subsequent periods are reversed for U.S.GAAP purposes.

(b) Deferred income tax

The amounts included in the reconciliation show the income tax effects of the differences between HKFRS and U.S.GAAP as described above.

HKFRS requires recognition of a deferred tax asset only to the extent that recovery of the deferred tax asset is probable, whereas U.S. GAAP requires full recognition of deferred tax assets, reduced by an appropriate valuation allowance if the recovery is less than 50% likely. Recognition of deferred tax asset previously not recognised under HKFRS is presented as a reversal of the valuation allowance under U.S. GAAP.

As set out in note 11 to the financial statements, the enterprise income tax rate for domestic enterprises will decrease from 33% to 25% with effect from January 1, 2008.

Under US GAAP, pursuant to the requirement of FAS109, all the adjustments in deferred tax arising from the change in taxation rate should be recognised in the income statement.

The impact as a result of the change of the tax rate to the deferred tax liability arising from the difference in the recognition of the carrying values of fixed assets apart from lease prepayments for land and building under and U.S. GAAP is a credit of RMB1,148 million to the income statement for the year ended 31 December 2007.

Besides, the write-down of net deferred tax assets generated from revaluation of lease prepayments for land and building of RMB664 million recognised in equity under HK GAAP should be recognised in the income statement under U.S. GAAP.

Therefore, the net impact on the income statement reconciliation in respect of change in statutory tax rate is an increase in profit of RMB484 million.

(c) Presentation of depreciation expense

Under HKFRS, depreciation expense can be excluded from “Network, operations and support” and separately disclosed on the face of the income statement.

Under U.S.GAAP, “Network, operations and support” expenses should include charges for depreciation of property, plant and equipment and amortisation of intangible assets. Industry practice adopted by the Chinese telecommunications sector is to present these costs of operations net of depreciations charges. In such circumstances, U.S.GAAP requires such facts to be highlighted on the face of the income statement.

(d) Presentation of amortisation of subscriber acquisition costs

Under HKFRS, amortisation of capitalized subscriber acquisition costs, being RMB1,887 million, RMB739 million and RMB0 million for the years ended December 31, 2005, 2006 and 2007 respectively is classified as selling expenses due to the marketing and promotional nature of the expenditure.

Under U.S.GAAP, amortisation of subscriber acquisition costs needs to be included in the item "Network, operations and support" expense for the Company.

(e) Gain on disposal of Guangdong and Shanghai branches

As set out in note 2 to the financial statements, the disposal of Guangdong and Shanghai Branches was completed on February 28, 2007. It is a disposal under common control. Under HKFRS, the gain on disposal was recognised in the income statement while under U.S. GAAP, the gain was recognised directly in the shareholders' equity in accordance with the requirement of FAS 141.

Other U.S.GAAP disclosures

(a) Comprehensive income

U.S.GAAP requires that all items that are required to be recognised as components of comprehensive income (including cumulative translation adjustment) be presented with the same prominence as other components in the financial statements. There are no material differences between total recognised gains and losses for the periods shown in the Consolidated Statements of Changes in Equity presented under HKFRS and U.S.GAAP comprehensive income, except for the differences between HKFRS and U.S.GAAP profit attributable to shareholders shown above.

(b) Recent HK Accounting Pronouncements

The HKICPA has issued a number of new and revised HKFRSs and HKFRS Interpretations ("HKFRS - Ints"), and HKAS and HKAS Interpretations ("HKAS - Ints") as set out in Note 3 to the Group's financial statements. Except The HK(IFRIC) - Int 13, 'Customer loyalty programmes', the Group did not early adopt any new statement of new or revised HKFRSs or HKFRS - Ints in the year ended December 31, 2007. The Group evaluated the impact of these new and revised HKFRSs and HKFRS - Ints as set out in Note 3.

