Discussion of Selected Items in the Interim Results

1 Robust Cash Flow and Solid Capital Structure

In light of the Group's increased revenue and its effective cost management efforts, the Group's strong cash flow was maintained. The Group's free cash flow (cash flow from operating activities after deducting tax and capital expenditure paid) for the first six-month period of 2002 was RMB13,994 million. On 1 July 2002, the Company used US$3.15 billion to pay the cash portion of the initial consideration for the acquisition of Anhui Mobile and the rest of the eight mobile telecommunications companies.

As at 30 June 2002, the Group's debt to capitalization ratio (capitalization represents the sum of total debt and shareholders' equity) was approximately 17.3 per cent., which represented a decrease of 3.5 percentage points compared with that at the end of 2001. As at 30 June 2002, total cash and bank balance of the Group was RMB55,868 million, of which 77.7 per cent., 9.6 per cent. and 12.7 per cent. was denominated in RMB, US dollars and Hong Kong dollars, respectively.

At the end of June 2002, short-term and long-term borrowings of the Group totaled RMB27,744 million, representing a decrease of RMB1,556 million over year-end 2001. 58.5 per cent. and 41.5 per cent. of the borrowings were denominated in RMB (mainly represented by RMB denominated bonds, bank loans and finance leases) and US dollars (mainly represented by US dollar fixed rate notes and convertible notes), respectively. 35.6 per cent. of the total borrowings of the Group were made at floating interest rates. The average interest rate of borrowings (ratio of interest expenses to the average balance of borrowings) of the Group was maintained at approximately 4.7 per cent. in the first half of 2002, whereas the interest coverage multiple (ratio of earnings before interest and tax to interest expenses) amounted to 35 times. Net cash position was RMB28,124 million. These indicate an improvement over the results recorded for last year and reflect the Group's long-standing prudent financial risk management policies, as well as its strong cash flow and repayment capabilities. Upon the completion of the acquisition of the eight mobile telecommunication companies in Anhui and the other provinces and municipality, pro-forma combined net debt as at 1 July 2002 was RMB31,477 million. Pro-forma combined debt to capitalization ratio as at 1 July 2002 was 30.1 per cent., which remained at a prudent level.

The Group will continue to pursue prudent financial policies, strictly control financial risks, improve financial management procedures, maintain debts at a prudent level and enhance its capital structure. The Group will endeavour to broaden its revenue sources, reduce expenditures and reinforce and develop favorable economic efficiency, with a view to generating greater returns to our shareholders.

Discussion of Selected Items in the Interim Results (Continued)

2 Capital Expenditure

The Group's planned capital expenditure (as part of a three-year rolling capital expenditure plan) for 2002 is approximately US$4.5 billion, while actual investments made in the first half of 2002 totaled approximately US$1.78 billion.

In order to facilitate further business development and explore new business opportunities, the Group has budgeted total capital expenditure of approximately US$12.4 billion for the period from 2002 through 2004. The capital expenditure is expected to be financed largely out of the Group's internal cash flow generated from operations. The Group will invest the planned capital expenditure primarily in the construction of GSM networks, support systems, transmission facilities and infrastructure buildings and the development of new technologies and new businesses.

3 Personnel Expenses

The Group employed a total of 39,558 employees as of 30 June 2002. Personnel expenses for the period were RMB3,002 million, representing approximately 5 per cent. of operating revenue, which was comparable with that for 2001. Increased incentive compensation to outstanding employees enables the Group to retain and attract talented staff. Concurrently, the Group endeavored to effectively control total personnel expenses and maintain salaries at a level representing a reasonable percentage of operating revenue. In order to align the interests of staff with those of shareholders, share options were granted to employees under the Company's share option scheme. Further details of the share option scheme and the share options granted are set forth in Note 15 of the "Notes on the Unaudited Interim Accounts" and in the section "Other Information — Directors' rights to acquire shares". The Group has also periodically provided training to its staff to encourage continuous learning and self-development, thus ensuring the Group's competitiveness in the ever-changing market environment.