

1 Robust Cash Flow and Solid Capital Structure

As a result of encouraging business growth, aggressive cost controls, effective management of capital expenditures, and given that the implementation of certain capital expenditure plans was deferred in the aftermath of the SARS outbreak, the Group recorded strong free cash flow in the first half of 2003. 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 2003 was RMB25,148 million. As at 30 June 2003, the total cash and bank balances of the Group were RMB57,968 million, of which 92.0 per cent., 5.1 per cent. and 2.9 per cent. were denominated in RMB, US dollars and Hong Kong dollars, respectively. As at 30 June 2003, the Group's debt to capitalization ratio (capitalization represents the sum of total debt and shareholders' equity) was approximately 23.8 per cent., which represented a decrease of 2.2 percentage points from the end of 2002.

At the end of June 2003, short-term and long-term borrowings of the Group totaled RMB57,390 million, representing a decrease of RMB3,590 million over year-end 2002. Of such borrowings, 25.0 per cent. will mature within one year, 14.9 per cent. will mature after one year but within two years, 16.2 per cent. will mature after two years but within five years, and 43.9 per cent. will mature after five years. 54.3 per cent. and 45.7 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, convertible notes and the balance of the deferred consideration for the acquisition of the eight provincial mobile telecommunications companies in 2002), respectively. 60.8 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 approximately 4 per cent. in the first half of 2003, whereas the interest coverage multiple (ratio of profit before interest and tax to interest expenses) amounted to 25 times.

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.

2 Capital Expenditure

The Group's budgeted capital expenditure for 2003 (as part of a three-year rolling capital expenditure plan) is approximately US\$5.6 billion. Due to the SARS outbreak, certain projects scheduled to be implemented in the first half of 2003 were delayed. Actual investments made in the first half of 2003 totaled approximately US\$1.6 billion. Capital expenditure will be financed primarily by cash flow generated from operations.

In order to facilitate further business development and explore new business opportunities, the Group has budgeted total capital expenditure of approximately US\$15 billion for the period from 2003 through 2005. 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 61,859 employees as of 30 June 2003. Personnel expenses for the period were RMB3,900 million, representing 5.1 per cent. of operating revenue, which was comparable with the pro-forma combined figure over the same period last year. 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, the Company adopted a share option scheme to grant share options to employees. Further details of the share option scheme and the share options granted are set forth in Note 17 of the "Notes on the Unaudited Interim Accounts" and in the section "Other Information — Directors', Chief Executive's and Employees' Rights to Acquire Shares" below.