(c) Recent U.S. Accounting Pronouncements

SFAS 157

In September 2006, the FASB issued SFAS 157, Fair Value Measurement. SFAS 157 defines fair value, establishes a framework for measuring fair value, and enhances disclosures about fair value measurements. The adoption of SFAS 157 will be effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Group is evaluating the impact adopting SFAS 157 will have on its financial statements.

In February 2008, the FASB issued FASB Stuff Position ("FSP") 157-2, Effective Date of FASB Statement No. 157. FSP 157-2 provides a one-year deferral of the effective date of FASB Statement 157, Fair Value Measurements, for nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed in financial statements at fair value on a recurring basis. The deferral is not available, however, to entities that issued interim or annual financial statements reflecting the measurement and disclosure provisions of Statement 157 before February 12, 2008.

SFAS 159

In February, 2007, the FASB issued SFAS 159 "The Fair Value Option for Financial Assets and Financial Liabilities-Including an amendment of FASB Statement No. 115". This statement permits all entities to choose to measure many financial instruments and certain other items at fair value at specified election dates. SFAS 159 will be effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The Group is currently evaluating the effect that the adoption of this statement will have on its consolidated results of operations and financial condition but does not expect it to have a material impact.

SFAS 141(Revised 2007)

In December 2007, the FASB issued FAS 141(Revised 2007) "Business Combinations" which replaces FASB Statement No. 141. This statement establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed in financial statements. This statement is effective as of the beginning of an entity's first fiscal year beginning after December 15, 2008.The Group is currently assessing the impact of adopting SFAS No. 141R on its consolidated results of operations and financial condition but does not expect it to have a material impact.

SFAS No. 160

In December 2007, the FASB issued SFAS No. 160, "Non-controlling Interests in Consolidated Financial Statement-amendments of ARB No. 51." SFAS No. 160 states that accounting and reporting for minority interests will be re-characterized as non-controlling interests and classified as a component of equity. The Statement also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the non-controlling owners. FAS 160 applies to all entities that prepare consolidated financial statements, except not-for-profit organizations, but will affect only those entities that have an outstanding non-controlling interest in one or more subsidiaries or that deconsolidate a subsidiary. This statement is effective as of the beginning of an entity's first fiscal year beginning after December 15, 2008. The Group is currently assessing the impact of adopting SFAS No. 160.

Financial Summary

Consolidated Balance Sheet information prepared under Hong Kong Financial Reporting Standards

	As at December 31,				
	2007	2006	2005	2004	2003
	RMB million	RMB million Restated Note 2	RMB million Restated Note 2	RMB million Restated Note 2	RMB million Restated Note 2
Fixed assets	**156,948**	168,141	168,760	166,994	181,734
Construction in progress	**3,990**	6,335	6,822	10,597	18,049
Other non-current assets	**9,982**	11,380	12,865	14,477	15,735
Cash and bank deposits	**5,395**	7,728	5,065	10,804	7,549
Other current assets	**10,113**	10,498	9,610	13,824	13,238
Total assets	**186,428**	204,082	203,122	216,696	236,305
Short-term bank loans	**11,850**	30,980	47,341	44,882	47,991
Accounts payable	**15,639**	17,661	16,726	21,128	20,196
Other current liabilities	**47,104**	42,192	34,337	40,082	50,217
Long-term bank and other loans	**14,425**	23,219	18,143	26,052	30,172
Deferred revenues	**4,314**	6,198	10,925	13,988	17,585
Other non-current liabilities	**11,044**	9,638	12,363	5,738	16,312
Total liabilities	**104,376**	129,888	139,835	151,870	182,473
Minority interest	**—**	—	—	—	3
Shareholders' equity	**82,052**	74,194	63,287	64,826	53,829
Total liabilities and shareholders' equity	**186,428**	204,082	203,122	216,696	236,305

Consolidated Cash Flow information prepared under Hong Kong Financial Reporting Standards

	Year ended December 31,				
	2007	2006	2005	2004	2003
	RMB million	RMB million Restated Note 2	RMB million Restated Note 2	RMB million Restated Note 2	RMB million Restated Note 2
Continuing operations:					
Net cash inflow from operating activities	**32,459**	32,050	32,191	32,696	29,163
Net cash outflow from investing activities	**(19,138)**	(24,051)	(22,993)	(26,893)	(32,800)
Purchase of fixed assets and construction in progress, repayments for leased land	**(20,684)**	(24,242)	(25,964)	(26,507)	(34,398)
Net cash inflow/(outflow) from financing activities	**(19,131)**	(6,477)	(14,746)	(2,237)	3,608
Discontinued operations					
Cash flow from discontinued operations	**3,491**	1,164	(132)	(349)	(355)
Increase/(decrease) in cash and cash equivalents	**(2,319)**	2,686	(5,680)	3,217	(384)

Financial Summary

Consolidated Income Statement information propoved under Hong Kong Financial Reporting Standards

	Year ended December 31,				
	2007	2006	2005	2004	2003
	RMB million	RMB million Restated Note 2	RMB million Restated Note 2	RMB million Restated Note 2	RMB million Restated Note 2
Revenues	**84,005**	84,194	83,927	81,051	76,709
Local usage fees	**19,989**	22,059	24,440	24,766	24,667
Monthly fees	**12,387**	16,546	18,170	17,941	16,476
Upfront installation fees	**1,283**	1,364	1,433	1,565	1,267
DLD usage fees	**8,769**	9,495	9,773	10,465	10,886
ILD usage fees	**791**	819	874	1,228	1,505
Value-added services	**6,114**	5,341	3,970	2,987	2,094
Interconnection fees	**8,376**	8,432	7,664	6,348	4,894
Upfront connection fees	**1,517**	2,406	3,405	4,346	5,122
Broadband service	**13,835**	9,916	7,289	5,033	2,815
Other Internet-related service	**532**	516	556	1,064	1,418
Managed data service	**1,284**	1,413	1,621	1,496	1,359
Leased line income	**2,521**	2,540	2,376	2,591	2,883
Information communications technology services	**3,990**	855	186	207	169
Other services	**2,617**	2,492	2,170	1,014	1,154
Operating expense	**(66,739)**	(64,643)	(62,868)	(62,569)	(64,106)
Depreciation and amortisation	**(25,495)**	(24,913)	(24,328)	(24,501)	(26,641)
Network, operations and support	**(14,145)**	(13,344)	(12,610)	(12,363)	(14,576)
Staff cost	**(12,223)**	(11,849)	(11,830)	(11,493)	(10,823)
Selling, general and administrative	**(10,615)**	(12,607)	(12,726)	(12,282)	(10,090)
Other operating expense	**(4,261)**	(1,930)	(1,374)	(1,930)	(1,976)
Other income	**1,221**	621	—	—	—
Interest income	**113**	135	134	68	91
Dividend income	**—**	—	29	17	45
Deficit on revaluation of fixed assets	**—**	(1,335)	—	(11,318)	(24,888)
Profit/(loss) from operations	**18,600**	18,972	21,222	7,249	(12,149)
Finance cost	**(3,333)**	(3,767)	(3,346)	(3,767)	(4,294)
Share of loss of associated companies	**—**	—	—	(1)	(416)
Profit/(loss) before taxation	**15,267**	15,205	17,876	3,481	(16,859)
Taxation	**(3,796)**	(3,727)	(3,526)	238	6,914
Profit/(loss) after taxation	**11,471**	11,478	14,350	3,719	(9,945)
Minority interests	**—**	—	—	—	1
Profit/(loss) for the year	**11,471**	11,478	14,350	3,719	(9,944)
Discontinued operations:					
Profit /(loss) for the year from discontinued operations	**624**	1,487	(400)	(951)	(906)
Profit/(loss) for the year	**12,095**	12,965	13,950	2,768	(10,850)